New South Wales Auditor-General's Report
Performance Audit

Efficiency and effectiveness in tax collection

Office of Finance and Services
Office of State Revenue

audit office
OF NEW SOUTH WALES

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In accordance with section 38E of the *Public Finance and Audit Act 1983*, I present a report titled **Efficiency and effectiveness in tax collection: Office of Finance and Services, Office of State Revenue.**

A T Whitfield PSM
Acting Auditor-General
25 June 2015

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Executive summary

Conclusion

While there is performance data and qualitative information that enables assessment of some aspects of the Office of State Revenue's (OSR) tax collection activities, it is difficult to make a confident overall assessment of efficiency and effectiveness. This is not a problem unique to OSR, as revenue collection bodies throughout Australia and overseas find it challenging to meaningfully measure their efficiency and, especially, their effectiveness.

Notwithstanding the limitations with the current performance management framework, OSR can demonstrate improved efficiency and effectiveness in specific areas of its business. It can do this by benchmarking against its own historical performance and against other revenue collection agencies, as well as by pointing to specific successful initiatives.

The performance data reported publicly in the Office of Finance and Services' annual report is limited and inadequate to promote public accountability in OSR's performance.

A better understanding of OSR's effectiveness may emerge from analysis of any gap between tax revenue actually collected and that which would be collected if all taxpayers met their obligations. OSR has committed to undertaking this analysis into potential 'tax gaps' that may exist across tax streams.

OSR could build a stronger evidence base for the level of resources needed to optimise tax revenue, as well as the optimal revenue that can be derived from existing resources. This analysis could usefully inform broader resource allocation decisions to help ensure that OSR has the resource capacity needed to optimise revenue.

Comparative performance benchmarking suggests that the OSR has become more efficient and effective in a number of areas, although this is not consistent. As shown at section 3, the OSR can demonstrate a number of initiatives that are likely to have contributed to improved efficiency and effectiveness.

Supporting findings

OSR has a commitment to continuous improvement

OSR demonstrates a commitment to continuous improvement and undertakes regular evaluations of projects and programs. It has a wealth of experience and expertise in revenue collection, and is able to demonstrate success across a range of activities. OSR's strategic planning process is comprehensive and includes extensive consultation with staff and stakeholders.

While other audits of performance measurement have linked weakness in performance frameworks to a lack of managerial and executive commitment, we did not find this with OSR.

However, as with many revenue collection bodies in Australia and overseas, it is not yet able to provide a convincing impression of its overall efficiency and effectiveness in tax collection.

Further work needed to establish if there is a 'tax gap'

OSR has a number of performance indicators that seek to measure efficiency and effectiveness. However, a crucial gap in assessing its effectiveness is knowing what proportion of the available tax base is collected compared to what should be collected if all taxpayers met their obligations.

OSR has committed to doing work to identify whether there is a 'tax gap' as part of its 2015-2021 strategic plan. Given OSR's key role as the primary revenue agency for NSW, we encourage this work being done as a matter of priority. As reliable tax gap analysis remains a challenge for many jurisdictions, there is opportunity for OSR to establish itself as a leader in this field.

Building a stronger evidence base for optimal performance

OSR's recent compliance enhancement programs have successfully highlighted the link between additional resourcing and additional revenue. Under these programs, for every additional dollar spent on tax collection, $10 was returned to the State. The total revenue collected exceeded targets.

Given the experience and expertise available to the agency, there is scope for OSR to conduct more sophisticated analysis to set compliance revenue targets that may be more challenging and drive better performance. Such analysis could aim to balance the full potential tax base, the costs to collect tax, and the burden imposed on taxpayers by different levels of compliance activity.

Analysis of the relationship between investment in compliance and tax collected could usefully inform future OSR resource allocation decisions. This includes internal decisions regarding how best to allocate resources within in OSR, as well as Government budget deliberations.

Improvements needed to OSR's performance framework

This audit also looked at OSR's existing performance measures. We found gaps in its performance framework. For example:

- despite a focus on improving rates of voluntary compliance, there are limited divisional key performance indicators (KPIs) for matters like taxpayer error rates, improvements in voluntary compliance, or community understanding of tax obligations.
- OSR aims to streamline processes and tax transactions, the measurement of which relies on the 'percentage of payments received electronically'. However, changes in this measure might simply reflect a broader shift in community preference to online payments.

OSR has many performance metrics that sit beneath its KPIs. These lower level and operational metrics are likely to be of value for internal decision making. However, an observer should be able to get a clear impression of OSR's efficiency and effectiveness from its high-level KPIs without having to drill down through multiple levels of reports.

Work is underway in OSR to review existing KPIs and ensure their alignment with OSR's strategic objectives. Later work will seek to align lower level measures with KPIs to ensure that there is a 'line of sight' from operational and individual performance management through to overall divisional KPIs.

Opportunities for more informative public reporting

OSR's current annual reporting, as part of the Office of Finance and Services, compares unfavourably with the more detailed reporting it undertook under previous governance arrangements with NSW Treasury. Very few performance measures are reported by OSR externally, either through the Office of Finance and Services (OFS) annual report or through other channels, such as OSR's website.

Knowing whether OSR operates efficiently and effectively is essential to determining whether it is delivering the community value and contemporary service referred to in OSR's vision statement. Without strong, transparent and publicly reported performance measures, the value for money provided by OSR in collecting a third of the States revenue may be difficult to establish.

Recommendations

1. OSR should clarify its definition of effectiveness so that the concept is not restricted by “doing more with the same resources or less”

2. In order to better demonstrate OSR’s overall effectiveness in collecting tax revenue, OSR should:

   a) work in collaboration with NSW Treasury and other expert bodies to progress tax gap analysis by the end of 2016–17

   b) build a stronger evidence base for setting compliance revenue targets and modelling different resource levels to optimise tax revenue collection

   c) ensure that compliance revenue targets incorporate the analysis performed under paragraphs a) and b).

3. OSR should review its current suite of key performance indicators and performance measures to ensure that by 2016–17:

   a) KPIs clearly demonstrate the extent to which OSR is efficient and effective in optimising tax revenue

   b) KPIs are aligned to, and can more clearly demonstrate the achievement of, organisational objectives and goals as per OSR 2021

   c) there is a clearer hierarchy of KPIs and measures to ensure that achievement of lower-level performance measures contribute to the achievement of higher level KPIs and organisation goals

   d) operational, business unit, branch and program plans each have measures to hold managers accountable for performance

4. OSR should enhance its governance and accountability arrangements with the Office of Finance and Services through:

   a) a framework agreement with the Office of Finance and Services that formalises and clarifies expectations, roles and responsibilities of each party, including to ensuring efficiency and effectiveness in tax collection

   b) improving the quality of monthly OSR management reporting to OFS with key performance indicators which demonstrate OSRs efficiency and effectiveness in tax collection

5. OSR should publish more performance information publicly on its efficiency and effectiveness, such as in the Office of Finance and Services annual report or on its own website.

Introduction

1. Office of State Revenue

The Office of State Revenue (OSR) is a division within the Office of Finance and Services (OFS). OFS is an executive agency of the Treasury and part of the Treasury and Finance 'cluster'.

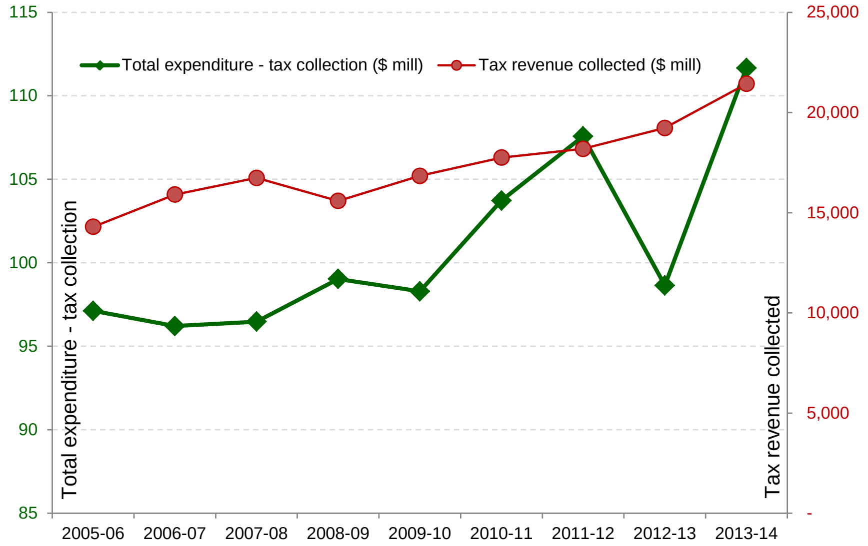
Under this arrangement, the Treasurer is coordinating minister for the cluster and the Treasury is the principal agency. There is also a Minister for Finance and Services with portfolio responsibilities within the cluster.

The Treasury is led by a Secretary, while the Office of Finance and Services is led by a Chief Executive. The OSR is led by an Executive Director, who also holds the statutory position of Chief Commissioner of State Revenue and Commissioner of Fines Administration.

The Executive Director of the OSR is directly accountable for his performance to the Chief Executive of the Office of the Finance and Services. This is discussed further in section 2.

Exhibit 1.1 shows total OSR revenue and expenditure from 2005–06 to 2013–14. In 2013-14, total revenue collected was $21.43 billion and total expenditure was $111.7 million.

Exhibit 1.1 Total OSR tax revenue and expenditure, 2005–06 to 2013–14



Source*:* Office of State Revenue, unpublished time series

Note: Expenditure figures exclude grants made under the First Home Buyers' Scheme

Scope and focus of this performance audit

The objective of this performance audit is to assess the efficiency and effectiveness of OSR in optimising taxation revenue collection. Taxation is the overwhelming majority of the OSR's total revenue. In 2013–14, OSR's three largest sources of tax revenue were:

- $8 billion in payroll tax
- $7.8 billion in duties
- $2.4 billion in land tax.

