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Inland Revenue
Department:
Procurement for
the Business
Transformation
programme



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Contents

Overview	3
Our recommendations	5
Part 1 – Introduction	6
Why we did our audit	6
Scope of our audit	7
How we carried out our audit	8
Structure of this report	8
Part 2 – Background	9
Procurement in the public sector	9
Procurement in the Business Transformation programme	9
Part 3 – A new approach to procurement	12
A centralised and collaborative approach to procurement	12
Restructuring the Commercial and Procurement team	13
Proactive and structured approach to managing relationships with suppliers	15
Early signs of positive results	16
Part 4 – Sourcing practices	19
Rules and policies are not always complied with	19
Quality controls need to be better applied and documented	21
Information management for procurement is inadequate	22
Probity is not well documented	23
Figures	
1 – Accountabilities of the Commercial and Procurement team	10

Overview

New Zealanders collectively pay about \$70 billion in tax each year. The Inland Revenue Department (Inland Revenue) is responsible for collecting tax. It is important that Inland Revenue collects taxes effectively because the funds are essential for the Government to provide New Zealanders with a wide range of services and support.

Inland Revenue is spending millions of dollars on its Business Transformation programme (the programme), which is designed to create a “modern revenue system” that will make it easier for taxpayers to pay their taxes.

This modern revenue system is intended to use more reliable information technology, be less costly to run than the current system, and accommodate government policy changes in a timely and cost-effective way. We have committed to report from time to time on aspects of the programme for its duration.

The programme is expected to cost between \$1.5 and \$1.69 billion and to be completed by 2021. Much of the programme’s costs come from purchasing goods and services. The public needs to have confidence that Inland Revenue is procuring these goods and services effectively and efficiently so the programme can achieve its objectives.

Because the programme needed a greater number of often more costly and more complex procurements than Inland Revenue had entered into before, Inland Revenue recently changed its approach to procurement, firstly for the programme and later throughout the whole organisation. This was a positive step taken to enable procurement to better meet the programme’s needs as well as Inland Revenue’s broader needs during and after the transformation.

We decided to look at whether the programme’s procurement is effective, is well managed, and complies with relevant rules and other requirements. As well as looking at Inland Revenue’s overall approach to procurement, we focused on two parts of the procurement process:

- sourcing goods and services; and
- managing relationships with suppliers.

We looked at a sample of individual procurements for goods and services related to the programme in detail. The procurements we looked at had been completed before Inland Revenue changed its procurement approach because not many had been undertaken under the new approach at the time of our audit. We found some instances where Inland Revenue did not consistently comply with relevant rules and policies. Although most of these instances were minor, there was one more significant instance. The timing of our audit meant that it was too early to assess whether or how the new approach had improved Inland Revenue’s compliance with relevant procurement rules and policies.

As part of its change in approach, Inland Revenue centralised and restructured its procurement function and brought in procurement specialists with appropriate skills and resources. This change was well thought out and caused minimal disruption for the rest of Inland Revenue.

The new approach focuses on relationships and outcomes, and aims to get the best results and value for money from purchasing goods and services. One aspect of this is that Inland Revenue works closely with its most important suppliers in a structured way to monitor their performance. This has helped improve suppliers' performance as well as helping Inland Revenue identify areas where it could improve.

In my view, Inland Revenue has a clear vision and purpose for its new approach to procurement. Although changes have been implemented only recently, there are early signs that those changes are likely to improve supplier performance and outcomes for Inland Revenue.

However, Inland Revenue still needs to make important improvements to some of the processes that support its new procurement approach. When we looked at individual procurements, Inland Revenue could not locate all the documents we asked to see. Also, in some instances, we could not find evidence that quality controls had been applied. We found an inconsistent approach to probity and inadequate documentation to support some probity decisions.

We have made four recommendations to help Inland Revenue improve the way it procures goods and services, including for the programme. Inland Revenue needs to make these improvements to ensure that its suppliers, the public, and staff can continue to have confidence that its procurement processes are consistently robust, fair, and transparent.

We will follow up on the progress Inland Revenue is making in implementing these recommendations as part of our ongoing review of the programme.

I thank Inland Revenue staff for co-operating with our audit. I also thank people we talked to from the Ministry of Business, Innovation and Employment, the office of the Government Chief Digital Officer, and the programme's suppliers.



