

In Confidence

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Office of the Minister of Revenue

Chair, Cabinet Government Administration and Expenditure Review Committee

Inland Revenue's July 2020 Transformation Update

Proposal

- 1 This paper provides an update regarding Inland Revenue's progress in modernising the revenue system. I am asking Cabinet to note the progress made to date and the impact of COVID-19 on Inland Revenue's capacity and on its plans for completing the transformation programme.

Executive Summary

- 2 Inland Revenue has chalked up some significant achievements in recent months. Release 4 of its transformation successfully went live on 16 April 2020, moving KiwiSaver and student loans to new systems and processes, and the department has played a key role in supporting our responses to COVID-19. Inland Revenue has achieved this while supporting customers, organising its people to work remotely and preparing for the peak tax season, including this year's automatic income tax assessments.
- 3 Going live in the middle of a pandemic was a difficult but necessary call to make. Not going live would have delayed making new services available to customers which make it easier for them to get the help they need and better ensure their payment obligations reflect their current income.
- 4 The majority of the go-live process was completed remotely, an undertaking made possible by the investment in transformation. The capabilities delivered by transformation have also underpinned our responses to COVID-19. Inland Revenue has supported the Ministry of Social Development to deliver the wage subsidy, implemented business tax changes to free up cashflow, and implemented the Small Business Cashflow (loan) Scheme. New systems and processes were able to be extended to accommodate these initiatives as the requirements were clear and simple and leveraged the out-of-the-box functionality of the core system.
- 5 To deliver all of this, Inland Revenue has had to make choices about where it focuses its efforts. It is clear that the system constraints of the past are now much reduced. However, Inland Revenue's ability to support customers is currently stretched to capacity. The department is providing a heightened level of support until the end of July 2020 to its customers and people following the Release 4 changes, supporting customers as they face challenging financial circumstances, and continuing to provide a wide range of services to customers every day.
- 6 In light of COVID-19, Inland Revenue is now re-planning the final changes of transformation, the work to close the programme, and the move to its new operating model. It is too early to say what the implications for the timeframes, costs and benefits of

the transformation programme will be. My working assumption is that Inland Revenue will complete transformation within the existing funding envelope approved in 2015 by government. Inland Revenue will keep the Minister of Finance and me fully informed as it thinking develops and will report back to Cabinet in November 2020.

- 7 Inland Revenue will continue to play a key role in our responses to COVID-19. It will be important for us to keep in mind Inland Revenue's capacity in the design of further COVID-19 response packages. We may need to consider trade-offs in the role the department plays, how Inland Revenue is best able to contribute, and when.

Release 4 has successfully gone live

- 8 Inland Revenue successfully implemented Release 4 of its transformation programme on 16 April 2020. This release moved KiwiSaver, Student Loans and the end-to-end processing of PAYE to new systems and processes. Enhancements were also made to digital services, income tax and Working for Families. More frequent and more detailed reporting of investment income information became mandatory from 1 April 2020. The changes made give New Zealanders more information and options as they manage through this difficult period.
- 9 New services are now available which make it easier for people to get the help they need and better ensure their payment obligations reflect their current income. All customers who are experiencing financial difficulties can apply for relief through a simple, new myIR¹ service. Employers can set up instalment arrangements themselves online for any debt they owe. Student loan borrowers who are struggling to make repayments can now apply for a special deduction rate online. Previously, customers had to ring or write to Inland Revenue to access these services. What took a number of days can now be done with a few clicks.
- 10 Going live as planned was not an easy call to make as the decision had to be made when New Zealand was barely a week into the Alert Level 4 lockdown. However, it was clearly the right decision. Inland Revenue considered a range of alternative dates, recognising that the risks of any future date were unknown. Before deciding to proceed as planned, Inland Revenue consulted a range of stakeholders, including tax professional bodies and KiwiSaver scheme providers. Not making the changes would have meant delaying benefits to customers and made it more difficult for Inland Revenue to help support our response to COVID-19.
- 11 The vast majority of the go-live process was completed remotely for the first time. This is a significant achievement and only made possible by the investment in transformation.
- 12 Inland Revenue has upgraded its workplace technology as part of transformation to ensure that it can continue to provide services in the event of disruption. This has enabled approximately 4,000 of its people to work remotely in response to COVID-19. Together with very good practices around how Inland Revenue manages each release and readies customers and its people for change, this made a very quick pivot to a remote cutover possible.
- 13 During the weekend of 9 to 15 April 2020 when Release 4 products were being moved to new systems and processes, there was a maximum of 8 people on site at Inland Revenue's offices at any one time, compared to a peak of approximately 100 people for

¹ Inland Revenue's secure online services

previous releases. Approximately 270 people worked on Release 4 cutover remotely, compared to less than 10 people for Release 3 in April 2019.