Given this focus, other sources of revenue – such as the collection of fines and debts – are outside the scope of this audit.

Further information on the audit scope is available in appendix 2.

OSR's Operations business model for efficient and effective tax collection

The Operations business unit of OSR has developed a business model for the effective and efficient administration of tax collection (Exhibit 1.2). Operations is the business unit of OSR most extensively involved in tax collection.

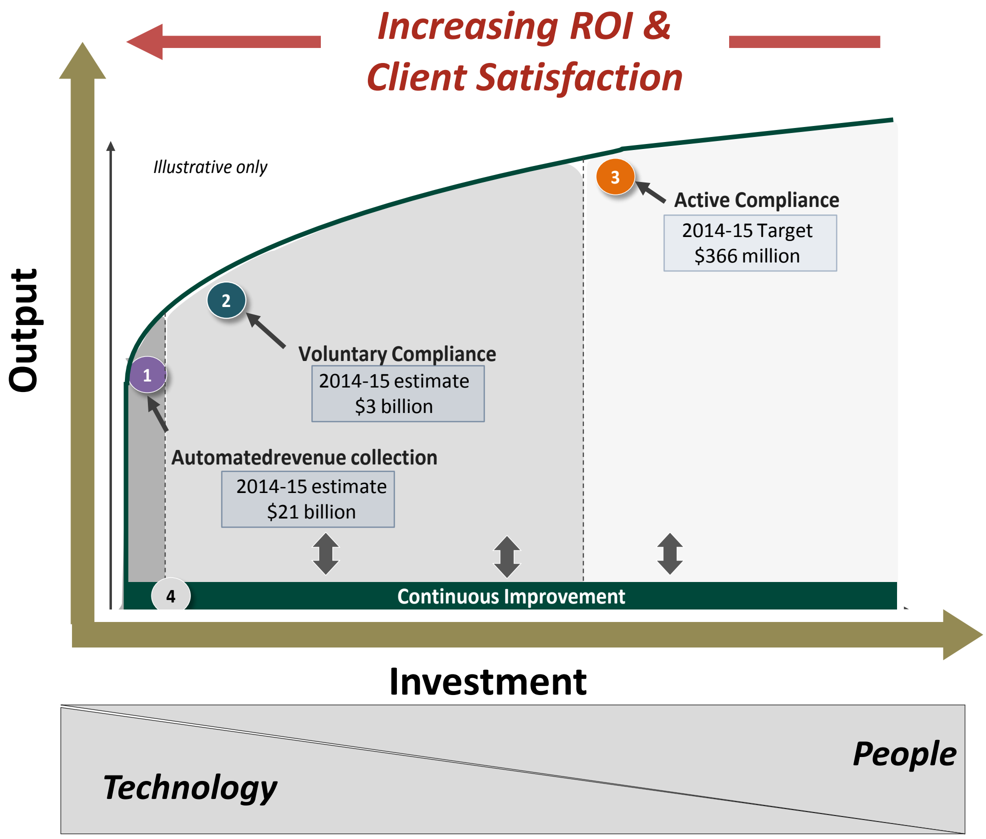
The model is driven by a 'key objective' of 'protecting and maximising' the revenue collected through automated and client-initiated collections. These types of revenue collection require a relatively small resource investment for a high return. The bulk of OSR's revenue falls within these categories.

In contrast, revenue collected through 'active compliance', such as by audits, is a relatively small component of total tax revenue – in 2014–15, the revenue target for active compliance is $366 million out of combined forecast revenue collection of $24 billion.

Despite representing a small slice of total revenue, compliance work is resource-intensive – in 2014, approximately 200 of the OSR's 1,300 staff were employed in tax compliance activities (about 600 of OSR's staff work in non-tax areas completely).

While this 'active compliance' activity is not as cost-effective as automated revenue collection and voluntary compliance, it serves an important role in deterring non-compliance.

Exhibit 1.2 OSR Operations business model for efficiency and effectiveness in tax collection



Source: OSR, unpublished.

Revenue agencies throughout the world have adopted business models similar to that applied by the OSR's Operations business unit. For example, Her Majesty's Revenue & Customs (HM R&C) in the United Kingdom applies a 'promote, prevent, respond' model to compliance that is aimed at moving more taxpayers to voluntary and automated payments. Under this approach, which aligns to the business model in OSR, HM R&C aims to:

> '…*promote* voluntary compliance by making it easier for taxpayers to get it right; *prevent* non-compliance by intervening at the point of transaction; and *respond* robustly to non-compliance by those who deliberately evade or avoid'

For the purposes of our audit, we define optimal tax revenue as where the tax revenue collected is sufficient to justify the:

- cost imposed on Government to collect it
- the cost imposed on taxpayers as a result of OSR compliance activities.

Perfomance framework for efficiency and effectiveness

Performance measures: 'what gets measured, gets done'

A sound performance framework, underpinned by good performance indicators and targets, serve a number of important functions in public sector agencies.

A performance framework should:

- inform high level decision making by clarifying objectives and responsibilities
- guide better performance with clear, attainable, and challenging targets
- make performance more transparent and enhance accountability of the agency to the Parliament and the community by understandable and accessible reporting.

The Ministerial Council of Federal Financial Relations (MCFFR) has suggested criteria that should apply to performance indicators for government service provision. It has posited that performance indicators should:

- be simple and comprehensible
- meaningfully measure what they purport to measure
- be supported by underlying data that is reliable
- form a hierarchy, with high-level performance indicators underpinned by lower level (more detailed but consistent) performance data where a greater level of sector specific detail is required for other purposes.

The intergovernmental Steering Committee for the Review of Government Service Provision (Steering Committee) has similar criteria, though most relevantly to this audit, the Steering Committee's expectations of an effective performance framework include that it:

- be comprehensive, assessing performance against all important objectives
- include high level performance indicators that focus on outcomes, reflecting whether service objectives have been met.
- be hierarchical, with high-level outcome indicators underpinned by lower level output indicators where greater detail is necessary
- be meaningful by including reported data that must measure what it claims to measure.
- be understandable so as to improve public accountability through data that is reported in a way that is meaningful to a broad audience, many of whom will not have technical or statistical expertise.

Developing performance indicators for tax revenue collection

The use of performance frameworks has been recognised as an approach to improve efficiency and effectiveness in revenue collection. Within this context, there is a wide range of indicators and performance measures used across countries (and even across Australia).

Broadly though, indicators for measuring the efficiency and effectiveness of tax revenue collection fall within three main categories:

- compliance
- quality of service
- cost.

A fourth category has been proposed for indicators that measure core organisational activities, though these simple input and output measures are often at best only proxies for measuring organisational performance.

The Australian Taxation Office (ATO) has set out an internationally regarded framework for developing performance indicators for revenue collection. The ATO asserts that a suite of performance indicators should be capable of providing a 'defensible picture' of performance.

The ATO also endorses the widely used 'SMART' test to validate performance indicators, where the indicators should be: specific; measurable; achievable; relevant; and timed.

The Organisation for Economic Co-operation and Development (OECD) adds additional criteria for testing performance indicators for use in revenue agencies. Indicators should be:

- comprehensive in their view of performance
- attributable to the revenue body's action
- meaningful for external stakeholders.

The role of measuring 'tax gap' in effectiveness

The 'tax gap' is the difference between the tax revenue that ought to be collected and tax actually collected. Measuring the tax gap can provide decision makers important insights into the types and extent of non-compliance that contribute to a tax gap, either overall or in respect to a specific type of tax. An accurate measure of the tax gap can indicate the effectiveness of a revenue authority, such as OSR.

Much has been written over the last two decades about the complexity of calculating the tax gap, particularly as it relates to specific types of taxes and work in this area is evolving. Most research in this area has focussed on measuring the tax gap as it relates to income tax. The development of a broader evidence base for other forms of taxation has been slower to develop. There are issues related to the development of a robust methodology for calculating the tax gap and often tax gap measures tend to be quite specific for both the jurisdiction and the type of tax or duty being assessed.

While it remains a challenging and methodologically under-developed field, there is some limited tax gap analysis done in Australia for non-income taxes (for example, the Goods and Services Tax and the Luxury Car Tax), as well as internationally.

Notably, HM R&C in the United Kingdom now attempts to measure the tax gap for all areas of taxation and revenue. Other jurisdictions that measure the tax gap include the United States and the European Union. Denmark has a tax gap indicator, accompanied by a target to keep the tax gap at below 3.1% of GDP.

Performance reporting in the Office of State Revenue

As part of its performance framework, OSR has a range of high level key performance indicators (KPIs). As OSR is a division of the Office of Finance and Services (OFS), these high-level KPIs are referred to as 'divisional KPIs'.

There are four types of KPI measured by OSR:

- 'vision' KPIs to measure whether OSR's vision is being achieved
- 'driver' KPIs to allow visibility of key aspects of OSR's operating performance
- 'strategic' KPIs to measure the achievement of OSR's Strategic Plan
- 'business as usual' KPIs at the business unit and branch level.

The tax-related KPIs in each category are shown below in Exhibit 1.3, also sub-categorised by 'pillars' described in OSR's 2021 strategic plan.

