The Treasury

Budget 2016 Information Release

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[1]	to prevent prejudice to the security or defence of New Zealand or the international relations of the government	6(a)
[4]	to prevent prejudice to the maintenance of the law, including the prevention, investigation, and detection of offences, and the right to a fair trial	6(c)
[11]	to damage seriously the economy of New Zealand by disclosing prematurely decisions to change or continue government economic or financial policies relating to the entering into of overseas trade agreements.	6(e)(vi)
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[31]	to maintain the current constitutional conventions protecting collective and individual ministerial responsibility	9(2)(f)(ii)
[33]	to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials	9(2)(f)(iv)
[34]	to maintain the effective conduct of public affairs through the free and frank expression of opinions	9(2)(g)(i)
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[37]	to enable the Crown to carry out commercial activities without disadvantages or prejudice	9(2)(i)
[38]	to enable the Crown to negotiate without disadvantage or prejudice	9(2)(j)
[39]	to prevent the disclosure of official information for improper gain or improper advantage	9(2)(k)
[s18(c)(i)]	that the making available of the information requested would be contrary to the provisions of a specified enactment	
[40]	Not in scope	

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In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) and section 18 of the Official Information Act.

Reference: T2015/2567 SH-13-5-5

Date: 6 November 2015

To: Minister of Finance
(Hon Bill English)

Deadline: 5pm, Monday 9 November
(if any)

Aide Memoire: Business Transformation - Business Case

You are meeting with the Minister of Revenue and officials on Monday 9 November to discuss Inland Revenue's Business Transformation Business Case. Inland Revenue (IR) intends that the final version of this document will be considered by SEC on 18 November and at Cabinet on 23 November.

The business case represents the culmination of nearly three years of planning, and IR has worked extensively with customers, stakeholders, and the Corporate Centre to refine its proposals. Treasury supports the proposal that IR has presented in the business case. This note outlines a number of key points and questions you may want to consider.

1. The updated business case envisages a radically different IR at the conclusion of the Business Transformation Programme

The proposal in the business case includes significant legislative, business process and technology change over a period of seven years. By the end of the programme, the shape, structure, and workforce of IR is proposed to be radically different.

For this reason, the business case focuses on the strategic and economic cases; it has less detail on implementation in later years. The first two to three years of the programme are reasonably certain; there is more room for movement in later years, primarily to account for changes or further advancements in technology, other business priorities, and any responses to the planned policy consultations that IR has proposed. We think this flexibility is important, and we consider that the reporting arrangements that are proposed will provide ample opportunity for Cabinet and Ministers to check in on progress. IR has also proposed to set aside a significant funding contingency to account for changes to assumptions throughout the life of the programme.

2. There are some significant changes between the Programme Business Case presented in 2013 and this proposal

The updated business case shows that IR has responded to several of the questions that were originally posed at the time of initial consideration of the business case in 2013. The main changes include:

- implementing changes to tax and social policy products in a staggered, iterative manner, over a period of seven years, compared to a ten-year timeframe;
- focussing on implementation of a relatively simple tax type (GST) first, compared to what was presented in the original business case (PAYE);
- including a significant contingency ($109m) for the programme, in line with best-practice project and programme management, and;
- including a replacement of their core enterprise resource planning (ERP) technology platform ($120m) in the scope of the programme.

Treasury supports all four of these changes. We have previously advised you that IT projects should be progressed in small, lower-risk pieces. We believe IR's approach to implement changes in a staggered manner, and focus on a reasonably simple tax type first, will allow IR to approach its first stage of implementation with the best chance of success.

3. There are assumptions on costs and benefits that you should be aware of

We have previously reported (T2015/2413 refers) that IR's contribution of funding to BT is heavily dependent on:

- retiring its FIRST legacy system on schedule, and
- realising administrative savings, mainly through reducing its workforce by a third.

Significant optimism bias over costs and benefits appears to be typical among ICT investments across the public sector. IR has since provided us with further information on the costs and benefits associated with the programme. Particular points of note are outlined below.

There will be very limited financial ability to stop transformation once it is commenced

If programme completion is delayed by 12 months, additional costs of $200m-$230m will be incurred. We note that the cost of maintaining FIRST alongside the new core platform (GenTax) accounts for a substantial portion of the total cost of BT (approximately 17%), and consider that a similarly substantial portion of the annual "burn rate" would continue to be incurred if complete transition from FIRST is not achieved. Once begun, it is important that transition between FIRST and GenTax is completed, and as quickly as practicable.

Realising administrative savings will be required for IR to fund the programme and meet its baseline commitments

In calculating benefits arising from administrative savings over the life of the programme, and therefore the level of funding available to reinvest in BT, IR has assumed a 30% reduction in FTEs at the end of the programme. IR has indicated that it would likely require an additional $17m in Crown funding to complete the programme for each percentage point actual FTE reduction is below target. If, for example, IR achieves a 23% reduction in FTEs (75% of target), it will require an additional $130m to complete BT.

The tax revenue forecasts are at the higher end of other jurisdictions' estimates following transformation

IR has estimated cumulative revenue uplift of $2,490m-$5,420m over the length of the programme, based on an annual uplift of $1,500m at its end. This corresponds to a 2.5% increase in real terms; this is at the top end of the range of other jurisdictions' experiences (0.3%-2.8%).

The anticipated reduction in compliance costs is highly sensitive to digital uptake from customers

A large component of the programme's contribution to BPS Result 9 stems from reducing the cost to businesses of complying with tax obligations, particularly for small businesses. Realisation of this benefit is jointly dependent on increased use of digital channels by businesses, and reducing hours of effort to comply through these digital channels. We consider that by leaving use of digital channels as voluntary, rather than selectively mandating it, IR is placing much of its ability to deliver reductions in compliance costs outside of its control. You may wish to further explore BPS Result 9 considerations during your discussions on Monday 9 November.

Cost impacts for other agencies are not fully included in this business case

The cost estimates included in the business case do not include the costs that may arise for other agencies. There are two ways that IR's transformation programme will impact on agencies. These are:

- Where another agency or department is part of the delivery chain associated with a particular tax or social policy service. Specific agencies that we expect to be impacted include ACC, MSD, and Customs.
- As all agencies and departments participate in the PAYE system, there are costs that agencies will need to bear in order to update their payroll systems and software, similar to how businesses will need to adjust their own approach to PAYE.

IR has in place processes to engage with agencies to identify these costs. You may wish to ask the Minister of Revenue how he plans to consult with his Ministerial colleagues on these impacts, and the plan for presenting these costs to Cabinet.

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5. **Finally, Treasury would prefer that the proposal is first considered by the Investment Panel**

BT is a very large investment, with significant capital and operating funding requirements. The size of the investment suggests that the proposal would benefit from being considered in the context of system-level trade-offs and prioritisation. Consideration at the Investment Panel would allow Treasury to provide a better view of how this proposal compares to other proposals that are expected as part of Budget 2016.

Inland Revenue is scheduled to present to the Investment Panel on 24 November. An initial consideration by the panel would mean IR would need to defer consideration of the business case to Cabinet by a fortnight. We consider that this is preferable; you may wish to indicate a preference to the Minister of Revenue.

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