- 14 The benefits of the changes made in Release 4 are already evident. New processes are far more efficient, meaning customers' accounts are far more up-to-date and accurate. This is particularly important in the current environment and will help support the recovery from COVID-19.
- 15 For example, since go-live Inland Revenue has been able to transfer contributions to KiwiSaver scheme providers far more quickly. In the weeks immediately after go-live, around three-quarters of members' contributions were transferred to scheme providers within 3 to 7 working days and 99% were transferred within 14 days. Previously, it would take Inland Revenue, on average, 20 to 23 working days to transfer contributions. As at 8 June 2020, Inland Revenue had passed 27 million messages worth \$1.7 billion to scheme providers since go-live on 26 April 2020. This compares with the previous peak in August 2019 of 7.9 million messages worth \$785 million. New Zealanders now have their contributions invested far more quickly which, over time, should have a beneficial impact on their retirement savings.
- 16 Similarly, there have been significant improvements in the administration of student loans. Closing a loan is now an overnight process with nearly all loans automatically ceased when they are paid off. Previously it took up to 42 days due to the amount of manual work involved. During this period customers often continued to have deductions made from their salary and wages. As at 4 June 2020, since go-live around 24,000 borrowers have been advised that their loans have been paid off, with \$5 million refunded to them.
- 17 Release 4 builds on previous releases and is further helping to ensure that people make and receive the right payments. The automatically issued income tax assessment process for 2020 began on 18 May 2020. The process will run more smoothly this year as a result of Release 4 go-live. Inland Revenue has made some enhancements to the process to ensure refunds get to people as quickly as possible, including running the process over a shorter time period. As at 8 June 2020, approximately 1.1 million New Zealanders had automatically been issued with their tax refunds totalling \$571 million. Some 160,000 have received a bill and have until 7 February 2021 to pay it. The threshold for writing off debt was increased from \$50 to \$200 this year. This means fewer people will have bills to pay and fewer will call Inland Revenue.
- 18 Inland Revenue is now in the early life support period for Release 4, where a heightened level of support is available to customers and its people. As with any release, Inland Revenue has found that some things have not worked quite as expected and has made changes as a result. The level of changes being made is far lower than for previous releases. Customer reaction has largely been muted, which is unsurprising given the circumstances, and while some are taking time to get used to new ways of doing things, others say they are finding the changes easy to work with.

These represent the latest in a series of significant changes since 2017 to the way Inland Revenue operates

- 19 Customers are spending less time and effort ensuring they meet their obligations and receive their correct social policy entitlements. Tax is being more correctly withheld and entitlements more accurately calculated during the year. We now have greater agility to make policy changes and to better use the information Inland Revenue holds to deliver improved outcomes for New Zealanders. Inland Revenue itself is now far more resilient,

as has been amply demonstrated by the department's response to COVID-19. These outcomes have been achieved through a combination of changes to policy, process, technology and Inland Revenue's operating model.