Greg Schollum
Deputy Controller and Auditor-General

12 March 2018

Our recommendations

We recommend that the Inland Revenue Department:

1. improve its compliance with the Government Rules of Sourcing and its own policies to ensure that it always follows a robust, fair, and consistent approach to procurement;
2. as a matter of priority, strengthen the way it applies and records quality controls for procurement so it can show that quality controls are always applied as intended;
3. prioritise improvements to how it keeps procurement and contract records to ensure a complete and accessible audit trail; and
4. put adequate probity assurance arrangements in place and document the probity approach for procurements, including decisions about obtaining and acting on probity advice, to clearly show that procurements have been fairly conducted through a transparent and impartial process.

1

Introduction

- 1.1 In this Part, we set out:
- why we did our audit;
 - the scope of our audit;
 - how we carried out our audit; and
 - the structure of this report.

Why we did our audit

- 1.2 New Zealanders collectively pay about \$70 billion in tax each year. The Inland Revenue Department (Inland Revenue) is responsible for collecting and managing tax. Effective tax collection allows the Government to provide New Zealanders with a wide range of services and support.
- 1.3 To collect taxes efficiently, Inland Revenue needs robust and up-to-date systems and processes. About seven years ago, Inland Revenue began a significant Business Transformation programme (the programme) to simplify and streamline its business processes, policies, and customer services and upgrade its technology platform. Inland Revenue wants to create a “modern revenue system” that makes it easier for taxpayers to pay their taxes.
- 1.4 Inland Revenue estimates the total cost of the programme to be between \$1.5 and \$1.69 billion and expects it to be completed by 2021. Stage 1 of the programme went “live” in February 2017, two months ahead of schedule.
- 1.5 Stage 1 introduced new online services for Goods and Services Tax and made it possible for new businesses to register online for an Inland Revenue Department number. At that point, Inland Revenue had spent about \$190 million on the programme.
- 1.6 Stage 2 of the programme involves streamlining personal and business income taxes. Inland Revenue expects stage 2 to be completed by 2019.
- 1.7 The changes and cost involved in the programme are significant. It is also an important project for New Zealanders because it will introduce new and modern processes and technologies for collecting tax and paying entitlements. For these reasons, we have decided to report from time to time on aspects of the programme for its duration.
- 1.8 Our first report on the programme, published in April 2015, looked at the way the programme was governed.¹ The programme had several strengths, including a comprehensive and clear governance structure, an established methodology, and an advanced approach to managing risks.

¹ Office of the Auditor-General (2015), *Inland Revenue Department: Governance of the Business Transformation programme*, Wellington.

- 1.9 The programme's governance arrangements largely met our expectations. The governance was providing clear direction to the programme. We recommended that Inland Revenue continue to adapt the programme's governance arrangements for the programme's duration.
- 1.10 This is our second report on the programme. For this audit, we decided to look at procurement. Procurement is much more than just a purchasing process. When we talk about procurement, we are talking about an end-to-end process that involves:
- deciding which goods and services need to be procured to enable the entity to do its job and do it better;
 - going through a sound sourcing process that is founded on the principles of good procurement practice;
 - ensuring that delivery against the contract, and the relationships that underpin it, are well managed and that the procurement delivers what is needed and the intended benefits; through to
 - evaluating the results and lessons from the procurement and either disposing of or terminating or replacing those goods and services.
- 1.11 Inland Revenue is spending millions of dollars on goods and services for the programme. It is important that Inland Revenue procure these goods and services effectively and efficiently so it can deliver the programme's objectives and achieve value for money.
- 1.12 We looked at whether procurement for the programme is well managed and whether it complies with relevant rules and requirements.

Scope of our audit

- 1.13 For this audit, we looked at two parts of the procurement process:
- how Inland Revenue sources goods and services, focusing on compliance with applicable rules and policies; and
 - how Inland Revenue manages its relationships with suppliers.
- 1.14 We also looked at Inland Revenue's overall approach to procurement. Inland Revenue has recently changed its approach to procurement. We wanted to see whether the new approach has been implemented effectively and whether it is helping Inland Revenue to improve the way it procures goods and services.
- 1.15 We did not look at policy decisions about the programme or whether the programme is achieving its intended outcomes.

