Inland Revenue
Te Tari Taake

Inland Revenue report: Transformation status update: October 2019

Date:	08 November 2019	**Priority:**	Medium
Security level:	In confidence	**Report number:**	IR2019/509

Action sought

	Action sought	Deadline
Minister of Finance	**Note** the contents of this report	None
Minister of Revenue	**Note** the contents of this report	None

Contact for telephone discussion (if required)

Name	Position	Telephone
Greg James	Deputy Commissioner, Transformation	Withheld under s18(c)(i) of the OIA

08 November 2019

Minister of Finance
Minister of Revenue

Transformation status update: October 2019

Executive summary

1. This report summarises the progress and highlights of transformation for October 2019.

2. Release 4 remains on track. Solution design is 99% complete and we expect to remain at this level for some time as issues are identified during testing. We remain slightly behind schedule with testing, which is not a cause for concern. We successfully passed checkpoint 1 in the readiness assessment framework during the month.

3. A lot of work is underway to ensure customers are on the right rates for their employment and investment income. This will help the automatic assessment process to run more smoothly next year and should mean refunds or bills to pay are smaller.

4. As receiving employment income information more regularly is a key enabler, we have begun applying the late filing penalty of $250 to employers who are not providing employment income information every payday. We expect around 10,000 employers to be affected. This compares with between 5,000 to 6,000 employers a month who received late filing penalties before 1 April 2019 for filing their employer monthly schedule late, as we can now identify late filing more effectively. Our community compliance team will shortly begin visiting approximately 1,000 employers who are not filing on time.

5. We are seeing some early signs of significant shifts in customer behaviour. More and more customers are interacting with us digitally. We received no mail at our Upper Hutt processing centre on one day for the first time ever during the month. As at 31 October 2019, 0.02% of the payments made from START were cheques, representing less than 0.01% of the value of payments made. There were five days during the month when no cheques were issued for products administered in START.

6. Scoping and planning for Release 5 are progressing well. Detailed planning is underway for the third release in Ātea; replacing the internal systems and processes that support the day-to-day running of Inland Revenue.

7. Transformation's Red, Amber, Green (RAG) status remains at light amber overall this month (as shown in table 1 below). There has been no change in the status of any of the ten reporting keys.

Table 1: Transformation's RAG status

	Overall	Scope	Risk	Issues	Inter-dependencies	Schedule	Resource	Stakeholder Engagement	Delivery Partners	Financials	Benefits
CURRENT	Light Amber	Light Green	Light Amber	Light Amber	Light Green	Light Amber	Light Amber	Light Green	Light Green	Green	Light Amber
PREVIOUS	Light Amber	Light Green	Light Amber	Light Amber	Light Green	Light Amber	Light Amber	Light Green	Light Green	Green	Light Amber

8. The overall budget (excluding the contingency held by the Commissioner) for the transformation programme, from 1 July 2019 until 30 June 2020, is $221.7 million for operating expenditure and $90 million for capital expenditure.

9. Based on current forecasts, we expect to complete delivery within budget (including contingency) for operating and capital expenditure. The remaining contingency available for the period to 30 June 2020 is $6.7 million for operating expenditure and $7.8 million for capital expenditure.

10. There is significant complexity in the remaining releases and our risk profile remains high. Examples of activities with risks include decommissioning and support for customers and our people after go-live of Releases 4 and 5. Based on the latest available estimate from earlier in the year, to address such risks we hold contingencies of $102 million in operating expenditure (excluding depreciation and capital charges) and $148 million in capital expenditure. These are point in time estimates. We regularly update our cost estimates and remaining contingency funding and will be reviewing these again soon. The contingency we hold is the difference between the available funding and the latest estimated cost to complete transformation. As our remaining cost estimate varies over time, so will the available contingency amount. This is separate to the contingency funding held by you that we handed back as part of the October Baseline Update.

11. In response to the Minister of Revenue's comment on the Transformation status update for September 2019 (IR2019/440 refers), we were over budget on operating expenditure due largely to the timing of staff exit payments (redundancy payments) related to planned changes within our information technology team. The costs are within the overall budget for transformation for the year and we incurred some payments earlier due to voluntary redundancies. The business transformation programme holds the budget for any exit payments related to implementing our future operating model.