- 20 Customers now have online services for all tax products, Working for Families, KiwiSaver and student loans. They can do far more for themselves including filing returns, keeping track of their payments, and making payments. Inland Revenue is using the employment and investment income information it receives more frequently to pre-populate individual customers' online accounts. This gives people greater visibility of what they have paid and what they owe and means that payments should be more accurate during the year.
- 21 Employers now have a single account with all their information in one place in myIR. They can see what they have paid and what they need to do in a single place. A survey completed in the first week after go-live found that 60% of employers were finding it easier to file.
- 22 The year ended 31 March 2020 was the first full year that Inland Revenue received employment income information every payday. It is also the first year Inland Revenue has received information about recipients of investment income more often from payers who chose to provide it. This became mandatory for payers of investment income from 1 April 2020. This more detailed and timely data means Inland Revenue can proactively contact customers during the year to ensure they are paying and receiving the right amounts. For example, once it became clear last year that a significant number of people were on an incorrect prescribed investor rate (PIR), Inland Revenue proactively contacted them about correcting their PIR. Of the approximately 140,000 customers who have had their automatic assessment so far this year, approximately 90,000 have had a more favourable outcome compared to last year as a result. Whereas they had a bill to pay last year, this year 68,000 have received a refund and 22,000 have had a small bill written off.
- 23 Third parties are now a much more integral part of the revenue system. Throughout transformation Inland Revenue has worked with those who advise and provide services to customers to ensure revenue processes fit seamlessly into normal business processes. Inland Revenue has recently established a tax agent cohort, which includes members from each of the big four firms, representative bodies, and agents based in the regions. It is proving to be a very valuable way for Inland Revenue to understand customer sentiment as the members represent a diverse range of customers across the country.
- 24 New analytical capabilities are shaping how Inland Revenue supports customers to pay and receive the right amounts across a range of areas. For example, understanding the impacts of COVID-19 on customers and the emerging trends in behaviours to inform what steps to take to support the best outcome for the customer. Text analytics are analysing notes in START² and myIR to determine why customers are calling and to identify those who might need some proactive support.
- 25 Changes to Inland Revenue's operating model and the implementation of Ātea³ are enabling the department to work more efficiently and productively. In recent months, Inland Revenue has achieved the target of paying 95% of domestic suppliers within 10 working days. The e-invoicing capability delivered as part of Ātea will enable Inland Revenue to increase this level of performance further, although the speed at which the

² START stands for simplified tax and revenue technology and is the name chosen by Inland Revenue for the GenTax software provided by FAST Enterprises LLC

³ Ātea is the name Inland Revenue has chosen for its new enterprise support services platform. Enterprise support services are the internal systems and processes that support the day-to-day running of Inland Revenue.

department will be able to proceed will also be dependent on the take up of e invoicing by businesses. The next release in Ātea is due to go-live at the end of July 2020. This is likely to be implemented remotely, further demonstrating the benefits of transformation.

The capabilities delivered by transformation have been key to supporting our response to COVID-19

- 26 Inland Revenue has played a significant role in delivering our response to COVID-19. The initiatives implemented have leveraged the capabilities delivered by transformation.
- 27 Having more up-to-date employment income information has enabled Inland Revenue to effectively support the Ministry of Social Development (MSD) in delivering the wage subsidy. Information about self-employed individuals, employers and employees was shared with MSD which enabled many applications to be automatically approved. Many however needed further clarification and a direct 0800 number was established for MSD staff to connect directly with Inland Revenue. As at 8 June 2020, Inland Revenue's people had answered more than 353,000 calls from MSD.
- 28 Business tax changes to free up cashflow, including a provisional tax threshold lift, the reinstatement of building depreciation and writing off interest on the late payment of tax have been implemented, as has a loss carry-back scheme. As at 8 June 2020, around 1,700 customers had received refunds through the scheme totalling \$8.5 million. Inland Revenue's new analytical capabilities are playing a role in the administration of the scheme by identifying areas of customer confusion and errors, both deliberate and inadvertent. Changes to loss continuity rules will be consulted on later in the year and applied retrospectively for the 2020/21.
- 29 Most recently, Inland Revenue was able to quickly implement the Small Business Cashflow (loan) Scheme. The payment and collection functionality already built within START was extended to accommodate this initiative as the requirements were clear and simple and leveraged the out-of-the-box functionality of the core system. This enabled Inland Revenue to implement the Scheme in a matter of weeks. As at 8 June 2020, Inland Revenue had received more than 77,000 applications and approved loans worth approximately \$1.2 billion.
- 30 Supporting our response to COVID-19 coincided with the implementation of Release 4, and when Inland Revenue was organising its people to work remotely and preparing for the peak tax season, including this year's automatic income tax assessments. I believe that Inland Revenue would not have been able to respond so effectively even as recently as two or three years ago.
- 31 It is clear that, as a result of the investment made in transformation, as a government we now have greater flexibility and agility to make changes. We will need to use this flexibility wisely.
- 32 Prior to transformation, Inland Revenue's heritage systems and processes were the greatest constraint on agility. They were complex, time-consuming and expensive to change. There were other constraints on the department, such as being unable to respond to customer demand at peak times, however these were not as significant as the constraints imposed by FIRST.⁴

⁴ FIRST is Inland Revenue's old core technology platform and is being replaced by START.

