The Treasury

Budget 2024 Information Release

September 2024

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[1] 6(a) - to avoid prejudice to the security or defence of New Zealand or the international relations of the government

[23] 9(2)(a) - to protect the privacy of natural persons, including deceased people

[25] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information or who is the subject of the information

[27] 9(2)(ba)(ii) - to protect information which is subject to an obligation of confidence or which any person has been or could be compelled to provide under the authority of any enactment, where the making available of the information would be likely otherwise to damage the public interest

[31] 9(2)(f)(ii) - to maintain the current constitutional conventions protecting collective and individual ministerial responsibility

[33] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials

[34] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions

[35] 9(2)(g)(ii) - to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment;

[36] 9(2)(h) - to maintain legal professional privilege

[37] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice

[38] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice

[39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage

[40] 18(c)(i) - that the making available of the information requested would be contrary to the provisions of a specified enactment

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Budget 2024 Bilateral: Hon Simon Watts (Minister of Revenue) Monday 11 March 3:30 pm

Proposed Agenda

1. Context around B24 and associated constraints
2. Inland Revenue Baseline savings submission
3. Minister of Revenue's proposal
4. Savings / Reprioritisation for new initiatives

Budget 2024 Package Talking Points

- Following agency submissions for Budget 2024, both operating and capital demands are significantly higher than the funding available.
- It is clear that ambition for new spending will not be achievable from both a fiscal and delivery perspective. The Government will need to balance its policy objectives with its fiscal objectives.
- In doing so, we need to acknowledge that we have three Budgets across this term - and therefore think carefully about what we do now versus what we do in future Budgets.
- We also need all Ministers to continue to push hard where they consider their agencies have not provided sufficient savings options or there are further savings available, particularly with regards to stopping funds and programmes not aligned with our priorities, or addressing back office and contractor and consultant growth.
- As we exit the 100-day period, I am also taking a stricter approach to out-of-cycle requests for funding ahead of Budget 2024. This will help ensure that we can assess the relative benefits of proposals across the full Budget package.

Vote-specific Talking Points

Inland Revenue Baseline savings submissions

- We recommend you push the Minister of Revenue and Inland Revenue to reconsider whether there is further room to scale up their savings package without impacting revenue collection or debt.
  - What other significant savings proposals did you consider but not put forward as part of the Initial Baseline Exercise?
  - What key trade-offs did you make in proposing savings?

Minister of Revenue's Proposal

- We recommend you make clear that the targeted savings options cannot be offset against the baseline savings expected of Inland Revenue.
- We also recommend you set clear expectations that Inland Revenue consider options to increase tax revenue for Budget 2024 if asked, and to support future Budgets as part of setting the Tax and Social Policy Work Programme.

Savings/Reprioritisation for New Initiatives

- We recommend you ask the Minister of Revenue and Inland Revenue to provide you with further detail on how Inland Revenue intend to achieve the return on compliance funding, what their plan is for hiring the FTE required, and to consider options to reprioritise some existing funding to achieve the increased compliance outcomes. It is important Budget Ministers understand the trade-offs associated with any reprioritisation.
  - Can the agency find some of the [33] of funding for compliance and debt management while still generating the same revenue?
  - [33]

- We recommend you push the Minister of Revenue and Inland Revenue to consider whether they can achieve further efficiencies in delivery of these policies, while clearly articulating the trade-offs, so that Ministers can make informed choices about the level of funding required.

Summary

Inland Revenue and the draft Budget package includes savings of $29.6m p.a. compared to the $39.6m p.a baseline savings target. The package is $10m or 25% under the target. [33]

Further initiatives have been presented, including additional funding to support compliance and debt management. Inland Revenue calculated that a [33] positive OBEGAL impact could be generated by [33] in further compliance and debt management activity. (1:8 ratio). Treasury is considering whether Inland Revenue could reprioritise some or all of the funding for the compliance initiative from within existing baselines.

Treasury has scaled Inland Revenue's request for other new initiative funding by $32.4m over the forecast period. Officials encourage you to test with the Minister of Revenue whether the new funding can be further scaled.