How we carried out our audit

- 1.16 To carry out our audit, we:
- reviewed and analysed relevant documents from Inland Revenue;
 - interviewed staff from Inland Revenue, including staff in the Commercial and Procurement team and staff in the programme;
 - spoke to people from the Ministry of Business, Innovation and Employment, the office of the Government Chief Digital Officer, and some of the programme’s suppliers;
 - viewed systems and tools used by Commercial and Procurement staff;
 - reviewed information and data from five procurements that were valued at \$100,000 or more to check that they complied with government rules and Inland Revenue’s policies and good practice; and
 - reviewed information and data from seven procurements that were valued at less than \$100,000 to check that they complied with government rules, Inland Revenue’s policies, and good practice.

Structure of this report

- 1.17 In Part 2, we describe how procurement works in the public sector and Inland Revenue’s Business Transformation programme.
- 1.18 In Part 3, we describe Inland Revenue’s new approach to procurement.
- 1.19 In Part 4, we discuss whether Inland Revenue is following relevant rules and processes for procurement.

Background

- 2.1 In this Part, we describe the context for procurement in the public sector. We also describe how procurement works in the programme.

Procurement in the public sector

- 2.2 Government agencies procure a wide range of goods and services, and the markets that they operate in also vary.
- 2.3 The Ministry of Business, Innovation and Employment has a leadership role in public sector procurement. The Ministry works with government agencies to lead best practice procurement in the public sector and make government agencies a customer of choice for suppliers. The Ministry focuses on using a collaborative and centre-led approach to raise standards, improve capability, and reduce duplication in government procurement.
- 2.4 The Ministry has published a series of procurement rules called the Government Rules of Sourcing (the Rules).² The Rules set out good practice guidelines for government agencies to follow in the sourcing stages of the procurement process.
- 2.5 The Rules are intended to help government agencies design processes that are robust and that build public confidence in how they plan and carry out their procurement. This should help increase public trust that government spending is being planned and executed well.
- 2.6 In 2009, Cabinet agreed to initiate the Government Procurement Reform programme, which is aimed at improving procurement policy and practice throughout the State sector. Some of the desired changes come from increased use of all-of-government contracts.
- 2.7 All-of-government contracts establish single-supply agreements for selected goods and services to deliver cost and efficiency savings. Inland Revenue is moving away from owning assets and towards sharing assets and service contracts with other government agencies.

Procurement in the Business Transformation programme

- 2.8 Inland Revenue is procuring a wide range of goods and services for the programme. When stage 1 of the programme went live in 2017, Inland Revenue had more than 300 contracts with several different suppliers. Most of these contracts were worth more than \$100,000, and some were worth significantly more than \$1 million. Together, these contracts will cost Inland Revenue more than \$500 million for the programme's duration.

² The Government Rules of Sourcing can be found at www.procurement.govt.nz and include a full description of which agencies are required to follow the Rules.

- 2.9 Because of the significant value of the contracts, it is important that Inland Revenue procures these goods and services in a cost-effective way. It also needs to manage these contracts well to get the best outcomes from them.
- 2.10 Inland Revenue's Commercial and Procurement team is responsible for leading procurement for Inland Revenue, including for the programme. The team is accountable for five functions in Inland Revenue (see Figure 1).

Figure 1
Accountabilities of the Commercial and Procurement team



Source: Adapted from an Inland Revenue presentation, October 2016.

- 2.11 Inland Revenue has also adjusted its governance arrangements to meet the needs of the organisation as the programme has progressed. The Commissioner of Inland Revenue is now the programme sponsor. This recognises the significance of the programme to the whole organisation. Inland Revenue's Investment and Performance Committee provides governance oversight for procurement and is part of the Executive Governance System.
- 2.12 Like all government agencies, Inland Revenue is expected to follow the Rules. These are supplemented by its own procurement guidance and policies. These are consistent with the Rules but include additional requirements and detail that are specific to Inland Revenue and the programme. Examples include Inland Revenue's procurement policy and organisational probity framework, and a sourcing strategy for the programme.

3

A new approach to procurement

- 3.1 In this Part, we discuss:
- Inland Revenue’s centralised and collaborative approach to procurement;
 - the restructuring of the Commercial and Procurement team;
 - Inland Revenue’s approach to managing relationships with suppliers; and
 - early signs of positive results.