- 33 System constraints are no longer the issue, provided exceptions are minimised, requirements are clear and a good fit with Inland Revenue's capabilities, and data sources are well understood. This is a huge change as the answer to "can the system do this" is now almost always yes, rather than no.
- 34 The constraint now is Inland Revenue's ability to support customers. Meeting customer demand has always been a challenge for Inland Revenue and this is particularly true in a COVID-19 world. While the investment in workplace technology and the move to broad-based roles are enabling Inland Revenue to be more agile, there are limits to what can be achieved.
- 35 Inland Revenue estimates the productivity of its people had reduced by up to 25% as some people do not have the technology to enable them to work remotely, some have sub-optimal home set ups, and some have reduced availability due to childcare needs. This situation improved under Alert Level 2, with productivity significantly restored by the end of May 2020. Inland Revenue is working through how best to support its customers and its people during the respond, recover and rebuild phases.
- 36 It is clear that the improved agility to make changes provided by new systems and processes is currently out-pacing Inland Revenue's organisational agility and capacity. This is something we will need to bear in mind in the design of further COVID-19 response packages. Inland Revenue is key to supporting our response, however we may need to consider trade-offs in the role the department plays, how Inland Revenue is best able to contribute, and when.

Inland Revenue is also making other changes to better support New Zealanders at this time

- 37 Inland Revenue's priorities are supporting customers, supporting our response to COVID-19, and continuing to support Release 4. There is a way to go before Inland Revenue can confidently say Release 4 has been bedded in. The early life support period is scheduled to run until 31 July 2020.
- 38 In dealing with customers as they respond to and recover from COVID-19, Inland Revenue is taking, and will continue to take, a highly supportive and empathetic approach. The focus is on helping customers through this period and working with them to find the best way to manage their obligations. There is now a great deal of flexibility available to Inland Revenue in dealing with customers who have been affected by COVID-19, such as extending dates or time periods and varying requirements. By working with customers to get the best outcome, Inland Revenue is helping to minimise the impacts of the disruption, minimise additional stress, and support businesses to remain operating where possible.
- 39 This has required some trade-offs to be made to maintain services and support customers. During the respond phase, with limited exceptions, no new audit or debt collection cases will be opened and existing disputes will be managed as judiciously as possible. Inland Revenue's specialists in these areas are supporting COVID-19 activities and other priority work for around 50-70% of their time. The balance of their time is on case work in progress, reviewing disbursements, customer-initiated work such as voluntary disclosures, rulings, and annual risk reviews for the largest businesses.
- 40 This balance will change as the economy recovers from COVID-19. Inland Revenue will adjust its resourcing, including the amount of time its specialists spend on particular activities, to reflect the needs of the recovery and rebuild phases.

- 41 In exceptional cases, Inland Revenue will still pursue enforcement activity. I expect these to be very isolated cases and for action to be taken only where there is a clear and material risk to the integrity of the revenue system.
- 42 Inland Revenue will not achieve some of its performance measures this year in light of COVID-19, given the necessary and sensible decisions the department has made about where to focus its resources. The department's performance frameworks may need updating to reflect its greater agility and the impact that circumstances can have, such as COVID-19, that sometimes require difficult trade-offs to be made.

