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Briefing note

Reference:	PAS BN2014/88
Date:	28 February 2014
To:	Gary White, Revenue Advisor, Office of the Minister of Finance
cc:	Maraina Hak, Revenue Advisor, Office of the Minister of Revenue IRD/Treasury Officials - as per email distribution list
From:	Chris Gillion, Policy Manager
Subject:	**BUDGET SENSITIVE: Further information on administrative costings for potential changes to Parental Tax Credit**

On Friday 21 February 2014, officials provided a report to the Ministers of Finance, Labour and Revenue outlining a possible package of additional assistance for families with a new born baby, for Budget 2014 (T2013/3191 refers).

The note provides some further information on the administrative costing estimates for implementing the potential changes to the Parental tax Credit (PTC) that were discussed in this paper, namely:

- An increase in the amount of PTC, to pay $225 per week (option A)
- An increase in both the amount and the length of payment time, to pay $225 per week over 10 weeks (option B)

The number of the existing PTC recipients is 15,500 as of March 2012. The increase in the PTC under option A leads to higher payments for 16,500 families. Under option B, the increase of the PTC and the extended payment period will impact 17,000 families will benefit (because the full abatement income threshold is higher).

Summary

The key points to note from this briefing note are:

- The administrative costs have a high contingency attached; because the detailed policy design has not yet been completed, there is a high level of uncertainty, particularly in relation to the IT costs.
- The one-off implementation costs are high largely due to the need to cater for a transition over two tax years, that is, the need to run two PTC rates and/or pay periods concurrently.
- There are options around the communication package deployed, depending on whether a minimalist or a broader strategy is adopted.

Administrative costings breakdown

The high-level indicative costings to implement the proposed PTC changes were approximately $6m, with additional annual on-going costs of $0.5 - $0.7m per annum. These costs break down as follows:

Cost type	Indicative Costs ($m)	Contingency		Total ($m)
		Level (%)	Amount ($m)	
One off implementation costs				
Project management/delivery	1.5	75%	1.1	**2.6**
ICT costs	0.9	100%	0.9	**1.8**
Customer communications	0.9	75%	0.7	**1.6**
Implementation total	**3.3**		**2.7**	**6.0**
Annual on-going costs *(from financial year 2014/15)*				
Additional customer contacts - due to increase in customer base	0.4	75%	0.3	**0.7**

What is included in each cost element of the one-off implementation costs?

The one-off implementation costs are the costs necessary to make the PTC changes to pay out the higher rate and/or over a longer time period.

The implementation costings have been prepared on the basis that the PTC changes will be effective from 1 October 2014, and only apply to eligible families with babies born on or after that date. As noted in the report (T2013/3191), this mid-year change to PTC can only be paid out as an end of year lump sum.

This means the project will be implemented in two overlapping phases between May 2014 and June 2015. The first phase will ensure that, from 1 April 2015 new PTC applicants receive the new PTC amount of $225 in a regular weekly payment. The second phase will create the end-of-year lump-sum payment for parents who qualify and apply for the increased amount between October 2014 and March 2015, and also address the need for a transitional rate to apply over the two tax years (discussed below). These are one-off costs for the year of implementation only.

Project management/delivery *(up to $1.5m exc. contingency, or $2.6m inc. contingency)*

This covers the costs for the implementation project team to design, document and deliver the changes to Inland Revenue's systems and processes; this includes providing the specifications for the IT coders to make the necessary changes to the FIRST system, any on-line calculators and so forth.

The team also develop and update external communications, such as website, forms, publications, letters, notices of entitlement and advertising, and internal communications, including staff training and updates for front-line contact centre scripts and knowledge databases.

The nature and/or complexity of the change determine the project resources and associated costs. The current estimates are based on costs incurred for similar projects in the past.

ICT *(up to $0.9m exc. contingency, or $1.8m inc. contingency)*

This costing covers the work of the developers and coders in making the PTC changes in the IT system, as well as the testing and post-implementation checking referred to above. There are no additional hardware or software costs for these PTC changes.

Interaction with other Working for Families Tax Credits

As noted above, this project will be implemented in two overlapping phases between May 2014 and June 2015. The phase 1 work will be progressed alongside Inland Revenue's Annual Returns cycle which includes Working for Families events, such as changes to payment or abatement rates.

The number of the existing PTC recipients is 15,500 as of March 2012. It is estimated that with the introduction of the PTC change the population may increase. Phase 1 will include testing the IT coding for the new PTC payment to ensure the payments are correctly and accurately calculated and made for these recipients.

PTC is one of the four components of the Working for Families Tax Credits (WfFTC). The total population for entire WfFTC is approximately 602,000. Although PTC is only one element of the WfFTC, each component of the WfFTC payment system needs to be tested to ensure there is no impact to the wider WfFTC recipients, who might be indirectly affected by the changes.

Transition across tax years

One feature of the PTC change is the need to maintain a transitional rate; this adds to the complexity of the IT coding needed.

The issue is that, for a child born just before 1 April 2015 (i.e. late February or early March), the PTC application date is critically important to how their PTC will be paid.

- PTC applications received before 1 April 2015 will be paid under the old rate for 8 weeks crossing over into the next financial year (and then, if a 1 October start date is used, the remainder of their PTC payment will be paid as a lump-sum after the end of the tax year).

- Conversely a child born on the same date may have a PTC application lodged after 1 April 2015, and therefore will be paid at the new rate on a weekly basis.

The system therefore needs to be able to deal with paying out at two PTC rates/periods in the transitional year only, and identify entitlement based on date of application. This transitional issue arises regardless of whether the changes start from 1 October 2014 or 1 April 2015.