Summary of our findings

- 3.2 Inland Revenue’s new approach to procurement uses a new and centralised team of procurement staff and focuses on relationships and outcomes. The new approach seeks to get the best results and value for money.
- 3.3 Inland Revenue first introduced this approach to meet the needs of the programme’s costly and complex procurement. Inland Revenue considered that this approach would support better procurement for the whole organisation and implemented it throughout the organisation from the end of 2016.
- 3.4 Although changing the procurement approach caused some disruption, staff feedback on the new team and its procurement work is increasingly positive. The new approach is encouraging Inland Revenue to think about procurement more strategically.
- 3.5 Inland Revenue has implemented the changes only recently, but there are early signs that its approach will improve the way it does procurement. Inland Revenue also estimates that it is making financial savings.
- 3.6 One aspect of the new approach is Inland Revenue’s open and regular dialogue with its most important suppliers. This has helped Inland Revenue get a more comprehensive understanding of the performance of its suppliers and how they can improve. It also draws attention to ways Inland Revenue can improve. Inland Revenue has been responsive to feedback from suppliers and has made changes where it sees a need for improvement.

A centralised and collaborative approach to procurement

- 3.7 Inland Revenue has recently changed its approach to procurement. Previously, procurement staff in each business unit carried out the procurement process. This approach focused largely on following each step in the procurement process, rather than on the outcome desired.
- 3.8 Because the programme required more and increasingly complex procurements, Inland Revenue started to change the way it approached procurement. It wanted to deliver better results for the programme by focusing on relationships and outcomes.

- 3.9 Inland Revenue considered that this new approach, which was aligned to its overall vision for the transformation, could also deliver better results for the whole organisation. Towards the end of 2016, Inland Revenue began to implement this approach throughout the whole organisation.
- 3.10 As part of this change, Inland Revenue centralised and restructured its procurement function, bringing in specialists with the skills and resources to deliver its approach successfully.
- 3.11 Although the same Rules and policies apply, the new approach is more flexible and agile, and is intended to factor in the commercial needs of the whole organisation. For example, rather than automatically renewing contracts to supply goods and services to one business unit, Inland Revenue will now identify the need for those goods and services throughout the whole organisation and find the best way to meet that need.

Restructuring the Commercial and Procurement team

- 3.12 As a result of the restructure of Inland Revenue's procurement function, there are now three teams in the Commercial and Procurement team:
- **the performance and capability team**, which focuses on processes and practices throughout the team;
 - **the commercial corporate team**, which focuses on the end-to-end management of corporate sourcing and contract management; and
 - **the commercial information and communications technology team**, which focuses on the end-to-end management of information and communications technology (ICT) sourcing, including software licences.
- 3.13 Role descriptions for positions in the Commercial and Procurement team clearly describe what the new staff are responsible for.
- 3.14 The Commercial and Procurement team is responsible for procurement and contract management for all business units in Inland Revenue. The Manager Commercial ICT, and the two Commercial Specialists who report to them, are also responsible for the commercial management of the programme.
- 3.15 Although the Commercial and Procurement team is responsible for procurement, Inland Revenue recognises that other teams in the organisation also have a role to play. Inland Revenue acknowledges that successfully managing suppliers requires the contribution of all relevant people within the organisation. This means empowering business units to manage their own procurement, with the Commercial and Procurement team providing specialist advice and support.