Exhibit 1.3 Tax related key performance indicators

<table>
<tr><th colspan="3">Vision: An excellent organisation of professional people proudly delivering community value and contemporary service.</th></tr>
<tr><th>Strategic KPIs</th><th>Driver KPIs</th><th>Vision KPIs</th></tr>
<tr><td colspan="2">Pillar: 'Client experience'
'Make it easy for clients to do business with us'</td><td></td></tr>
<tr><td>Percentage of payments received electronically (tax)</td><td>Percentage of telephone calls answered within 2 minutes (Tax and Grants Call Centre)
Client satisfaction survey;
• satisfied OSR services
• satisfied with online services</td><td rowspan="7">Client Satisfaction Survey
• OSR explains the reasons for their decisions
• OSR staff are courteous and professional
• satisfied with online services

Cost to collect $100 tax</td></tr>
<tr><td colspan="2">Pillar: 'Compliance'
'Maximise compliance'</td></tr>
<tr><td>Cost to collect $100 tax</td><td>Percentage of debt intake resolved in the year of intake (tax)</td></tr>
<tr><td>Percentage of revenue received on time from monthly lodgers</td><td></td></tr>
<tr><td colspan="2">Pillar: 'Processes and systems'
'Processes and systems meet the needs of our stakeholders'</td></tr>
<tr><td>Collectable debt* as a percentage of revenue collected (tax)</td><td>Stability of OSR systems (percentage of productivity lost due to system outages)</td></tr>
<tr><td></td><td>Percentage of objections allowed/partly allowed</td></tr>
</table>

Source: OSR, unpublished. * 'Collectable debt' is that component of tax debt with no legal impediment to recovery.

In addition to these KPIs, there are a large number of performance measures at the business unit and branch levels. As well as informing decision making in their respective work areas, these performance measures and metrics are used in various internal governance forums, such as a monthly Corporate Management Forum, and monthly revenue reporting to the Office of Finance and Services and to Treasury (see 'Internal accountability mechanisms' at page 22).

Key findings

2. Does the Office of State Revenue have a performance framework that enables it to monitor and report its efficiency and effectiveness in optimising tax revenue?

There are gaps in measuring and reporting tax collection effectiveness, while measures of efficiency would be strengthened by more sophisticated approaches that more convincingly attributed results to OSR activity.

This is not a problem unique to OSR, as revenue collection bodies throughout Australia and overseas find it challenging to meaningfully measure their efficiency and, especially, their effectiveness.

While there are many performance metrics at operational levels, overall KPIs provide only a limited impression of OSR's efficiency and effectiveness. Accountability for how well OSR collects around one-third of State revenue is further hampered by limited reporting to Government, the Parliament, and the public.

2.1 How does OSR define efficiency and effectiveness and what are the implications for tax revenue collection?

Separating efficiency and effectiveness

Any sound performance framework is underpinned by clarity and accuracy in the definition and application of key terms. How the OSR defines 'efficiency' and 'effectiveness' can affect what is meant by good performance.

OSR defines 'efficiency' as being:

> "… concerned with the relationship between input and output. The objective is to obtain the maximum output from a given level of input, for example, doing the same or more with fewer resources (input)"

This is consistent with common definitions of efficiency and seems appropriate for application to tax collection.

OSR's definition of 'effectiveness' is less well suited to measuring progress towards outcomes. In its value for money framework, OSR defined effectiveness as:

> "…the extent to which a service, process, project fulfils its intended purpose. It relates to the achievement of organisational goals and objectives (measures of output and outcomes including quality), ie doing more with the same resources or less" [emphasis added].

It is accurate to define effectiveness as being about whether goals, objectives or outcomes are achieved. However, the expression '…*doing more with the same resources or less*' is related to the concept of efficiency, not effectiveness.

Building an evidence base for optimising revenue

OSR has achieved considerable success in recent years with its compliance enhancement programs, under which additional funding has been sought and obtained from the Government for additional active compliance activities. Under these initiatives, for every additional $1 spent on tax collection, an additional $10 was returned to the State. OSR's success in meeting and exceeding budgeted revenue for these programs suggests that there may be scope for further pro-active compliance efforts.

OSR has said that it would be premature to seek further resources at this time, particularly while OSR is working to deliver already promised revenues from existing compliance enhancement work. Some senior managers with whom we spoke indicated that they would be reluctant to seek additional resources due to the difficulties that would follow in recruiting, training and accommodating additional staff.

We understand that all agencies have day to day operational imperatives and that funding decisions are a matter a Government.

However, OSR could establish a firmer evidence-base for the right mix of activities – and the level of resources to fund them – that would optimise OSR's community value. These activities could include active compliance, as well as initiatives to encourage automatic payment and voluntary compliance, such as education, online initiatives and greater automation. This analysis could be offered to inform Government budgetary deliberations.

Such analysis would balance the full potential tax base, the costs to collect tax, and the burden imposed on taxpayers by different levels of compliance activity.

This, together with the anticipated work on tax gap analysis, suggests that the determination of compliance revenue targets could be more sophisticated – and achieve greater returns to the State – than simply focusing on historical performance and adjusting for economic circumstances.

We did not view evidence that target-setting considered what revenue could be achieved under different resourcing assumptions. The current approach may result in relatively unambitious targets that fail to encourage innovation and improved performance.

Recommendations

1. OSR should clarify its definition of effectiveness so that the concept is not restricted by “doing more with the same resources or less”
2. In order to better demonstrate OSR's overall effectiveness in collecting tax revenue, OSR should:
   a) work in collaboration with NSW Treasury and other expert bodies to progress tax gap analysis by the end of 2016–17
   b) build a stronger evidence base for setting compliance revenue targets and modelling different resource levels to optimise tax revenue collection
   c) ensure that compliance revenue targets incorporate the analysis performed under paragraphs a) and b).

2.2 Are OSR measures of efficiency and effectiveness adequate?

Key factors impacting on OSR efficiency and effectiveness

OSR's performance framework exists to support OSR's objectives and outcomes, as well as providing a mechanism for transparency and accountability in achieving those outcomes.

OSR's strategic plan and the Operations Branch's business model indicate that the critical factors which drive efficient and effective tax collections include:

- encouraging clients to voluntarily meet their tax obligations, namely to be registered for tax and to pay the right amount at the right time with minimal OSR intervention
- using technology to streamline and, where possible, automate tax transactions and client interface, such as through on-line payroll tax assessments with automated reconciliations to help tax payers self-assess more accurately
- identifying and following-up on those who do not comply through risk based auditing and investigations and using technology to detect non-compliance.

For example, these factors can be seen in:

- the OSR Operation's business model for efficiency and effectiveness in tax collection, which is driven by the 'key objective' of 'protecting and maximising' the revenue collected through automated and client-initiated revenue collections (voluntary compliance).
- Pillar 1 of OSR's strategic plan, which emphasises service themes of simplicity, self-service, online availability, account transparency and clarity of service standards, coupled with an understanding of taxpayer needs to make it easy for clients to conduct their business
- Pillar 3 of OSR's strategic plan, which emphasises compliance as OSR's 'core business' and undertakes to invest in education and client advisory services and manage compliance activities based on risk, transparency and client behaviour.

A sound performance framework would include divisional – that is, high-level – KPIs that provide a defensible picture of how efficiently and effectively OSR is pursuing these strategic aims.

These divisional KPIs would, in turn, be supported by lower level performance measures, thereby establishing a 'line of sight' from operational activities through to OSR's vision.

There are limitations to how adequately OSR's key performance indicators demonstrate efficiency and effectiveness

The current suite of KPIs (Exhibit 2.1 below) do not provide a robust or comprehensive overall assessment of how well OSR is performing regarding those factors that will drive its efficient and effective tax collection.

There are few KPIs that reveal how well OSR is moving clients to automated and voluntary payments. Those that are relevant are:

- various client satisfaction survey results
- *percentage of telephone calls answered within 2 minutes*
- *percentage of revenue received on time from monthly payroll tax lodgers*.

The relationship between voluntary compliance and timely answering of the phones seems weak. Additionally, elements of the client satisfaction survey (*explained reasons for decisions*, *staff are courteous and professional*) seem only indirectly related to 'protecting and maximising' automated payments and voluntary compliance.

The *percentage of revenue received on time from monthly payroll tax lodgers* is useful – at least as a proxy indicator – for that specific tax stream, although it is not helpful for monitoring overall voluntary compliance across all tax areas. We note that there are no measures to monitor client error rates, which would have bearing on the effectiveness of promoting education and simplicity in tax processes – essentially, helping people to do their own tax arrangements accurately.

There are also limited KPIs around streamlining processes and transactions:

- *percentage of payments received electronically* – this measure stems back to 1999 when electronic payments were uncommon. Today, electronic payments are the norm, as reflected by the high results reported by OSR. There seems limited value in measuring what is now normalised behaviour as a KPI.
- *cost to collect $100 taxation* – as discussed below, this measure appears to be given an undue prominence in tax collection performance measurement.
- *client satisfaction with OSR on-line services*, this measure is of some value, although this indicator offers no insight into the proportion of transactions processed electronically. We also note that there are no indicators to monitor productivity gains achieved from on-line serves. Nor are there any indicators to monitor the impact of efforts in this area such as reductions in staff and resources invested in processing transactions.

There are no KPIs on simplifying tax collection to make it easier for clients to engage with the tax system without having to seek advice and information from OSR.

Measuring the cost to collect tax as an indicator of efficiency

Across Australia and overseas, the cost to collect $100 of tax is a leading performance measure for efficiency.

While conceptually simple to understand, this indicator may provide a distorted view of efficiency. It can also potentially discourage efforts to increase overall revenue collection. Recent enhanced compliance activities performed by OSR achieved returns on investment that were good, although lower than more routine collection activities. This resulted in a slightly higher cost to collect figure, notwithstanding that total revenue increased.

Managers we spoke to in OSR and across other revenue agencies had mixed views on this indicator. Some thought it had little value and rarely considered it in their decision making, while others felt that it was appropriate as one in a suite of indicators.

The KPI *cost to collect $100 tax* is discussed further in section 3.