The final stage of the transformation programme is being re-planned

- 43 The end of transformation is now in sight. Implementation began with Stage 1 in February 2017 and has included the progressive migration of products to new systems and processes, wide-ranging changes to policy and legislative settings including the biggest change in a generation for individuals, and changes to the way Inland Revenue works, along with new tools and technology.
- 44 Following Stage 1, Inland Revenue moved to implementing changes in a series of releases to reduce risk and to minimise impacts on customers. The programme will conclude as planned, with a final stage, Stage 4.
- 45 The majority of the products Inland Revenue administers are now running on new systems and processes. The exceptions are Child Support, paid parental leave, and some minor products. This group of products is part of the final stage, along with the decommissioning of heritage systems and processes, completing the implementation of Ātea, and completing the implementation of new analytics and intelligence capabilities.
- 46 Inland Revenue will continue to work differently, with many of its people, including those working on transformation, continuing to work remotely currently. As the Minister of Finance and I refresh the tax policy work programme in light of COVID-19 and as thinking develops on the next wave of response and rebuild, Inland Revenue may well need to use some of its design and delivery teams to further support new policy responses. Therefore, it is necessary and sensible for Inland Revenue to re-plan the work remaining to complete transformation.
- 47 Given the impacts of COVID-19 on Inland Revenue, officials advise me that it is no longer possible to complete the final stage as a single major release in April 2021 as planned. Inland Revenue's commitment to completing transformation as quickly as possible to provide customers and government with as much flexibility as possible and to reduce risk is unchanged. What will change is the approach to the final stage. It is likely that products will be progressively moved to new systems and processes in a series of smaller changes over a longer period, rather than as a single, large block of change.
- 48 Some of the smaller products, for example unclaimed monies,⁵ can be implemented largely by the programme without having much impact on the wider business. However, child support will only be successful with the involvement of experts from across Inland Revenue. Child support implementations are notoriously difficult as they affect a

⁵ Unclaimed money is money held by a person or organisation, such as a solicitor or a Bank, where the owner of that money (or someone with authority to act on behalf of the owner) cannot be found. In general, money is classed as unclaimed after a certain length of time has passed since the person or organisation holding the money has been able to contact the owner. The length of time depends on the type of money. For the most part, unclaimed money is eventually transferred to the Crown, usually to the Treasury or the Inland Revenue Department, or the Public Trust.

vulnerable customer group with complicated personal circumstances. Inland Revenue deals with approximately 164,000 parents who pay child support. It is important for Inland Revenue to take the time to get this right, particularly given current circumstances.

- 49 While Inland Revenue has demonstrated it can move products to new systems and processes remotely, the design and build phases for the core system have not been conducted remotely before. Typically, design and build require significant collaboration and this may not be as efficient and effective while the majority of Inland Revenue's people are working remotely. This means it is highly likely that child support will be implemented later than April 2021 and that the end date of the programme will be pushed out beyond the expected end date of September 2021.
- 50 Inland Revenue does not expect the delay to be a lengthy one and is committed to completing transformation and closing down the programme as quickly as possible in 2021/22. The caveat will be the amount of additional COVID-19 related work we ask Inland Revenue to do.
- 51 It is too early yet for Inland Revenue to be definitive about what the re-planning of the final stage will mean for the timeframes and costs of the transformation programme. Inland Revenue is working through the options and is keeping the Minister of Finance and me fully informed. My working assumption is that Inland Revenue will complete transformation within the existing funding envelope approved in 2015 by government. A full update will be provided by Inland Revenue in its November 2020 report to Cabinet.

The final stages of organisation design are also being re-planned

- 52 Proposed changes to Inland Revenue's organisation design are being re-planned. This will help to ensure that Inland Revenue's people can focus fully on supporting customers and our response to COVID-19 without the distraction of a consultation process. Inland Revenue had previously indicated (CAB-19-MIN-0583 refers) that further changes would take place during 2020 and 2021. This will now occur later than the timeframes originally envisaged.
- 53 Organisation change is still required in the near future to ensure that customers' and the government's needs can continue to be met, that the gains made by transformation are enduring, and that Inland Revenue can operate sustainably. Recognising the current environment, Inland Revenue's current thinking is that organisational change will take place more incrementally over a sustained period during late 2020 and in 2021. An update will be provided in Inland Revenue's November 2020 update to Cabinet.
- 54 Retaining resources for slightly longer than planned does provide some opportunities. It will better position Inland Revenue to provide on-going support to customers as we chart a course through COVID-19.
- 55 We could choose to leverage Inland Revenue's capabilities to design and deliver our COVID-19 responses, after having considered the implications and trade-offs. This could also provide opportunities for other agencies to learn from Inland Revenue's experience and expertise and to leverage the investment made in transformation.
- 56 Many agencies are already doing so, particularly in the enterprise support services area. Inland Revenue has provided 32 other agencies with access to the common process model. The department is also working with a number of agencies, including Customs, StatsNZ and Withheld under Section 9(2)(i) of the Official Information Act 1982., that have chosen to implement the cloud-

based Oracle technology Inland Revenue is using to support their back-office functions. There could also be opportunities for other agencies to leverage the investment made in Inland Revenue's core systems.