Manual process?

Consideration has been given to using a manual process, rather than making IT changes for the transitional period. However this option was discounted for the following reasons:

- PTC cannot be calculated in isolation, as the entitlement and abatement rules cascade through all of the WfFTC.

- System changes will already be in place for the change to the payment rate/period, and the lump-sum end of year square up. Therefore the calculation can be done automatically.

- A manual process as a short-term solution is cumbersome and likely to result in errors. This will impact on the customer and may result in under or over payments, or delays in receipt. It may incur unforeseen long-term administrative costs for IR.

Customer Communications *(up to $0.9m exc. contingency, or $1.6m inc. contingency)*

This estimate covers the actual costs of delivering external communications, includes peak-season advertising (47%), the printing and posting or one-off letters for customers (33%) and insert and flyers (10%), plus costs related to strategy, creative, production and media (10%).

The communication strategy cannot be fully planned at this stage because of unknown factors such as the customer impact, timing of the legislation and phasing of the implementation. For example it is not yet clear if one-off letters will be required in addition to peak season advertising. However, for illustrative purposes we have set out in appendix 1 an outline of three possible levels of communication engagement (low, medium and high). The strategy selected will impact on the costs incurred.

October 2014 versus April 2015 start date

For the IT costing, the resources can be segregated between a 1 October 2014 start date and a 1 April 2015 start date, because specific IT resources are assigned to cater for the backdated entitlements created as a result of a mid-year change. Of the total IT costing of $1.8m, approximately $0.4m is attributable to the October 2015 start-date work, and the remainder to the April 2015 start date work (contingencies applied).

Unlike the IT costings, the project management/project delivery costings do not have a 'segregation' point, so it is difficult to split out which specific resources cater for the 1 October announcement date. As explained above, whichever date is used there is still a need to maintain a transitional rate to deal with payments over the two tax years. The project resources need to be in place from May 2014 to June 2015 to deliver these required system and business changes, and therefore the implementation date does not impact the work effort associated with delivery of these changes.

Likewise with the communications costings; in general the level of communications activity is not dependent on whether the changes occur in October 2014 or April 2015.

What is included in the annual on-going costs?

The additional annual on-going costs of $0.5 - $0.7m per annum (from financial year 2014/15) are largely due to increase in customer base, which creates additional contacts such as telephone calls, forms to process, letters and review correspondence.

Contingencies

As noted in report T2013/3191, standard contingencies were applied to these costings.

Inland Revenue cost all projects based on the best information to hand at the time the costing is done and within the timeframe allocated. Often this timeframe is determined by requests external to Inland Revenue as in this case, given the Budget 2014 timelines. This means that a high level/best estimate approach is used.

To compensate for this IR use a process to arrive at a contingency factor based on an evaluation of the uncertainties and risk involved for the implementation of the project and associated with the high level cost estimate undertaken. This is applied to the base costs to provide a more robust overall cost. As the requirements and implementation dates are refined for the project further, the contingency factor is adjusted and the overall cost may be revised. This approach is recommended by the Treasury for all projects funded by the Crown.

Inland Revenue have applied the contingency tool based on current assumptions about these changes. The risk level for this project is currently **high**; so the recommended level of contingency to be applied is in the range of 50% to 75%. The overall contingency rating selected is based on the uncertainties and risk involved for the implementation of the project, and takes into account several factors, including:

- Customer & Organisational Impact

Detailed design work has not been completed, so we cannot accurately determine the level of change and amount of work the project will need to do to implement the changes. And as noted above, the communication plan is also not fully developed.

- Technology Impact

The business requirements are not robustly designed due to the restricted scoping timeframe. The IT architecture documents and non-functional requirements have not yet been prepared, so the complexity of the solution, including functionality, integration, and IT interfaces are not well defined.

- Planning, resourcing and engagement

The initial, high level costing was provided within a short time frame. The detailed design work to implement the policy has not yet been done.

At this time IR have used a 75% contingency for all non-IT costs, as the detailed design and development work on the proposals has not yet been completed.

A 100% contingency was used for the IT cost because the timing and phasing of the implementation is not certain; there is a high probability that short-term contractors will be brought in to implement the changes

Based on the above approach the deterministic cost of the PTC initiative was estimated to be $3.3m and there is a possibility that the maximum cost of the changes will be up to $6m. However it is also possible that this can be brought down, once we have further information and time to understand the scope and requirements to implement the initiative.

Consultation with Treasury

Treasury was informed about this briefing note.

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Appendix 1: Indicative communications strategies

Low

This would involve low level targeted advertising, to increase awareness about the increase in PTC and who is eligible. This would include online, radio and print advertising.

	Year one	**Year two**
Advertising	$250,000	$180,000
Total	**$250,000**	**$180,000**

Medium

Along with an advertising campaign discussed above, customers would receive a letter and or insert in follow up communications focussing on how they can apply and encouraging online applications. This will focus on encouraging use of digital and online applications.

	Year one	**Year two**
Advertising	$250,000	$180,000
Inserts/flyers/emails	$50,000	$40,000
Total	**$300,000**	**$220,000**

High

In addition to the communications outlined in the 'low and 'medium' options, this would include an additional letter drop to all WfFTC recipients would reinforce the increased payment and time plus echo the efficiency of the online mechanism.

	Year one	**Year two**
Advertising	$330,000	$180,000
Inserts/flyers/emails	$50,000	$40,000
One off letter tbc* (WfFTC)	$300,000	
Total	**$680,000**	**$220,000**