Exhibit 2.1 OSR Tax Related Key Performance Indicators, 2015–2021

Vision KPIs **Measures whether OSR's vision is being achieved**	**Targets**
Client satisfaction survey: OSR explains the reasons for their decisions	>75%
Client satisfaction survey: OSR staff are courteous and professional	>80%
Client satisfaction survey: satisfied with online services	>85%
Cost to collect $100 tax	<$0.49
Strategic KPIs **Measures the achievement of OSR's Strategic Plan**	**Targets**
Percentage of payments received electronically (tax)	>90%
Percentage staff with recreation leave >30days	0%
Sick leave taken per FTE	<49 hours
Cost to collect $100 tax	< $0.49
Percentage of revenue received on time from monthly lodgers	>95%
Collectable debt as a percentage of revenue collection (tax)	<1.20%
Driver KPIs **Allows visibility of key aspects of OSR's operating performance**	**Targets**
Percentage of telephone calls answered within 2 minutes (tax and grant calls)	>80%
Client satisfaction survey: satisfied with OSR services	>86%
Client satisfaction survey: satisfied with OSR on-line services	> 85%
Percentage of staff with accumulated recreation leave over 25 days without future leave booked	<3.5%
Days lost due to workers' compensation claims	<0.5%
Percentage of staff with workers' compensation claims arising from workplace injuries	<1.7%
Percentage return to work within three months	>90%
Percentage of debt intake resolved in the year of tax intake (tax)	>85%
Stability of OSR systems (Percentage of productivity lost due to systems outages)	<1.1%

Source: OSR, unpublished.

OSR has additional divisional KPIs planned to present a more nuanced assessment at divisional level. These include:

- *Reduction in cost per payment*
- *Proportion received through digital channels.*

Adequacy of business unit performance measures

We have also examined measures used by business units with the greatest impact on tax revenue collection.

These business units are:

- Operations, which is responsible for:
  - researching, developing and implementing programs to encourage better compliance.
  - detecting underpayment and non-compliance through audits and investigations.
  - enforcing lodgement of returns and information from defaulting taxpayers

- Technical and Advisory Services, which provides specialist tax technical knowledge and services to internal and external clients of OSR, with an emphasis on the development of revenue policy and the independent review of transactions requiring specialised knowledge and services.

State Debt Recovery is also deemed to have day to day administrative role for state tax revenue. While debt recovery is outside the scope of this audit, we have referenced debt collection performance measures for tax, as these may have bearing on the efficiency and, more likely, effectiveness of tax collection.

Operations business unit measures

The business plan for the Operations contains the following key measures relating to tax collection:

Sick leave down by 10%	Reduce payments by cheques
Clients meeting voluntary obligations Compliance targets achieved	External data processing time turnaround time down 25%
Average number of years assessed for new clients<2.5years	Reduce time to detect non-compliance

The above measures do not sufficiently demonstrate the extent to which the Operations business unit is efficient and effective. For example, a key pillar of the Operations unit business plan is to 'maximise compliance'. Several performance measures relate to this pillar, but have varying degrees of usefulness.

- *compliance targets achieved:* as discussed earlier, there is opportunity for a stronger evidence base in how compliance revenue targets are set, which would in turn make this measure more meaningful.

- *reduce time to detect non-compliance* – This measure is a reflection of how well OSR is targeting its audit and investigations based on limited resources. This does not necessarily indicate whether or not there is unidentified tax owed. More broader targeting may find more non-compliance with longer periods of outstanding tax owing.

- *increase in clients meeting voluntary obligations* is measured by the proportion of on-time lodgement of returns and on-time payment as well as voluntary registrations. However, an increase in the volume of voluntary registrations may reflect efforts by OSR to improve voluntary compliance but it could also reflect changes in economic conditions such as increased employment rates, wage growth or increase in land values. This measure is unrelated to rates of non-compliance or non-registration.

Operations is the key business unit responsible for OSR's tax collection activities. As such, we would expect to see more meaningful leading measures that demonstrate the efficiency and effectiveness of its contribution to tax collection activities. Instead, there are fewer measures reported at this business unit level than reported at the divisional KPI level. It is more usual in a performance framework hierarchy for a larger number of lower level performance indicators – usually output or activity measures – to feed into a smaller number of higher-level, broad-based, and outcomes-focused indicators.

There are additional performance metrics that sit underneath the Operations business unit measures. These additional metrics are specific to each key tax stream. The metrics for each stream provide more comprehensive performance data at an operational level. For payroll tax and land tax, these metrics are set out in detailed Program Plans, which describe OSR's risk-based approach to tax compliance. While some measures share limitations already discussed (such as difficulty in attributing causation to OSR activities), the data would usefully inform day to day decision making.

These lower level metrics are detailed and likely to be useful for internal decision making, though are less visible for the purposes of showing overall divisional efficiency and effectiveness. The key internal reporting mechanisms are shown in Exhibit 2.4 on page 22.

We understand that the nature of the different taxes administered by OSR results in some performance measures being managed at the program level. This is similar to most government agencies that deliver a range of different types of services or programs.

Detailed operational metrics should not be a substitute for high-level measures that are fit for the purpose of reliably assessing OSR's efficiency and effectiveness. An observer should be able to get a clear impression of OSR's overall efficiency and effectiveness from its Key Performance Indicators, without having to drill down through multiple levels of reports.

Technical and Advisory Service business unit measures

Current measures mean that it is not possible for TAS to demonstrate success in carrying out vital tax administration roles, or in contributing to the efficiency and effectiveness of OSR overall. We recognise that the outcomes of these functions can be difficult to measure in a way that is more meaningful that than simply counting activities or outputs.

These measures are mostly workflow and output-related, which may be fit for the purpose of day to day management and administration. However, few of these measures relate to outcomes, which would allow TAS to demonstrate its contribution to efficient and effective tax collection.

There are no outcome measures for critical activities performed by TAS that improve tax collection efficiency and effectiveness. For example, measures for education activities include the number of events, webinars and expos held, but there are no measures around the impact of these events in improving voluntary compliance or helping those who owe tax "get it right the first time".

Another example of an important activity lacking adequate outcome measures is the advice TAS provides to government on reforming legislation. For example, it is difficult to demonstrate the impact of TAS advice aimed at simplifying tax is having on improved tax collection efficiency and effectiveness.

The Technical and Advisory Service (TAS) business unit's performance measures are shown below in Exhibit 2.2.

Exhibit 2.2 Technical and Advisory Services Monthly Dashboard Performance Measures

- Number of objections
- Objections received by Tax type, for example, duties, payroll, landtax
- Objections Determined by tax type
- Objections Outstanding by tax type
- NCAT and court matters/ lodged determined and current
- Appeals on hand by tax type
- Appeals on hand by Jurisdiction eg NCAT, Supreme court, court of appeal, high court
- Private ruling received
- Help desk enquiries for land and payroll tax and duties by telephone, face to face, private ruling, internal/external advising, complex issues
- Number of Technical and Client education events ; internal, external, webinars and expos
- Outreach: number of places visited, client numbers, enforcement orders, sanctions lifted
- Prosecution matters, received determined and onhand
- Complaints registered compared to prior year
- Design and Publishing projects opened and completed
- YTD web changes completed-all sites

Source: OSR, unpublished.

Key gaps in OSR KPIs and performance measures

Is there a 'tax gap' undermining effectiveness?

One of OSR's objectives is to "maximise compliance". To be effective in achieving this objective, OSR would need to collect all tax revenue from all individuals and businesses who incur a tax liability, regardless of whether or not they come forward and declare that liability. This is commonly referred to as the potential tax base.

The total potential tax base is well understood for some taxes, such as land tax. However, it is less well understood for other large taxes such as payroll tax. As a result the total size of the potential tax base in NSW is unknown. Therefore it is difficult to know how effective OSR is in collecting tax. Such assessment would require a comparison of current revenue collected against estimates of the potential tax base.

Measurement of the tax gap can provide decision makers insight into the types and extent of non-compliance which contribute to the tax gap. An accurate measure of the tax gap can provide a measure of the effectiveness of a revenue authority.

OSR has no current tax gap analysis to help monitor and demonstrate its overall effectiveness in tax collection. Previous attempts by OSR to estimate the gap were limited to examining gaps in collection for specific areas of payroll tax. Findings from this analysis were found to be inconclusive.

We acknowledge that determining a tax gap is a potentially complex task. Most research in this area has focussed on measuring the tax gap as it relates to income tax.

However, OSR plans to conduct a new tax gap analysis as part of its strategic plan and discussions have commenced with experts in the field.

Other areas that may lend themselves to meaningful measurement

Key overall gaps in performance reporting overall include an inability to adequately measure the efficiency and effectiveness impacts of OSR efforts in:

- simplifying and strengthening tax legislation/regulation to make collection more efficient and effective
- education and communication to help shift community attitude and practice towards voluntary compliance
- making it easier for people and businesses to comply with their tax obligations
- helping people and business who owe tax “get it right the first time” with minimal OSR intervention
- building community confidence in the tax system
- optimising levels of automated tax collection overall
- improving performance across all revenue streams not just key revenue streams
- deterring non-compliance.

OSR KPIs and lower level performance measures not yet aligned to Organisational Goals

We expected to find a hierarchy of indicators and measures such that more detailed measures used to drive performance at the business unit level are aligned to KPIs, which in turn are aligned to meeting OSR 2021 goals. This would allow managers working at the business unit level and below to monitor and be accountable for their contribution to:

- meeting divisional KPIs
- achieving OSR’s overall objectives and desired outcomes.

We found that it is difficult to see such a performance measurement hierarchy.

For example, there are more than twice as many KPIs relating to tax collection as there are in the Operations unit’s business plan. Yet this Unit is responsible for most of OSR’s tax collection related activities. In turn, there are more detailed measures for the key tax stream programs which report to the Operations unit. However, we found no clear link between these lower level measures and

- Operations Unit measures
- OSR divisional KPIs
- *OSR 2021* goals

OSR advised that the current suite of KPIs were designed to align to its previous strategic plan and work is underway to better align KPIs with its current plan by the end of 2015–16. Following this improvement in KPI alignment, OSR intends to review lower level performance measures to ensure they also align with the revised KPIs and the new strategic plan.