Recommended action

12. I recommend that you **note** the contents of this report.

Noted

Noted

Greg James
Deputy Commissioner, Transformation
08 November 2019

Hon Grant Robertson
Minister of Finance
/ /2019

Hon Stuart Nash
Minister of Revenue
/ /2019

Key risks and issues

13. The transformation programme's risk profile remains light amber with a future trend of light amber. A light amber profile means that appropriate mitigations are in progress and are expected to be successful. There is no expected impact on key dates.

14. No new issues (risks that have been realised) were reported to the Portfolio Governance Committee (PGC) during the month. The issue reported to the PGC last month relating to the platform we use to deliver webinars to tax agents and employers has been resolved. However, a risk has been raised and is being managed at programme level until we successfully run a webinar. Mitigations are in place to manage any remaining risk.

15. The issue reported to the PGC in August 2019 (IR2019/371 refers), relating to slow network performance for some of our as-a-service internal applications has also been resolved. Changes have been made to improve response times and any residual risk is being managed as part of an existing risk at programme level.

16. As at October 2019, the programme had a total of 58 open risks[1], of which 13 are reported to the PGC.

17. There was no change in the status of any of the risks reported to the PGC during the month.

18. In response to the Minister of Revenue's comment on the Transformation status update for September 2019 (IR2019/440 refers), the consequences of the risk relating to Release 4 implementation and key business events[2] all occurring during the period April to July 2020 and not being co-ordinated properly are:

- we would be unable to manage customer demand and/or implement fixes at the pace required
- our reputation would be damaged if one or more of these key events failed.

19. Also, in response to the Minister of Revenue's comments on the September status update (IR2019/440 refers), the factors we believe will significantly influence people's decisions to remain with the programme are:

- continuing to have opportunities to develop new skills and capabilities
- doing fast-paced, exciting and rewarding work on a once-in-a generation change
- feeling they are contributing to making a difference for New Zealanders.

20. The factors that may influence people to leave the programme and result in this risk being realised are:

- other development opportunities within Inland Revenue becoming available, particularly as we progress the design of our future organisation
- employment opportunities outside Inland Revenue, particularly across the state sector, as other agencies embark on their own transformation programmes.

[1] The number of open programme risks has increased by three; three new risks were opened during the month and all are managed at programme level.
[2] Key business events include the second round of automatic assessments and some first-time events such as the rollover of Working for Families in START (this is when entitlements for the following year are estimated and communicated to customers).

21. The top risks for transformation are support for heritage systems ending in 2021, the timing of benefit realisation, and Release 4 and key business events occurring concurrently during April to July 2020. Mitigations are in place for all these risks.

Release 4

22. Release 4 remains on track for April 2020, and continued focus is required to ensure the release remains on schedule.

Some components of Release 4 have been implemented

23. The short process rulings service came into effect on 1 October 2019 as planned and we have had two applications to date.

24. The Minister of Revenue is receiving a weekly status update regarding the implementation of the research and development tax incentive (IR2019/605 / CI B-19-033 and IR2019/625 / CI B-19-034 refer).

25. The Memorandum of Understanding between Inland Revenue and Callaghan Innovation, regarding how the core team administering the research and development tax incentive will operate, was agreed by both agencies on 15 October 2019 and signed by the Commissioner on 21 October 2019.

26. The second release of functionality for the research and development tax incentive to a selected group of customers was implemented on 30 October 2019 including:

- a supplementary return for the 2019/20 tax year onwards
- the START version of the eligibility tool
- general (in-year) activity approval and significant performer elections.

27. We will use the pilot to further refine the customer experience and progressively allow customers to file.

28. In response to the Minister of Revenue's comment on the Transformation status update for September 2019 (IR2019/440 refers), we did not estimate how many customers would have been part of piloting this functionality. Overall, we estimate that less than 10 customers would have been affected if the functionality had been delayed. Most customers (who are on a standard balance date) will use this functionality from April 2020.

Solution design and testing

29. Design is continuing as new design requirements are uncovered during testing as expected. As at the end of October 2019, solution design was 99% complete. Assuming we follow the same pattern as Release 3, we are likely to stay at this level for some time. Solution development is on schedule.

30. Writing test scenarios for business system testing (ensuring START works as expected) is slightly behind plan, as is test execution. This reflects the amount of work required to be done between now and the second readiness checkpoint on 12 December 2019. Mitigations include additional resourcing, overtime and reviewing the schedule. There is no cause for concern and testing is on track for go-live in April 2020. As at 1 November 2019, we had completed approximately 54,000 scenarios and tested approximately 33,000 of them.