- 3.16 The Commercial and Procurement team has filled all the new positions that resulted from the restructure and has the capacity it needs to work effectively. Although the Commercial and Procurement team is structured into three different teams, resources can be moved between these teams when workloads are high. Capacity can sometimes be stretched, but this is expected to improve as business units take more responsibility for managing their more routine supplier relationships.
- 3.17 Inland Revenue accepted that abruptly changing its procurement staff would result in some loss of institutional knowledge. However, it expected the disruption to be temporary. Inland Revenue believed that a quick transition would enable staff to implement the new approach more effectively.
- 3.18 As expected, there was some initial disruption after the restructure. Inland Revenue staff we spoke to six months after the restructure said that the disruption had caused some delays. However, the speed of the Commercial and Procurement team's work is increasing. Importantly, the disruption from the restructure has not affected the programme's timelines.
- 3.19 The Commercial and Procurement team is receiving increasingly positive feedback from other business units in Inland Revenue. Staff from other business units were surveyed on how the team was performing in February and September 2017.
- 3.20 The February 2017 survey showed that the "churn in resources" was seen as causing confusion about who was responsible for what, but that there was a sense that this would improve once the new team structure had settled in. Of the survey's respondents, 73% responded positively to questions about the team's productivity, communications, business value, and culture. In September, 86% of survey respondents responded positively to these questions.
- 3.21 Internal support for the Commercial and Procurement team is also helping with the transition process. The new structure and function of the Commercial and Procurement team was communicated effectively in Inland Revenue before the changes were made. People told us that Inland Revenue's senior executives were open to new ideas to improve the ways the Commercial and Procurement team operated.
- 3.22 Induction for staff joining the Commercial and Procurement team after the restructure was limited. New staff were given standard Inland Revenue induction modules but not anything specific to procurement. There was a specific induction module available for staff involved with the programme, but staff were not aware of it when they started. Induction about procurement in the public sector would be useful for staff joining from the private sector and help them become effective faster.

- 3.23 Nevertheless, ongoing training and development is helping staff in the Commercial and Procurement team. A dedicated team in the Commercial and Procurement team is responsible for capability and performance. This team has arranged monthly forums and produced practice notes. It has organised negotiation training and is developing scenario training on conflicts of interest. Coaching and professional accreditation are also available from this team.

Proactive and structured approach to managing relationships with suppliers

- 3.24 As part of its new approach to procurement, Inland Revenue is taking a more structured approach to the way it works with suppliers. This means that, for example, Inland Revenue is now working more closely, and in a different way, with its most important suppliers. These are suppliers that provide complex services and are critical to achieving the programme's objectives.
- 3.25 Inland Revenue currently identifies about nine suppliers as the most important. Inland Revenue has regular and open dialogue with these suppliers to help get the best outcomes for both parties.
- 3.26 Each month, the Commercial and Procurement team asks relevant Inland Revenue staff to score the performance of each of these nine suppliers and provide other feedback. The Commercial and Procurement team uses this information to identify risks and areas for improvement. The team also uses the information as the basis for monthly meetings with these suppliers. Managing contracts in this way gives Inland Revenue an up-to-date picture of the performance of its most critical suppliers.
- 3.27 Staff working in the programme said that this process helps to get the best performance from suppliers and identifies problems before they become serious. For example, the Commercial and Procurement team had monthly meetings to resolve an issue with the accuracy of one supplier's billing. The accuracy of billing improved as a result.
- 3.28 Suppliers we spoke to also told us that they see value in this open, regular, and structured way of working. They said that it helps them improve their performance and make sure issues get resolved before they escalate.
- 3.29 Inland Revenue produces a high-level quarterly report that consolidates performance information about its most important suppliers. Reporting performance like this helps Inland Revenue identify trends in supplier performance. It also helps Inland Revenue identify lower-performing suppliers and the areas that they need to improve in.

- 3.30 The most recent quarterly report showed that service levels were dropping slightly for all suppliers included in the report. The report gave Inland Revenue the information it needed to start addressing the issue.

Managing issues with supplier performance

- 3.31 Inland Revenue acknowledges the risk that suppliers may breach their contract and has steps in place to manage this risk. Inland Revenue believes its approach to managing relationships with suppliers is important for avoiding breaches of contract. Therefore, proactive contract performance and supplier management should be done as a matter of course.
- 3.32 The way Inland Revenue manages relationships with suppliers allows it to identify breaches of contract when they happen and to respond quickly and effectively. Most breaches are minor and are resolved through regular supplier meetings. If the issue is still not resolved after three months, staff will involve more senior personnel.
- 3.33 For more serious breaches, the process generally involves both Inland Revenue's corporate and legal department and senior executives. Inland Revenue can also withhold payments. Serious breaches that require escalation are rare. This supports Inland Revenue's belief that its approach to managing relationships with suppliers prevents breaches from occurring.