OSR has already commenced action to address some of these gaps in performance reporting starting with divisional KPIs. For example, work is underway developing KPIs and other performance metrics that measure client error rates to better assess progress in making it easier for people and businesses to comply.

We commend efforts by OSR to review its KPIs and lower-level performance measures.

Given the importance of ensuring managers have the information they need to better manage OSR efficiency and effectiveness, we believe that efforts to improve existing measures and KPIs should settled as soon as possible.

OSR’s work on reviewing its KPIs and measures is discussed further below.

Recommendations

3. OSR should accelerate current efforts to review its current suite of key performance indicators and performance measures to ensure that by 2016–17:

    a) KPIs clearly demonstrate the extent to which OSR is efficient and effective in optimising tax revenue

    b) KPIs are aligned to, and can more clearly demonstrate the achievement of, organisational objectives and goals as per OSR 2021

    c) there is a clearer hierarchy of KPIs and measures to ensure that achievement of lower-level performance measures contribute to the achievement of higher level KPIs and organisation goals

    d) operational, business unit, branch and program plans each have measures to hold managers accountable for performance.

2.3 Governance and accountability in performance management

In examining OSR's performance framework, we have looked at the governance and accountability arrangements that apply to performance measurement and reporting. These can be thought of as the mechanisms that create incentives for good performance and consequences for underperformance.

As the key revenue collection agency for NSW, it is imperative that OSR be able to provide a strong picture of its efficiency and effectiveness.

OSR governance and accountability within the Office of Finance and Services

OSR is a division of the Office of Finance and Services (OFS). The OSR Executive Director is a member of the OFS Executive and reports directly to the OFS Chief Executive Officer.

In reviewing OSR's accountability to OFS for the efficient and effective collection of tax revenue, we found that:

- OFS does not set tax compliance revenue targets for OSR – OSR sets its own compliance revenue targets based on NSW Treasury tax revenue forecasts, which are informed by OSR previous performance.
- There is no one in OFS responsible for the overall monitoring of OSR performance other than the OFS CEO.
- OSR reports monthly to the OFS on tax collection performance, although reporting is minimal and, in our view, inadequate to provide a credible impression of efficiency and effectiveness. Only four measures are reported:
    - cost to collect $100 tax
    - percentage of payments received electronically (Tax)
    - percentage of revenue received on time from monthly lodgers
    - collectable debt as percentage of revenue collected (Tax)
- The OSR Executive Director is directly accountable to the OFS CEO by way of the former's performance agreement. However, the key indicators in this agreement are OSR's divisional KPIs, which we have found to have some limitations.
- OFS Internal Audit Unit conducts an extensive program of audits at OSR annually and these are reported to the OFS CEO and Audit & Risk Committee.
- OFS Corporate Risk assists OSR with risk management and includes regular reporting on risk status to the OFS Audit and Risk Committee. Briefing papers on risk status are provided to the Chief Executive, Chief Financial Officer and Deputy Secretary, Corporate Services.

While these arrangements seem adequate, there is no overarching formalised framework agreement that sets out these roles, responsibilities and expectations of each party. This could be a useful instrument for adding certainty to these arrangements.

There is also scope to improve the meaningfulness of OSR monthly management reporting to OFS by reviewing the existing suite of KPIs to ensure that the information reported to OFS provide a clear impression of how efficiently and effectively OSR is collecting tax.

There is limited external accountability for tax revenue administration

OSR describes itself as "NSW's principal revenue management agency, fairly administering revenue for and on behalf of the people of NSW". However, there is limited information made available to the Government and Parliament, or the public on the efficiency and effectiveness of NSW tax revenue administration. Key tax-related measures reported to government and the public are show in Exhibit 2.3 below.

This information does not adequately demonstrate the efficiency and effectiveness of tax administration to the NSW Government, Parliament or the people of NSW.

Given the importance of OSR's taxation collection to the State budget, and in turn to the services provided to NSW residents, we expected to see more robust levels of accountability and transparency around how well OSR is carrying out its tax administration role.

We found that OSR's current annual reporting compares unfavourably with the detailed and informative reporting it undertook under previous governance arrangements with NSW Treasury.

As a division of OFS, OSR's annual reporting to Parliament and the community is limited to around two pages of OFS' annual report. As indicated above, very few performance measures are reported.

In New South Wales, it is a statutory requirement that agencies, where practicable, include in annual reports:

> '…qualitative and quantitative measures and indicators of performance showing the level of efficiency and effectiveness' (*Annual Reports (Departments) Regulation 2010*).

In our view, the public reporting of OSR's performance fails to satisfy the intent of this requirement.

Knowing whether OSR operates efficiently and effectively is essential to determining whether it is delivering the "community value and contemporary service" referred to in OSR's vision statement. Without strong, transparent and publicly reported performance measures, the value for money provided by OSR may be uncertain to establish. This is particularly problematic in an era of contestability for government service provision.

Exhibit 2.3 Performance measures externally publicly reported

OFS Annual Report 2013–14
• *Cost to collect $100 tax*
• *Percentage of payments received electronically(tax)*
• *Percentage of revenue received on time from monthly lodgers*
• *Client Satisfaction Survey- Satisfied with OSR services*
• *Collectable debt as a percentage of revenue collected (tax)*
Budget paper 3 Service measures
• *Percentage of payments received electronically*
• *Cost to collect $100 tax*
• *Percentage of telephone calls answered within 2 minutes*
• *Financial Indicators: Total expenses excluding losses*
Reports to Treasury
• *Daily revenue reports tracked against Treasury forecasts*

Internal accountability mechanisms

We examined internal governance arrangements in place to hold OSR management accountable for efficient and effective tax administration.

OSR has a culture of monitoring activity and workflow, as demonstrated in its comprehensive governance mechanisms. OSR has an extensive range of governance forums, each supported by their own metrics. Key governance mechanisms are shown below in Exhibit 2.4.

The value of these mechanisms, at least in regard to providing insights on efficiency and effectiveness, depends on the quality of performance information used for these mechanisms.

Most of the mechanisms draw their performance information from OSR's suite of divisional KPIs, as well as operational metrics.

For example, the key measures reported to the Corporate Management Forum (CMF) meeting are:

- divisional KPIs
- financial measures examining variance from cost budgets
- other performance measures sourced from key business unit and program level performance measures across different areas of the Operations Unit.

Given our overall finding that divisional KPIs do not adequately demonstrate efficiency and effectiveness, we believe that accountability mechanisms are therefore compromised. Accountability mechanisms need better information on tax collection efficiency and effectiveness if they are going to hold managers to account for performance in this area.

OSR's work to review existing KPIs and measures should help to improve the effectiveness of its current governance mechanisms.

Exhibit 2.4 Key internal governance and reporting mechanisms within OSR

- OSR fortnightly Director's Meeting led by the Executive Director to monitor and review strategic and operational issues.
- A Finance Committee oversees operational financial matters and budgetary reviews and is a standing committee of the abovementioned Directors meeting
- Monthly Corporate Management Forum attended by directors and their direct reports to review operational and strategic issues, track the achievement of the operational plan, and monitor divisional KPIs
- A Business Metric Committee which meets monthly to promote cross-business unit director discussion.
- A Portfolio Governance Board which monitors key projects that OSR considers important in helping to meet strategic plan goals
- An Enterprise Project Management Office which coordinates the Portfolio governance board and meets monthly to discuss issues around;
  - whether OSR is committing to the right projects at the right time and whether decisions to proceed are made with a clear understanding of cost, risks and impacts
  - the internal evaluation of projects and the success of those projects in meeting desired outcomes
- The achievement ERC savings targets
- Performance agreements for all executive level management
- Monthly Operations Unit management Reports
- Monthly Operations Unit Compliance Revenue reports to hold managers accountable for driving improved efficiency and effectiveness.

Recommendations

4. OSR should enhance its governance and accountability arrangements with the Office of Finance and Services through:

   a) a framework agreement with the Office of Finance and Services that formalises and clarifies expectations, roles and responsibilities of each party, including to ensuring efficiency and effectiveness in tax collection

   b) improving the quality of monthly OSR management reporting to OFS with key performance indicators which demonstrate OSRs efficiency and effectiveness in tax collection.

5. OSR should publish more performance information publicly about its efficiency and effectiveness, such as in the Office of Finance and Services annual report or on its own website.

2.4 Continuous improvement in the OSR performance framework

OSR reviews its KPIs annually in consultation with key managers. This is to ensure that KPI target levels are appropriate and to ensure that the KPIs remain relevant to achieving organisational goals.

OSR's strategic plan, *OSR 2021*, has recently been finalised following extensive consultations with OSR management. OSR is also conducting a major review of KPIs. The current suite of divisional KPIs were the result of a review of the KPIs established for 2013-14. An interim assessment of those KPIs was conducted, where obvious changes to align to *OSR 2021* were made and gaps identified.

Working with key management in workshops, OSR examined the extent to which current indicators cover the desired outcomes and strategies of *OSR 2021*. As a result of this gap analysis, OSR identified a suite of between 13 and 16 new indicators for trialling. It was agreed that the new KPI trial would be conducted during 2014–15, ready for formal adoption in OSR's 2015–16 KPIs.

Once the divisional KPIs are trialled and accepted, the next phase will be to ensure that the business unit performance measures align to *OSR 2021*. Currently, business unit plans, such as the Operations Unit plan, do not have a comprehensive suite of performance measures. This will be addressed once the trial suite of KPIs have been tested and a revised suite of OSR Divisional KPIs is agreed for 2015–16.