Readiness checkpoint 1

31. On 24 October 2019, we successfully passed checkpoint 1 in the readiness assessment framework. This checkpoint includes assessing whether solution design and build and testing are progressing to schedule, that preparations for readying customers and our people for change are underway, and that cut-over and contingency planning are on track.

Benefits of Release 4

32. On 30 October 2019, our Performance & Investment Committee approved the expected administrative savings resulting from reduced work effort in our transactional and interactional work. Savings are forecast to be modest this year, with more significant savings expected from the 2020/21 year.

Other updates

Enterprise support services/ Ātea

(Internal processes and systems that support the day-to-day running of Inland Revenue)

33. In response to the Minister of Revenue’s comment on the Transformation status update for September 2019 (IR2019/440 refers), we have not changed our payment terms as part of the transformation of our back-office processes. We have configured Ātea based on best practice business processes and workflows. This means it will be easier for our suppliers to transact with us and to be paid promptly once goods or services have been delivered.

34. In the 2018/19 financial year we paid 72% of domestic invoices within 10 days. With the implementation of our new system and processes we expect to be able to pay all of our suppliers within 10 working days. We will be monitoring the time it takes to pay our suppliers as we embed our new processes and our Ātea toolset.

35. On 24 October 2019, the Portfolio Governance Committee agreed to begin detailed planning for the third release of Ātea. This release will complete the move of our finance and human resources functions and move our performance management functions to new systems and processes. This release will also include e-Invoicing. We expect to complete detailed planning by the end of November 2019.

36. Planning for the fourth and final release of Ātea is expected to be completed early in 2020. This release includes our payroll, contract management, risk management and health and safety functions.

Helping customers to pay and receive the right amounts

37. Since August 2019, we have been notifying customers on the wrong prescribed investor rate, letting them know what rate they should be using, and recommending they contact their scheme provider to update it. By the end of November, we expect to have notified approximately 960,000 customers.

38. There are a further approximately 250,000 people who were on the wrong prescribed investor rate for the 2017/18 tax year that we will notify once they have filed their 2018/19 income tax returns. Until they file their 2018/19 return, we will not be able to determine what rate they should be using.

39. This is in addition to the approximately 444,000 people on the wrong prescribed investor rate we contacted as part of the 2019 automatic income tax assessments.

40. Since 24 September 2019, we have been contacting customers we have identified are using an incorrect tax code. We estimate there are around 200,000 people using an incorrect tax code, working for around 30,000 employers. We are sending employers with multiple employees on an incorrect tax code one letter with all of the changes that need to be made.

41. We have prioritised contacting customers this has the largest impact on. To prepare customers we have posted messages on social media, updated our website, contacted large employers and intermediaries to give them a heads-up, and put messages on our phone.

42. During October 2019, we began writing to customers using a tax code that is not optimal. For example, a customer using the correct secondary tax code but their secondary income spans tax brackets resulting in too much tax being deducted. We are recommending these customers apply for a tailored tax code. Once we have calculated the tailored tax code, we will notify both the customer and their employer. Customers apply for a tailored tax code through myIR.

43. We can identify people using the wrong tax code or using a sub-optimal tax code because we are receiving employment income information more regularly. Most employers are meeting their payday filing obligations. A small minority are not.

44. In mid-October 2019, we began applying late filing penalties to employers who had not met their payday filing obligations for the third time. These employers had received two previous warnings. The late filing penalty is $250, and we expect around 10,000 employers to be affected.

45. This compares with between 5,000 to 6,000 employers a month who received late filing penalties before 1 April 2019 for filing their employer monthly schedule late. We have been able to identify late filing more effectively following the introduction of payday filing, as FIRST had some limitations. As employers now generally need to file more often, they could be late more often.

46. In mid-November 2019, our community compliance team will begin visiting approximately 1,000 employers who are not filing their employment income information on time and who also have other issues, for example missing information. In addition, our letters and emails to employers encourage them to let us know if they do not need to file for a number of months so that we can reset indicators and reverse penalties if needed.

47. We are beginning to receive investment income information more regularly. One of the seven biggest payers of investment income is in the process of moving to the new reporting requirements. We expect this payer to move to the new requirements during December 2019. The seven biggest payers account for around 70% of the market. Approximately half a dozen smaller payers have already opted in.

48. From 16 October 2019, we began proactively contacting approximately 76,000 Working for Families customers who we estimate may receive more than they are entitled to for the year, based on the information we hold. We do this every year to ensure customers receive the right payments and do not have a debt to repay at the end of the year. This can mean payments decrease or stop entirely for the rest of the year if customers have already received their annual entitlement. In the future, we will identify customers in this situation weekly so we can resolve any issues earlier.