Two-way communication with suppliers

- 3.34 Suppliers also provide Inland Revenue with feedback about what is working well and what could be improved. Inland Revenue also looks at what it can do to help improve supplier performance, rather than just looking at what the supplier can do.
- 3.35 This two-way communication means that Inland Revenue can respond to any feedback or issues that suppliers have about how it operates. For example, Inland Revenue has improved its scorecard system so suppliers can rate Inland Revenue's performance. Inland Revenue has also been responsive to suppliers that have asked it to take more innovative approaches.

Early signs of positive results

- 3.36 Inland Revenue is starting to look at whether its new approach to procurement is saving money. The Commercial and Procurement team uses a spreadsheet to track savings. Savings can be achieved when the Commercial and Procurement

team renegotiates a contract to get a better price or reviews Inland Revenue's requirements for a particular item or service and identifies a more cost-effective solution.

- 3.37 The Commercial and Procurement team then works out the value of any savings achieved. To date, the Commercial and Procurement team has estimated that it has saved \$18 million for Inland Revenue. These savings have not been verified, so we cannot confirm them. Measuring cost savings from procurement will help Inland Revenue to see what effect the new team is having over time. We encourage Inland Revenue to continue measuring cost savings, have them verified, and report them publicly.
- 3.38 The Commercial and Procurement team has a focus on building strong relationships with other business units in Inland Revenue. Staff are now approaching the Commercial and Procurement team more proactively. These relationships within Inland Revenue are helping the Commercial and Procurement team understand business needs throughout the whole organisation and provide procurement solutions that best meet those needs. This has increased the team's workload.
- 3.39 The feedback the Commercial and Procurement team has received about its performance from business units throughout Inland Revenue – for example, from the survey of other business units mentioned in paragraphs 3.19-3.20 – shows an improvement in performance. By continuing to get this feedback on a regular basis, the Commercial and Procurement team can track its performance.
- 3.40 Inland Revenue does not currently assess how individual procurements contribute to the programme's intended benefits. We encourage Inland Revenue to consider how individual procurements help to achieve benefits for the programme as a whole and how to measure that.

Sharing lessons from the new approach to procurement

- 3.41 The Commercial and Procurement team is open about sharing information with other government agencies. Inland Revenue has shared procurement and contract management-related lessons with a range of government agencies, including the Treasury, the Accident Compensation Corporation, Land Information New Zealand, the Earthquake Commission, the Department of Corrections, and the Department of Internal Affairs. It has also shared lessons with the governments of Singapore and New South Wales.

- 3.42 One example of Inland Revenue sharing its experience and lessons learned is its “competitive dialogue”³ case study, published in 2014. The case study was targeted at government agencies that might be considering using competitive dialogue or were in the early planning stages of a procurement process. This case study has made information about the benefits of competitive dialogue and how to best use it available to the wider public sector.
- 3.43 The Commercial and Procurement team is also sharing information about supplier performance with the Government Chief Digital Officer. This means that knowledge about an underperforming supplier can be shared with other government agencies that are using, or thinking about using, the supplier. It also helps the Government Chief Digital Officer to monitor the performance of suppliers under all-of-government contracts.

³ Competitive dialogue involves discussing all aspects of a contract with a shortlist of suppliers before final proposals are requested.

Sourcing practices

4.1 In this Part, we consider whether Inland Revenue is following relevant rules and policies when sourcing goods and services. We discuss:

- non-compliance with rules and policies;
- the need for Inland Revenue to apply and document quality controls better;
- the need for Inland Revenue to improve its information management; and
- the need for Inland Revenue to document probity better.

Summary of findings

4.2 The introduction of its new approach to procurement is a positive step forward for Inland Revenue, but we found weaknesses in compliance with good practice for sourcing that Inland Revenue needs to address. Inland Revenue needs to improve these important aspects of its sourcing practices to ensure that its new approach can be successfully applied.

4.3 There were some instances of non-compliance with rules and policies in our review of some individual procurements. One instance was more significant and could expose Inland Revenue to the risk of legal challenge.

4.4 The Commercial and Procurement team does not have a structured approach to compliance or quality control but expects documents to be checked and signed off by the right people at the right times. Poor information management for procurement meant we could not tell whether this is happening and means that Inland Revenue does not know whether checks and sign-offs are happening as intended.

4.5 Inland Revenue's Probity Assurance Plan is out of date, and the Commercial and Procurement team does not consistently follow it. For example, there was limited documentation about some probity decisions, which means that decision-making about procurements is not always transparent.