While indicators are reviewed annually there has not been significant changes to indicators over the last 4 years.

While continuous improvement taken by OSR is to be commended, there is room for improvement.

One observed limitation is that KPI review efforts are mostly based on internal consultation and consultation with other jurisdictions who, we are advised, do not appear to be much further advanced in this area.

Such consultation is good practice. However, better practice is to combine this consultation with broader international research of measures used by other revenue collection agencies nationally and internationally. We found no evidence of such research being conducted.

OSR is pursuing valuable initiatives, including plans to undertake tax gap analysis, work on improving compliance effectiveness measures and the previously described work to revise the current review of existing KPIs.

Given the importance of this work in helping OSR to better assess its own performance and in improving overall OSR accountability, the Audit Office is of the view that greater priority and urgency is needed to ensuring planned changes in this area happen within the next 12 months.

3. Can it be shown that efficiency and effectiveness performance standards for the Office of State Revenue have been met or progress has been made?

In section 2, we reported on the adequacy of OSR's performance framework. We found that there is scope to improve the framework to provide clearer evidence of the OSR's efficiency and effectiveness.

In this section, we look at what the existing evidence – in the form of performance data and qualitative evidence – actually tell us about OSR's performance.

There is some evidence that the Office of State Revenue has made progress toward improving its efficiency and effectiveness.

While the performance framework can be improved, the results achieved in existing performance measures can be benchmarked against OSR's historical performance, as well as against other revenue collection agencies. This benchmarking suggests that the OSR has become more efficient and effective in a number of areas, although this is not consistent.

The OSR can demonstrate a number of initiatives that are likely to have contributed to improved efficiency and effectiveness.

3.1 OSR's results against performance measures

In looking at OSR's performance, we sought to compare its results against:

- its own single year targets
- its own performance over time, through a time series
- the performance of revenue collection agencies in comparable jurisdictions.

Each of these approaches can have substantial limitations. Some measures may not be comparable over time due to policy changes or the unavailability of data, while comparisons between jurisdictions can be imperfect due to different policy, legislative and administrative arrangements for tax collection.

These challenges hinder the extent to which any one performance measure can be taken as being comprehensive. Instead, gaining an impression of OSR's efficiency and effectiveness requires viewing a full suite of measures.

Publicly available performance information

Since becoming a division of the Office of Finance and Services, OSR provides relatively little performance information publicly.

Some information is provided on the 'Data and statistics' page of OSR's website. This is limited to high-level aggregate data about types of revenue collected.

While it is high-level, this data does provide some helpful, although short, time series.

Data is also published on actual versus budgeted revenue, although this is limited to just two years. As shown in Exhibit 3.1 below, for the three leading tax streams, revenue outstripped budgeted on three occasions over the two years. In both years, actual land tax was less than budgeted. Actual versus budgeted revenue is not a KPI in OSR's strategic plan.

Exhibit 3.1 Difference in actual and budged tax revenue, 2011–12 and 2012–13

Tax stream	2012–13	2011–12
Duties	2.6%	2.2%
Payroll	-1.1%	1.6%
Land Tax	-7.4%	-3.9%
Other	1.9%	3.3%
Total	-0.7%	1.0%

Source: http://www.osr.nsw.gov.au/sites/default/files/file_manager/revenue_earned_actual_v_budget.pdf

Other summary information is provided in various pages on OSR's website. For example:

- The 'Compliance' page includes a summary of compliance activities for the current year. It includes the numbers of audits conducted in 2013–14 and the additional revenue identified by those audits.
- Data is also published on separate web pages for five previous client satisfaction surveys.

This performance information is not presented with any comparison to a benchmark, target, or in a time series.

Client satisfaction survey performance measures on experiences with OSR

Exhibit 3.2 collates the client survey data from OSR's website into a time series. In addition to the eleven measures listed, there is an additional measure on overall satisfaction with OSR.

For all respondents, satisfaction rose from 78% in 2010 to 89% in the August 2012 survey. Satisfaction with OSR services is a divisional KPI and has a target of 86%.

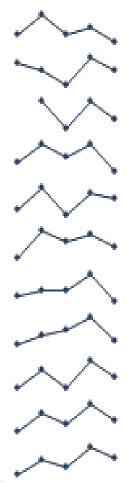
Other client satisfaction matters that are also KPIs are:

- *Courteous and professional staff* – 2014–15 target ≥ 80%
- *Staff give reasons for decisions* – 2014–15 target ≥ 75%

Across all measures, client satisfaction with OSR is generally high, including in comparison to results for similar bodies in other states and territories.

Exhibit 3.2 Client satisfaction with OSR

Client satisfaction survey – performance measures	2010	2011	2012	2012	2013
Website provide required information	85	88	85	86	84
Website easy to use	83	82	80	84	82
Self-service options meet needs		84	81	84	82
Phone services easy to use	72	76	73	76	70
Payment methods meet needs	83	87	82	86	85
Courteous and professional staff	82	89	86	88	85
Staff give reasons for decisions	72	73	73	76	71
Problems resolved in timely manner	73	75	76	79	74
Provides sound advice and information	77	82	77	85	80
Staff are knowledgeable and competent	79	84	81	87	82
Information from OSR is consistent.	77	82	80	87	83



Source: OSR benchmarking reports. Two surveys were run in 2012 in March and August.

Results publicly available in annual reports

Since 2010–11, the OSR's annual reporting to Parliament has been through short contributions within OFS' annual report. Exhibit 3.3 below collates the performance information included in those reports.

In the most recent annual report (2012–13), five KPIs were reported:

- *Overdue debt to tax collected (%)*
- *Cost to collect $100 tax*
- *Payments received electronically (%)*
- *Returns on time from monthly lodgers (%)*
- *Client satisfaction with OSR services (%)*

As shown in Exhibit 3.3, OSR has some success in achieving its targets. However, as discussed in section 2.2, we are not convinced that these KPIs provide a sound reflection of OSR's efficiency or effectiveness in collecting one-third of the State's revenue base.

Exhibit 3.3 OSR KPIs included in Office of Finance and Service's annual reports

Performance measure reported	Year						
	2007–08	2008–09	2009–10	2010–11	2011–12	2012–13	2013–14
				OSR included in Office of Finance and Services annual report			
Overdue debt to tax collected (%)	0.97	1.54	1.4	1.54	1.31	1.3	1.1
Cost to collect $100 tax ($)	See Exhibit 3.4 below						
Payments received electronically (%)	66	78	88	90	91	91	90
Returns on time from monthly lodgers (%)	–	–	–	–	88	96	97
Client satisfaction with OSR services (%)	–	–	–	–	88	88	88
Revenue to budget (%)	107	107	106	100	101	–	–
Revenue identified through compliance ($mill)	286	318	317	328	299	–	–
Sick leave taken per FTE (hours)	–	–	–	–	53.7	–	–

Target met   Target not met

Note: All results and targets are sourced from OFS annual reports from 2010–11 to 2013–14. Results for 2007–08 to 2009–10 were included in the 2010–11 OFS annual report.

'–' Data were not published that year.

Performance over time in the cost to collect $100 tax

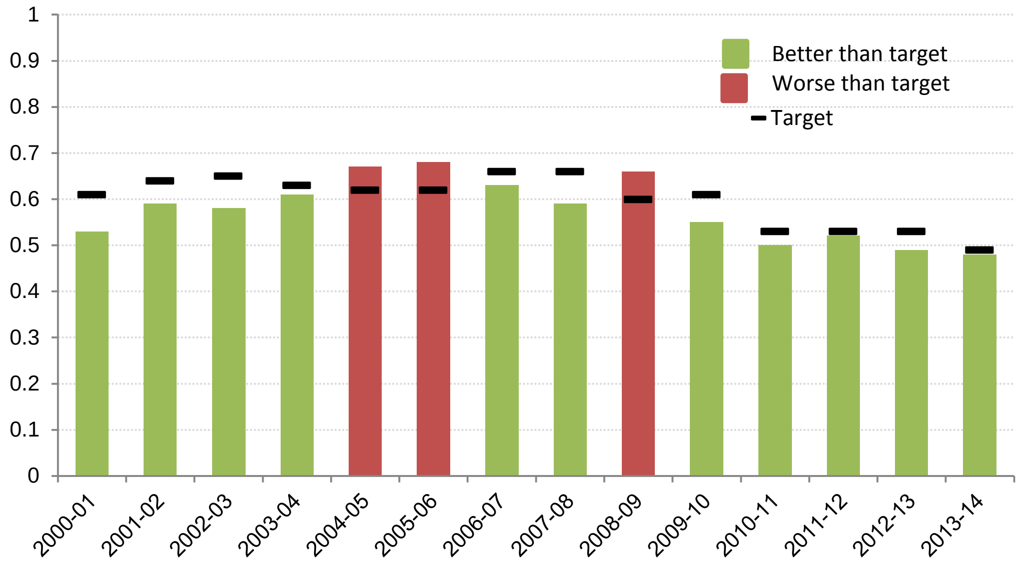
In section 2, we noted a range of limitations with the performance measure *cost to collect $100 tax.* During the audit, the majority of revenue agencies we spoke to agreed that it was an imperfect measure, although none argued that it was of no value. Instead, it was suggested that this indicator should be treated as one of a suite of relevant indicators, and not considered in isolation.

Exhibit 3.4 shows actual and targeted costs to collect for 2000–01 to 2013–14.

Over this period, the cost varied between around 50 cents to around 70 cents per $100 of tax collected. There appears to be an overall downward trend in this result since 2005–06, except for an apparent outlier spike in 2008–09.

The OSR's cost to collect was better than the target in 11 of the 14 years.

Exhibit 3.4 Cost to collect $100 taxation, 2000–01 to 2013–14



Source: OSR, unpublished.