Context:

Inland Revenue is a large agency with a total departmental baseline of $797.3m for 2023/24, declining to $731.3m for 2024/25. It had 4023 FTE with personnel costs of $479.4m in 2022/23. Inland Revenue collects 80% of the Crown's revenue and administers five social policies (Working for Families, child support, student loans, KiwiSaver and paid parental leave).

Inland Revenue achieved significant efficiencies through their Business Transformation which spanned from 2015 to 2022. Transformation resulted in significant reductions to both the departmental baseline as well as FTEs over that period. The reduction in baseline and FTE is not reflected in a reduction in output as shown by the cost of tax collection having nearly halved since 2015. The cost of collecting $100 reduced from 80 cents in 2014/15 to 43 cents in 2022/23. We note that the Commissioner is under a statutory obligation to collect the highest net revenue over time that is practicable within the law.

The agency has significantly reduced FTEs by 1656 FTE between 2014/15 and 2022/23 (from 5679 FTEs in 2014/15 to 4023 FTE in 2022/23 meaning a 29% reduction over the period). During that period, departmental output expenditure reduced by $41m in nominal terms from $701m to $660m.

Inland Revenue received a boost in funding in 2023/24 to manage remuneration cost pressures. Inland Revenue's temporary COVID-related funding ends in 2024/25, as a result there is a downward trend in departmental funding from this year. Inland Revenue faces cost pressures for remuneration and inflation over the forecast period, compounding to $63m in 2027/28, whilst dealing with a reducing baseline over the same period. To manage these Inland Revenue is already reprioritising within their baseline. Inland Revenue's forecast baseline is shown below:

	$ million – increase / (decrease)				
	2023/24	2024/25	2025/26	2026/27	2027/28
Baseline (after OBU 2023)	797.292	731.280	698.164	697.446	709.455

Baseline savings submission:

Inland Revenue has submitted baseline savings options totalling $29.6m per annum, falling $10m (approximately 25%) short of their $39.6m p.a. baseline savings target.

The two baseline savings options submitted were:

ID 15770 – Inland Revenue baseline savings – reduction in operating expenditure – $14.6m p.a. – Treasury's recommendation is to support

This initiative involves a $14.6m p.a. reduction in departmental operating expenditure on travel, training, accommodation, overtime, and contractors and consultants. Treasury officials support this savings initiative.

ID 15772 – Inland Revenue baseline savings – reduction in systems maintenance and change capacity – $15m p.a. – Treasury's recommendation is to support

Treasury considers this option to be realisable savings. However, the implementation of a reduction in change capacity in particular might lead to future cost pressures and increase the cost and lead-in time of previously manageable changes to the tax system. In order to avoid future costs outweighing the savings over the forecast period, future projects will need to be prioritised by both ministers and the agency.

[33]

Minister of Revenue's proposal:

[33]

Savings / Reprioritisation for new initiatives:

Reprioritisation for compliance funding

Inland Revenue's compliance bid sought departmental funding [33] to drive a positive OBEGAL net impact of [33] over the forecast period, through new tax compliance and debt recovery activity. This submission is based on the National/NZ First Coalition agreement to "increase funding for IRD tax audits to urgently expand the IRD tax audit capacity, minimise taxation losses due to insufficient IRD oversight, and to ensure greater integrity and fairness in our tax system."

The [33] (net impact after departmental cost) is made up of a combination of tax revenue and secondary non-departmental impacts (e.g. reductions in debt impairment). The current Budget package only includes the tax revenue component [33] against the operating allowance. The remainder relates to secondary non-departmental impacts such as reductions in debt and debt impairment. Treasury's fiscal management approach is to only manage the direct impacts (tax revenue) against allowances. However, ultimately whether to recognise secondary impacts against the Budget allowance is a decision for ministers to make. Treasury will provide further advice on this ahead of Budget Ministers three. Any additional revenue collected through this initiative, or reduced debt impairment, would flow through to OBEGAL.