Rules and policies are not always complied with

4.6 Inland Revenue expects staff to comply with relevant rules and processes, including the Government Rules of Sourcing (see Part 2). To support staff to follow the Rules, Inland Revenue has created its own policies and procedures. These policies and procedures outline Inland Revenue's approach to procurement and provide guidance, such as who has the authority to sign contracts and other important documents.

4.7 Inland Revenue has also put several processes and tools in place to support compliance. They include checklists, templates, and practice notes prepared by the Commercial and Procurement team's performance and capability team.

These are available on the Commercial and Procurement team's intranet site. The programme also has a detailed sourcing strategy, which has clear objectives and is consistent with the Rules.

- 4.8 We reviewed information and data from five large and seven smaller procurements to assess whether the Commercial and Procurement team was complying with the Rules and Inland Revenue's own policies. Inland Revenue was not able to provide all the information we needed to carry out this part of our audit. We based our assessment on the information that was available.
- 4.9 One procurement we looked at had a significant non-compliance issue. Inland Revenue had accepted an alternative price submission from a supplier late in the submission process but did not give the same opportunity to the other short-listed supplier. This is not good practice and does not comply with the Rules.
- 4.10 As well as this issue, there were several incidents of poor practice and non-compliance. For example, we could not find supporting documentation for contract variations, and there was incomplete documentation about conflicts of interest. Based on the available evidence, these examples appear to be the result of poor awareness or understanding of the Rules and Inland Revenue's policies. We did not find any evidence of intentional non-compliance.
- 4.11 For the individual procurements that we looked at in detail, planning and justification were generally done well. However, there is still room for improvement in two aspects of procurement:
- **Panel of pre-approved suppliers:** Inland Revenue is increasingly using panels of pre-approved suppliers for procurement. There needs to be better documentation of the justification and appropriate planning for the selected approach, as well as a consideration of any risks.
 - **Conflict of interest declarations:** Conflict of interest declarations were not fully completed and retained in all instances. Inland Revenue needs to ensure that conflict of interest declarations are reviewed in a timely way so that any issue can be managed before it causes any problems to the process.
- 4.12 The individual procurements we looked at to check for compliance are from before Inland Revenue restructured its procurement function. However, Inland Revenue's new procurement approach must still comply with the Rules and Inland Revenue's own policies. For example, the Rules apply to relevant agencies regardless of the overall approach individual agencies might take.

- 4.13 We consider that Inland Revenue is in a good position to make the improvements that we have identified. Inland Revenue is expecting the new Commercial and Procurement team to tighten up practices and bring more rigour to procurement processes.
- 4.14 The Commercial and Procurement team was working on some improvements at the time of our audit. It was too early to assess the effectiveness of these improvements. Inland Revenue needs to ensure that the improvements it makes strengthen compliance.

Recommendation 1

We recommend that the Inland Revenue Department improve its compliance with the Government Rules of Sourcing and its own policies to ensure that it always follows a robust, fair, and consistent approach to procurement.

Quality controls need to be better applied and documented

- 4.15 We did not see evidence of quality controls being consistently applied to all of the procurements we looked at. The Commercial and Procurement team's approach to quality control is to ensure that the appropriate people review and sign off documents at appropriate times. This helps to pick up errors or identify any non-compliance that might occur.
- 4.16 The Commercial and Procurement team has processes in place to support quality controls. These processes include peer review, managerial review, a delegation matrix, and external probity advice. The template for procurement plans includes a table that shows who has to approve important documents or stages of a procurement.
- 4.17 The Commercial and Procurement team also uses cover notes to help check compliance with relevant rules and policies before procurements and contract renewals are signed off. Cover notes can include information such as contract value, applicable rules, and available funding sources. This means that, when the appropriate people sign off procurements, they have the information they need to understand what they are signing and whether it is appropriate for them to sign.
- 4.18 Although we were told about these quality controls and saw the requirements of different control points described in the procurement plan template, we did not see evidence that the Commercial and Procurement team consistently applies them in practice.

- 4.19 This means that neither we nor Inland Revenue can be sure whether the Commercial and Procurement team is routinely complying with the Rules or with its own policies and procedures. Given that, we found several examples of non-compliance, Inland Revenue needs to urgently improve how it applies and records quality controls for procurement.