While the cost to collect $100 of tax has fallen since 2005–06, further analysis would be required to establish the extent to which this was driven by economic growth and other factors beyond OSR's control. Increases in payroll tax through economic growth and stamp duty on real estate are likely to have outstripped the cost pressures on OSR's operations.

A better way to assess efficiency, and a related concept, productivity, of OSR's tax collection needs to consider the relationships between input (OSR staff primarily responsible for tax collection) and output (the work that those OSR staff do).

The following section explores one possible method of assessing efficiency and productivity of OSR's tax collection. The assessment utilises data from OSR and publicly available information from the Australian Bureau of Statistics.

A better way to measure efficiency and productivity to the cost to collect $100 tax

We have used a simple method to illustrate what could be an improved way for measuring efficiency using the *cost to collect $100 tax*. This highlights that with further analysis, OSR could derive defensible measures of efficiency and productivity.

Our method deflates nominal costs to arrive at a real cost trend over time, and adjusts nominal revenue to remove economic effects outside OSR's control. This method usually also takes into account quality in measuring efficiency and productivity, although we did not have a suitable quality indicator for revenue collection – see Appendix 2.

As an example, we have adjusted nominal payroll tax revenue to remove the effects of NSW economic growth, which has likely affected payroll tax collection. Nominal duty revenue has been adjusted to remove the effects of large rises in Sydney property prices. Nominal costs have also been adjusted. The indices used to deflate the data are shown in Appendix 3.

OSR may be able to refine these economic and wage growth adjustments using its detailed internal data and other economic data.

As can be seen in Exhibit 3.5:

- from 2008–09 to 2012–13, the adjusted cost to collect payroll tax increased less than the nominal cost – from 30 cents to 36 cents per $100 – this likely reflects OSR's enhanced compliance activities in recent years, which successfully increased revenue although at higher than usual cost
- from 2010–11 to 2012–13 (the years cost data is available for duties), the adjusted cost to collect duties decreased the same in real terms as nominal terms.

Exhibit 3.5 Cost to collect $100 tax, nominal and adjusted

Payroll tax					
	2008–09	**2009–10**	**2010–11**	**2011–12**	**2012–13**
Nominal	0.30	0.34	0.34	0.37	0.38
Adjusted	0.30	0.33	0.32	0.34	0.36
Duty					
	2008–09	**2009–10**	**2010–11**	**2011–12**	**2012–13**
Nominal	–	–	0.30	0.30	0.22
Adjusted	–	–	0.30	0.28	0.22

Source: OSR, unpublished. Note: '–' data were not available.

We have also developed a related tool for measuring productivity – the measure of physical outputs to physical inputs. For OSR, we have defined outputs as being adjusted revenue. A better output measure would relate to volume of transactions, weighted by costs. We have defined the physical input as Full Time Equivalent staff working on tax collection.

Using this approach, we have calculated a 'productivity score'. Exhibit 3.6 shows that from 2008–09 to 2012–13, the physical productivity of payroll tax collection has deteriorated from a score of 43 to 31, whereas the physical productivity of collecting duties has improved over the three years for which the cost to collect is available.

Exhibit 3.6 Productivity score for collecting payroll tax and duty

	2008–09	2009–10	2010–11	2011–12	2012–13
Payroll tax	43	37	34	33	31
Duties	–	–	34	39	48

Source: OSR, unpublished. Note: '–' data were not available.

Performance over time in Unregistered Payroll Tax compliance

Payroll tax is the largest contributor to OSR's revenue collection, providing around $8 billion in 2013–14. Payroll tax compliance projects are also the largest sources of compliance revenue. Payroll tax compliance returned $168.4 million in 2013–14, exceeding the budgeted revenue of $150 million. The largest contributor to this revenue was the Unregistered Clients project, earning $45.6 million against budgeted revenue of $36 million.

Considerable attention has been given in recent years to better targeting of businesses that may be required to register and pay payroll tax. How frequently audit cases find revenue results is called the 'strike rate'. The strike rate was 97% in 2013–14, meaning that almost every unregistered payroll tax audit resulted in unpaid payroll tax liability being identified.

On the face of it, this improved strike rate is a considerable success and indicates that there is considerable scope to collect more tax at minimal cost to OSR.

Exhibit 3.7 shows that from 2006–07 to 2013–14:

- the strike rate for unregistered payroll tax audits rose from 55% to 97% (green line)
- payroll tax identified as payable fell from $48.5 million to $45.6 million (column graph)
- payroll tax collected from audits fell from $32.3 million to $29.7 million (green shading)

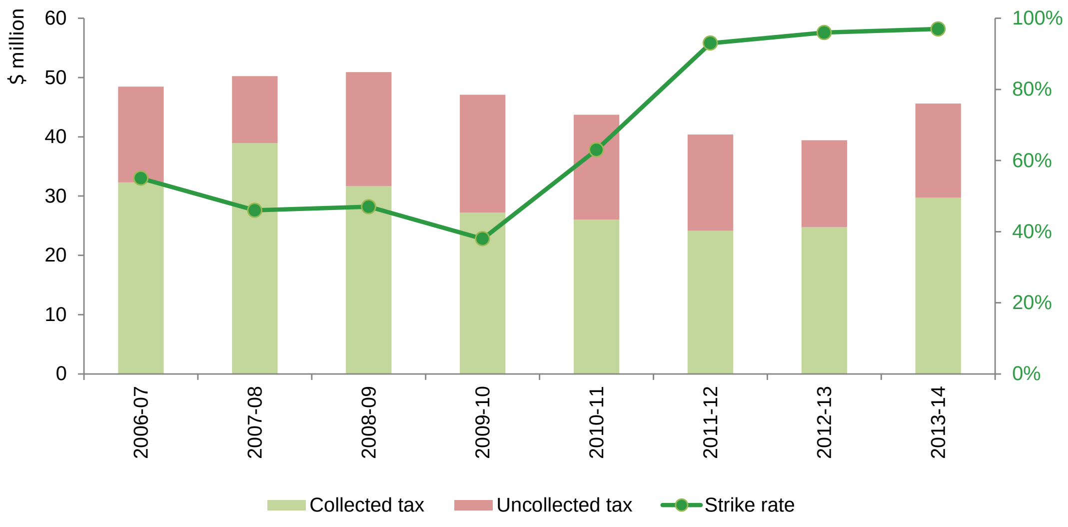
The red shading shows the gap between how much payroll tax was identified and how much was subsequently collected. From 2006–07 to 2013–14, this gap shrunk by only $0.3 million.

Also over this same period:

- the number of unregistered payroll tax audits fell from over 3,500 to 1,699
- average revenue collected per audit rose from $16,585 to $18,039, although after taking inflation into account, this is a fall in real terms
- the years of tax assessed as being outstanding fell from 2.2 years to 1.8 years.

Further calculations would be required to determine whether the improved strike rate has led to improved efficiency in these audits, although it appears that the overall fall in tax collected suggests a worse outcome for the State's revenue base.

Exhibit 3.7 Audit revenue and strike rates for Unregistered Payroll Tax



Source: OSR, unpublished

How well does OSR perform against others?

KPMG conducts an annual assessment of the performance of revenue office jurisdictions throughout Australia. This information is used by the Business Practices Committee (an inter-jurisdictional committee sponsored by the Commissioners of State Revenue) to facilitate the sharing of information, identify best practice and drive performance improvement.

The Business Practices Committee has been undertaking this benchmarking since 2000–01, focusing on seven KPIs, each comprising a suite of measures. These KPIs do not exactly align with the OSR's divisional KPIs, although some are conceptually related or measure more detailed activities.

The two tables below show where the inter-jurisdictional benchmarking has identified NSW as being a better and worse performer.

Exhibit 3.8 Measures where OSR is among the best performers (ranked as a top performer)

Performance measure	NSW	Median
Total revenue per Full Time Equivalent Employee ($ million)	$39.35	$26.85
Percentage of stamp duty documents self-assessed	86%	85%
Number of stamp duty phone enquiries per 100 stamp duty documents	13	21
Number of tax phone enquiries per 100 taxpayers	28	38
Number of electronic payroll tax enquiries per 100 payroll taxpayers	70	47
Percentage of land tax payment transactions received electronically	97.6%	86%
Percentage of land tax payment transactions received manually	2.3%	15.1%
Helpfulness of state revenue office staff	85%	83%
Overall quality of service satisfaction	87%	86%

Source: OSR, unpublished.

Exhibit 3.9 Measures where OSR is among the lowest performers

Performance measure	NSW	Median
Average debt over 12 months overdue as a percentage of overdue debt	24.8%	23.7%
Average telephone queuing time (minutes)	0.95	0.61
Percentage of calls abandoned	3.5%	3.0%
Number of electronic stamp duty enquiries per 100 stamp duty documents	1	2
Number of electronic tax enquiries per 100 taxpayers	6	7
Percentage of duties transactions received electronically	13.5%	22.6%

Source: OSR, unpublished.

3.2 What the OSR has done to improve efficiency and effectiveness

The focus of this audit is the performance framework used by OSR to assist its internal management and to promote transparency and accountability for its performance. In our discussions with OSR and other similar bodies, and from a review of literature, reliably and defensibly measuring efficiency and effectiveness in revenue collection remains a work in progress. This is the case in Australia and internationally.

This is partly because, as was put to us during this audit: “not everything lends itself to measurement.”

Accordingly, we have also noted a range of initiatives and activities beyond those captured in KPIs that may help to form a defensible impression of OSR’s efficiency and effectiveness. We formed the view that there is a depth of expertise and experience in OSR that has contributed to good results across a range of activities, although these are not always well captured by KPIs. As one interviewee noted: “perhaps we are not always very good at talking about our successes”.

The items below were not individually and comprehensively performance audited and so should be treated as being indicative only.