The current Budget package reflects [33] of the requested funding for the compliance initiative for Inland Revenue, with the expectation the other [33] is met through reprioritising existing baseline funding. We suggest you press the Minister of Revenue to reprioritise to meet a minimum of 50% of the funding required, and a higher proportion if possible. However, the increased revenue submitted by Inland Revenue was calculated on a fixed ratio of up to 8:1, which suggests if Inland Revenue cannot meet this proportion through reprioritisation it could lead to a reduction of the revenue that could be booked against the Budget allowance. Likewise, we would need to understand the impacts of shifting resource within the existing baseline and whether those changes have an impact on OBEGAL (for example shifting from social policy functions is expected to have a negative impact on debt and debt impairment). Further examination of the impact of any changes to the submitted bid will be required to ensure that an appropriate amount of increased revenue is managed against the allowance. This would need to be considered in the context of the level of any new funding and Treasury's assessment of Inland Revenue's ability to improve its current compliance and debt recovery activity (noting the Commissioner's existing statutory obligation to maximise revenue collection over time). Treasury officials would also need to understand the trade-off of any reprioritisation towards compliance activity within existing baselines. Inland Revenue is not currently aware that scaling down of administrative funding for compliance is being considered.

Deliverability of compliance funding return

Treasury considers there is a risk that a portion of the additional funding sought by Inland Revenue in its bid could be used to maintain existing service levels in other areas (e.g. call centre resources). While the call centre resources will be needed to support compliance, trade-offs with existing service levels could allow reprioritisation to support the compliance activity.

We also have concerns about the deliverability of the compliance initiative. The initiative seeks a significant increase of [33] from 2024/25. Approximately [33] of the requested funding relates to "back office" staff: managers, legal and IT support, and clerical/admin officers. The back-office support has been calculated on the basis of 1 manager for 15 staff. Treasury considers that some of these resources may be able to be reprioritised from other areas.

While in theory this initiative could be scaled up to generate more revenue and savings, the Treasury questions Inland Revenue's ability to hire the required FTEs and deliver the estimated return on investment under this scenario. [33]

Overall, the Treasury considers that there may be possibilities to reprioritise some existing resources to support the compliance activity. However, we also consider that there are significant risks to the level of increased revenue that would eventuate with reduced new funding for the initiative. There is a judgment call to be made on the level of comfort with those risks occurring while reprioritising existing resources.

Reduced funding for new initiatives

The Treasury has recommended reducing departmental funding for new policy initiatives such as Family Boost and Personal Income Tax threshold changes in order to generate further savings. This ensures a continued drive for efficiencies in Inland Revenue's implementation and delivery of new policy and aligns with the statutory obligations of the Commissioner.

The Treasury has recommended that Inland Revenue self-funds:

- All capital costs for all initiatives saving $7m over forecast.
- All capital -associated operating costs for all initiatives (excluding online gambling) saving $5.2m over forecast.
- All departmental costs for 2023/24 for all initiatives (excluding online gambling) saving $2.9m over forecast.
- [33]

We have also recommended a 30% reduction in the funding and FTE requests for the FamilyBoost and Personal Income Tax initiatives. This will result in a savings of $22.4m over forecast.

These recommendations reduce future operating expenditure by **$32.4m over forecast** compared with what Inland Revenue submitted.

Please note that there are risks with recommending these additional savings that need to be weighed up:

- Customers will have questions about changes to their entitlements. If Inland Revenue is under-resourced to manage these queries, there will likely be service complaints as well as incorrect processing of entitlements. This could undermine the effectiveness of the Government's social policies due to:
    - overpayment of entitlements which would create debt for customers who may find themselves unable to pay. This would then result in an increase to debt-impairment and debt write-offs. We note that there has been a significant increase in Inland Revenue's debt impairments in recent years.
    - families that are entitled to benefit from the social policy that Inland Revenue administers may get their payments late, at a lower level, or not at all.
- Inland Revenue may divert resources from their compliance activity to administering social policy. All departmental funding from these initiatives would go into Inland Revenue's Multi-Category Appropriation which can subsequently be overspent on categories provided the total does not exceed the overall appropriation. If resources are taken from revenue collection areas this could result in a decrease in Crown revenue.

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