Recommendation 2

We recommend that the Inland Revenue Department, as a matter of priority, strengthen the way it applies and records quality controls for procurement so it can show that quality controls are always applied as intended.

Information management for procurement is inadequate

- 4.20 Poor information management for procurement made it difficult for Inland Revenue to show us that it is routinely checking compliance with the Rules and its own policies. It also affected how we did our audit.
- 4.21 We wanted to review a range of procurements to ensure that they complied with the Rules and Inland Revenue's policies. However, the Commercial and Procurement team struggled to find the documentation that we asked for, and we had to reduce the number of procurements we intended to look at. Even then, the documentation for these procurements was incomplete and spread between different locations.
- 4.22 For example, in some procurements that we looked at, there was a lack of available records to show that correct procedures had been followed. This meant that we could not make a reliable judgement about how well the Commercial and Procurement team complies with the Rules or Inland Revenue's policies. We also could not make a reliable judgement about how consistently the team applies procurement practices or quality assurance controls.
- 4.23 An internal audit of procurement was expected to be completed in mid-2017, but it was delayed because the auditor had issues acquiring the relevant information.
- 4.24 The software programme that Inland Revenue uses to support procurement is not fit for purpose. It does not support workflows or the approvals process for contracts, and it is confusing for staff who use it. Inland Revenue is aware of these limitations and is in the early stages of acquiring a new software programme. Inland Revenue is currently collaborating with other government organisations that are looking for a similar product.

Recommendation 3

We recommend that the Inland Revenue Department prioritise improvements to how it keeps procurement and contract records to ensure a complete and accessible audit trail.

Probity is not well documented

- 4.25 In the procurement context, probity means making sure all suppliers have a fair opportunity as part of a process that is transparent, impartial, and equitable. It is important that Inland Revenue applies probity principles when procuring goods and services.
- 4.26 Organisations can get assurance about how well they have applied probity in several ways. Probity audits are one example. Probity audits provide an independent perspective and give assurance to all parties involved in the procurement process that all suppliers have had a fair opportunity and that the procurement process has been carried out transparently and impartially. Suppliers are also more likely to feel they can raise a concern if an independent party is involved.
- 4.27 Inland Revenue has decided to use probity advisors to check probity on a case-by-case basis. It has appointed lawyers for this purpose. Inland Revenue also provides staff with high-level guidance on how to conduct themselves when engaging with the supplier market to ensure that they comply with Inland Revenue's probity principles. This means that Inland Revenue expects staff to ensure that procurement is conducted fairly and understand what they need to do if there are barriers to this.
- 4.28 Inland Revenue's Probity Assurance Plan outlines the probity principles and procedures that apply to procurements for the programme. The plan sets out the probity requirements and obligations for each stage of the procurement process. It is intended to help ensure "that documented processes are applied, a clear audit trail is established and decision-making is fair, transparent and defensible".
- 4.29 The plan, published in 2014, has not been updated since Inland Revenue restructured its procurement function. It does not reflect the current governance arrangements for the programme or the restructured Commercial and Procurement team.

- 4.30 In the procurements that we looked at, the Commercial and Procurement team was not always applying the principles and requirements of the Probity Assurance plan. In particular, it did not document well the procedures for obtaining and acting on probity advice.
- 4.31 In one instance, probity advice was sought from Inland Revenue's external probity advisor but not acted on. In our view, there was inadequate documentation to give assurance that decision-making was fair, transparent, and defensible.
- 4.32 Inland Revenue needs to document decisions about probity issues more clearly. Individual procurement plans need to also set out the probity approach for that procurement so that this is clear from the outset.
- 4.33 For a programme of this scale and complexity, we expect Inland Revenue to be confident it is procuring goods and services for the programme in a transparent and impartial way. Because of the lack of probity audits and its weaknesses with probity processes, Inland Revenue needs to assure itself, its suppliers, and taxpayers that it has adequate probity assurance arrangements in place.

Recommendation 4

We recommend that the Inland Revenue Department put adequate probity assurance arrangements in place and document the probity approach for procurements, including decisions about obtaining and acting on probity advice, to clearly show that procurements have been fairly conducted through a transparent and impartial process.

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