- 57 For Inland Revenue, retaining these resources provides the opportunity to ensure the capabilities delivered by transformation are more fully embedded so it can continue to deliver government priorities successfully in the future.

There are some potential implications for benefit realisation

- 58 Realisation of the non-financial benefits of transformation, policy agility, system resilience and easier for customers, is already well-advanced. These benefits are expected to be fully realised by the close of the programme, albeit it is taking time for customers to get used to and trust new ways of doing things.
- 59 The re-planning of organisation design changes may have implications for Inland Revenue's ability to realise the administrative savings. The savings have already been removed from outyear baseline funding so the challenge for Inland Revenue is to manage within a reduced funding level. These savings are part of the funding available for transformation. It is too early yet for Inland Revenue to say what the implications will be.
- 60 Realising further reductions in businesses' compliance effort may be difficult to achieve in light of the economic impacts of COVID-19. The impacts may over-shadow businesses' perception of the extent to which their compliance effort has changed. To date, the compliance effort for small and medium-sized enterprises has reduced as expected.
- 61 Realisation of additional Crown revenue may also be impacted. Inland Revenue will continue to maintain the integrity of the revenue system, leveraging the enhanced analytical capabilities now embedded that will be critical to helping customers to get things right and ensuring revenue leakage is minimised.
- 62 Inland Revenue will provide an update on progress on realising its benefit commitments in its November 2020 update.

Risk remains high

- 63 While risk has reduced somewhat, it will remain high until transformation is complete. It is important to maintain momentum to ensure Inland Revenue moves completely off its heritage systems and processes. The department will go as fast as it can, as safely as it can.
- 64 The most significant risks I see for the remainder of the programme are:
- 64.1 The re-planning of the final stage and the work required to support our COVID-19 responses could slow programme momentum and make retaining key people more difficult. To mitigate this, a small group of people within the programme are focused on re-planning the final stage and on responding to COVID-19. This is enabling the majority of the programme team to remain focussed on their work. Inland Revenue has identified key people within the programme and has succession plans in place.
 - 64.2 Moving child support to new systems and processes is more difficult than expected. To mitigate this, Inland Revenue will involve specialists from across its business and external stakeholders as appropriate to ensure the design of services meet

customers' needs and that customers understand what is changing and why. Notwithstanding, there are likely to be difficulties as child support customers have complex circumstances and can be hard to reach.

64.3 Inland Revenue does not achieve all its benefits commitments. It is likely this risk will eventuate as a result of external factors or the impact of COVID-19 on the economy. As noted, there are potential implications for the financial benefits Inland Revenue committed to delivering. The Minister of Finance and I will be kept fully informed of any trade-offs that need to be made and any material changes will be brought to Cabinet to consider.

64.4 If COVID-19 and transformation work is not balanced appropriately, Inland Revenue may never complete transformation and will therefore be unable to fully migrate off heritage systems and processes. This would result in higher costs, as two core systems would have to be run and maintained indefinitely, higher operational risk due to on-going co-existence, and benefits not being fully realised. To mitigate this, the Minister of Finance and I will work with Inland Revenue to ensure an appropriate balance is maintained and that any trade-offs required are made visible.

Next steps

65 The next steps are to:

65.1 complete the re-planning of the final stage of the programme by August 2020;

65.2 support the passage of the Child Support Amendment Bill which contains key transformation proposals;

65.3 continue with the on-going programme of independent quality assurance; and

65.4 provide a further progress update to Cabinet by November 2020.

Consultation

66 A copy of this paper has been provided to the Accident Compensation Corporation; the Department of Internal Affairs; the Department of Prime Minister and Cabinet; the Ministry of Business, Innovation, and Employment; the Ministry of Education, the Ministry of Social Development; the New Zealand Customs Service; and Stats NZ.