49. All of this proactive activity has resulted in a high number of customers contacting us. This has put pressure on our contact centres. During some days in October we were unable to accept all calls.

50. Working with customers where we see things that aren't right and enforcing reporting requirements for employment and investment income will help to ensure that people pay

and receive about the right amounts during the year. Over time, this will reduce the value of refunds or bills to pay at the end of the year and help to reduce the number of customers who contact us.

51. Tax agents have also contacted us about letters that were going directly to their clients. Clients were receiving letters that previously were sent to their tax agent which is has caused confusion amongst their clients.

52. We have already fixed 8 letters that were going to clients incorrectly. We are working on fixing the redirection for the Statement of Account. This complicated build is underway so will take some time to deliver. We are also undertaking a full review of all letters.

53. Some letters will always go to customers. For example, bank account changes and the second notification of an outstanding amount (the first notification goes to the tax agent).

New analytical capabilities

54. Our new analytical capabilities are also helping to ensure people pay and receive the right amounts. For example, an upfront review of donation tax credit claims together with new systems and processes, has resulted in an increased number of claims being denied. As at 30 September 2019, approximately $21 million of the donation tax credits claimed so far this year have been denied. The total amount denied for the full tax year ended 31 March 2019 was approximately $7 million.

Changes in customer behaviour

55. We are seeing early signs of some quite significant shifts in customer behaviour that will help, in time, to reduce customer contacts. On 8 October 2019, for the first time ever our Upper Hutt processing centre received no mail. We checked that this was not a delivery issue for NZ Post, and it wasn't, there was simply no mail as more and more of our customers choose to use digital services.

56. On 11 October 2019, for the first time since we switched START on, we did not issue any cheques for any of the products in START. In total, there were five days during October when we did not issue any cheques from START. As at 31 October 2019, we had issued 45 cheques in total for the month, with a total value of approximately $69,000. In comparison, we had made around 211,000 direct credits with a total value of approximately $1.5 billion.

Testing new website content with customers

57. GST test content went live on our new website on 17 October 2019. It will be available for around 4-6 weeks for customers and our own people to provide feedback on. We are progressively moving all our content over from our old website. Our next areas of focus are property and Research and Development (R&D).

Independent quality assurance reviews

58. We have recently reported the results of the October 2019 Gateway review to you (IR2019/507 refers).

59. On 24 October 2019, KPMG briefed the Portfolio Governance Committee on the findings of their tenth independent quality assurance review and ninth technical quality assurance review (IQA10/TQA9). Fieldwork took place between 16 and 30 September 2019. We will report the results to you once KPMG have finalised the report.

60. As previously reported (IR2019/203 refers), the Office of the Auditor General (OAG) has been undertaking a performance audit of benefits management for transformation. The OAG team have now completed their fieldwork. To date, no substantive issues have

been highlighted. We expect to receive the OAG's draft report before Christmas and will brief you once this is available.

Lessons learned from Pou Whirinaki

61. In response to the Minister of Revenue's comment on the Transformation status update for September 2019 (IR2019/440 refers), broadening the people participating in assessing the backlog of issues will not involve more front-line staff being out of their business-as-usual roles. It is people in support roles, with the necessary technical expertise, who are now being involved in considering the materiality and impact of items in the backlog.

Release 5

62. Scoping and planning are progressing well. Product Owners have been appointed for Child Support, Unclaimed Monies and Paid Parental Leave, business profiles are being finalised, and the START team have been progressing product working sessions.

63. Deliverables have been agreed for the release. The base timeline will follow a similar path to prior releases and deployment dates, subject to detailed deployment planning. We have begun a business impact assessment so that we are able to start preparing our people and customers for the changes well ahead of the release.

64. There is a significant amount of discovery and analysis work underway to confirm the approach to fully decommissioning FIRST and all its satellite connections. We are also working with Unisys to identify all the contents of our heritage data centres so we can develop a comprehensive plan before the end of 2019.

65. Key risks, including decommissioning and scope risks, are being carefully monitored as this is the final release.

Coming up in the next two months

66. Key activities over the next two months include:

November 2019

- Cabinet considers the November 2019 Transformation Update.
- Trial run of scaled business simulation (practicing go-live step by step) testing.
- Workshop with unions.

December 2019

- Checkpoint 2 for Release 4 in the readiness assessment framework.
- Mock go-live testing begins.