Financial Implications

67 The proposals in this paper have no financial implications.

Human Rights

68 The proposals in this paper have no human rights implications.

Legislative Implications

69 The proposals in this paper do not require any changes to legislation.

Regulatory Impact Analysis

70 The proposals in this paper do not require a Regulatory Impact Statement.

Gender Implications

71 The proposals in this paper have no gender implications.

Disability Perspective

72 The proposals in this paper have no implications for people with disabilities.

Proactive Release

73 I propose to proactively release this Cabinet paper, and associated minutes in whole within 30 working days of Cabinet making final decisions.

Central agencies' comment (The Treasury, State Services Commission and Government Chief Digital Officer)

Acknowledgement of success

74 The central agencies commend Inland Revenue on the scale of their achievement since the last Cabinet update. Inland Revenue has successfully gone-live with Release 4, the most technically difficult release to date, with minimal issues, and have played a central role in delivering the Government's response to COVID-19 thus far.

75 Inland Revenue's ability to play this role is in large part due to the capabilities business transformation has created. This is evidence that the programme is delivering on its policy agility and system resilience benefits commitments. These benefits are outlined in paragraphs 58 to 61.

Risks to benefit realisation

76 Business transformation is tracking well on a technical level, but it remains an inherently high-risk programme that requires careful management to successfully complete. Central agencies have committed to work with Inland Revenue to ensure business transformation benefits are realised in a transparent and sustainable manner.

77 In our view, there are significant challenges to sustainably realising the projected revenue uplift and administrative savings, while also maintaining the tax system's integrity at current levels. Inland Revenue's current forecasted baselines implies a significant reduction in staff levels. There is a risk this decreases their ability to deliver their required outputs. COVID-19 and its related effects exacerbate these challenges and increases the risk that the programme's benefits will not be sustainably realised. This risk has two main drivers:

77.1 Constrained administrative capacity: Inland Revenue has played a central role in supporting the Government's COVID-19 response. The additional demands associated with the COVID-19 response have placed a heavy burden on the department's administrative capacity. Administrative constraints arising from these additional demands will affect the ability of the department to deliver both business-as-usual functions and future releases of business transformation.

77.2 Changing environment: the economic landscape has changed significantly since the approval of the business case (not least because of the impact of the COVID-19 pandemic). There is likely to be a greater demand for a different mix of outputs from Inland Revenue (e.g. direct customer contact and integrity activities). The full realisation of the financial benefits from business transformation may compromise the ability of the department to respond effectively to these changing demands.

78 While Cabinet has agreed to extra time-limited funding to mitigate the COVID impacts, this will not address the programme's pre-existing challenges.

Benefits prioritisation and next steps

79 Given the newly heightened risk environment, the Treasury agrees with Inland Revenue that it is necessary to re-plan the final stage of transformation.

80 Inland Revenue intends to report back to Cabinet on its benefit commitments in November. The Treasury recommends that this report back assess the impact of fully realising business transformation benefits on the delivery of the department's outputs – and, in particular, on the department's ability to deliver integrity activities. This will allow Ministers to consider the organisational impacts of future reductions in Inland Revenue's baseline as a result of realising the business transformation benefits.

81 Any reduction in the size of business transformation's financial benefits will have an ongoing fiscal impact, because the expected administrative savings have already been included in forecasted baselines. However, in light of the current and expected demands on Inland Revenue, the Treasury's preliminary view is that integrity work and revenue uplift should be prioritised over the realisation of administrative savings. The Treasury will provide full advice on benefits prioritisation after the completion of the re-planning and benefit commitment update.

Recommendations

I recommend that the Committee:

- 1 note that Inland Revenue successfully migrated KiwiSaver and Student Loans to new systems and processes on 16 April 2020;
- 2 note that the final stage of the programme will not now be implemented as single release in April 2021 thereby delaying the closure of the transformation programme;
- 3 note that changes to Inland Revenue's organisation design are being re-planned and will now be implemented incrementally during late 2020 and in 2021;
- 4 note that trade-offs may be required depending on any additional COVID-19 related work we ask Inland Revenue to do;
- 5 note the potential implications for realisation of financial benefits;
- 6 note that the next progress update will be provided to Cabinet by November 2020 and will include the revised timeframe for and, if necessary, costs of, the transformation programme.

Authorised for lodgement

Hon Stuart Nash
Minister of Revenue