- OSR has impressive results in its staff survey, with results that are consistently better than the average across its cluster. This includes in areas relevant to this audit, like whether staff feel they have sufficient information to do their jobs well and whether the agency is innovative.
- OSR has had success with its extended tax compliance program, under which it obtained an additional $20.36 million over 4 years through the Expenditure Review Committee (ERC) of Cabinet. In 2013–14, this additional compliance resource led to $75 million in additional revenue identified, easily exceeding the $37 million target. In 2014–15, OSR received further funding of $36 million from the ERC to 2017–18 to identify an additional $247.3 million in compliance revenue.
- OSR has had success in trialling behavioural insights techniques to improve client responsiveness. A 2013–14 land tax legal notice trial resulted in payment response rates of 39% compared to a benchmark of 27% for letters that did not apply behaviour insights.
- The Analytics and Intelligence team supporting the Operations Unit articulated a range of current or planned initiatives that would drive efficiency and effectiveness, including improving case management and selection, and proposed improvements to data management.
- As set out in section 2 of this report, OSR has a sound framework of management and operational committees. Managers and executives with whom we spoke indicated that these committees were important to monitoring and decision making. We noted that these committees were supported by detailed operational data.
- There was evidence of sound project evaluation practices in OSR, with structured processes in place that ensure projects remain in scope, on budget and on time. There was a clear impression of appropriate discipline to project management in OSR.

Appendices

Appendix 1: Response from Office of Finance and Services

NSW GOVERNMENT | Finance & Services

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Mr Tony Whitfield
Auditor-General
The Audit Office of New South Wales
GPO Box 12
SYDNEY NSW 2001

Your Ref PA6551
Our Ref EXEC15/131

Dear Mr Whitfield

Performance Audit – Efficiency and effectiveness in tax collection: Office of State Revenue

Thank you for providing me with a copy of the final report from the above performance audit.

Please find attached a formal response from the Office of Finance and Services to be incorporated into the published report.

I note your intent to table the report on 25 June 2015.

Yours sincerely

Anthony Lean
Acting Chief Executive 19 JUNE 2015

General Comments

OSR acknowledges the findings of the Auditor-General's report and broadly accepts the opportunities identified to improve the efficiency and effectiveness of our tax collection functions. We are pleased to see the Audit Office recognise that OSR has "a wealth of experience and expertise in revenue collection, and is able to demonstrate success across a range of activities". And, it was reassuring that the Audit Office observed that "While other audits of performance measurement have linked weakness in performance frameworks to a lack of managerial and executive commitment, we did not find this with OSR".

The report endorses the work already underway or identified in our strategic plan, OSR 2021. This includes our commitment to initiate a tax gap analysis and the work already underway to improve our KPIs and their linkage to OSR 2021.

The difficulties in assessing effectiveness and efficiency of tax revenue administration are not unique to OSR but a problem for all revenue agencies, nationally and internationally, as recognised in the report. We note the 2014 OECD guide on measuring tax compliance outcomes noted that "there is no single 'right' set of measures and revenue bodies will need to decide what measures they need to manage their organisation."

While broadly accepting the recommendations contained in the report there are a number of aspects of the report that, in our view, require clarification so that it presents a clear and accurate picture of OSR's performance. When commenting on the draft report OSR previously raised these issues with the Audit Office.

It is not our intention to list all of these matters in this response but some of the more material issues are outlined below.

Operational Context

The performance audit focused on the tax revenue operations of OSR, however these operations are part of a much broader organisation. OSR is responsible for four lines of business – tax revenue collections, fines administration, payment of grants and benefits and debt management.

Exhibit 1.1 on page 5 of the report, labelled "Total OSR revenue and expenditure, 2005-06 to 2013-14", is misleading. The revenue collection figures shown in the exhibit are accurate tax revenue collections but the expenditure figures shown are for all OSR expenditures, not just tax collection.

The expenditure figures shown include expenditures on all four lines of business while the revenue collections relate only to tax collections. This exhibit is misleading because the reader could interpret the chart to be saying that in 2013/14, for example, OSR collected around $21.4 billion at a cost of around $238.5 million. This is not correct. The actual cost to collect $21.4 billion was $111.7 million. The balance of expenditures related to fines administration, payment of grants and benefits and debt management.

Note: *Subsequent to receiving this response the Audit Office has revised Exhibit 1.1*

Productivity Calculation Methodology

In section 3 of the report, under the heading "A better way to measure efficiency and productivity to the cost to collect $100 tax", the report attempts to calculate "defensible measures of efficiency and productivity". The detailed workings for the calculations are contained in appendix 3 of the report.

The methodology "deflates nominal costs to arrive at a real cost trend over time, and adjusts nominal revenue to remove economic effects outside OSR's control". It has been applied to arrive at adjusted revenue, adjusted cost to collect and a productivity score for collection of payroll tax and duties. The methodology suggests that productivity for payroll tax collections has decreased from 43 in 2008/09 to 31 in 2012/13 while productivity for duties has increased from 34 in 2010/11 to 48 in 2012/13.

It is OSR's view that the methodology proposed in the report should be reviewed. Taking payroll tax as an example, OSR makes the following observations:

- the methodology proposes NSW state final demand as the deflator for payroll tax revenue. According to the Australian Bureau of Statistics (ABS), state final demand measures the total value of goods and services that are sold in a state to buyers who wish to either consume them or retain them in the form of capital assets. It excludes sales made to buyers who use them as inputs to a production activity, export sales and sales that lead to accumulation of inventories.

- OSR considers that NSW final state demand should not be a deflator for payroll tax revenue receipts over time. The key drivers of payroll tax revenues are changes in the employment and average weekly earnings. Care should also be taken as payroll tax is paid by less than 10% of employers in NSW there is the possibility that these official measures, which are representative of all employers in NSW, may not accurately reflect changes in employment or wage levels in employers liable to pay payroll tax.

- The proposed methodology also needs to take account of changes in the tax-free threshold and the rate of tax imposed.

Changes in either the rate or the threshold will have a material effect on revenue. From 2008/09 to 2012/13, the period covered by the methodology, the payroll tax rate reduced from 6.00% on 1 July 2008 to 5.45% on 30 June 2013, a reduction of 9.17%. Over the same period the threshold increased from $638,000 to $750,000, an increase of 17.55%.

The combined impact of a 9.17% reduction in rate and a 17.55% increase in threshold would have had a serious dampening effect on payroll tax revenues over the period. These should be reflected in the methodology and the productivity score calculated.

International Comparisons

On page 23, when commenting on OSR's performance framework, the report observes that " … better practice is to combine this consultation with broader international research of measures used by other revenue collection agencies nationally and internationally. We found no evidence of such research being conducted."

It is not correct to say that OSR does not conduct research into latest practices with the ATO and overseas revenue administrations. OSR keeps a close watch on latest developments within Australia and overseas in relation to all aspects of revenue administration, including performance management.

OSR maintains a close cooperative relationship with the ATO and does regular research into international developments through organisations such as the OECD, IMF and World Bank. Where appropriate, OSR factors the outcomes of this research into our strategic and operational activities.

The following table outlines our specific responses to individual recommendations made in the report.

Recommendation	OSR Response	Comment
1. OSR should clarify its definition of effectiveness so that the concept is not restricted by "doing more with the same resources or less".	Accepted	Within OSR's value-for-money (VfM) framework, effectiveness is defined as "... the extent to which a service, process or project fulfils its intended purpose. It relates to the achievement of organisational goals and objectives". The reference to "doing more with the same resources or less" was only ever used as an example of effectiveness, however we acknowledge the example should have been cited under efficiency. We will refine examples for "effectiveness" as part of our planned revisions to the VfM Framework.
2. In order to better demonstrate OSR's overall effectiveness in collecting tax revenue, OSR should: a) work in collaboration with NSW Treasury and other expert bodies to progress tax gap analysis by the end of 2016-17	Partially accepted	OSR has commenced work on tax gap estimation. A request for proposal has been issued to three organisations to commence a pilot study with payroll tax. The outcomes of the pilot will inform and shape the future of tax gap estimation within OSR. Expansion of the work to cover the full NSW payroll tax base will depend on the viability of the pilot study. It is worth noting that this study will, to the best of our knowledge, be unique in the Australian environment, and possibly in the world, for this type of tax. Not all revenue streams will warrant investment in tax gap estimation. OSR will formulate an approach, in conjunction with NSW Treasury, to determine where to allocate resources and effort to estimate tax gaps with the following guiding principles: • taxes generating the most revenue will be considered priorities for tax gap estimation. Lower annual revenues for some tax types could make it uneconomical to consider tax gap research • some tax designs have sufficient controls built into their design (e.g. poker machine taxes are controlled through an auditable network of licenced machines across the State) suggesting tax gap estimation will not be required for these types of taxes • some revenue streams may have drivers that are difficult to assess with sufficient reliability to warrant the effort. In conjunction with NSW Treasury we will assess the merits of pursuing tax gap assessment for each revenue stream separately and focus our efforts only on areas where it is agreed that a material improvement to revenue potential and compliance might result.
b) build a stronger evidence base for setting compliance revenue targets and modelling different resource levels to optimise tax revenue collection	Accepted	The realities of the budget process are that OSR, like other agencies, does not set its own operating budget without oversight. OSR has requested and received supplementation from Government from time to time based on clearly defined metrics for revenue collected through compliance activities. We will continue to ensure our compliance revenue estimation methodology is robust and caters for different revenue scenarios by modelling outcomes for different resourcing levels.

Efficiency and Effectiveness in Tax Collection | OSR | Performance Audit | Management Response | June 2015

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Recommendation	OSR Response	Comment
c) ensure that compliance revenue targets incorporate the analysis performed under paragraphs a) and b)	Accepted	Agreed.
3. OSR should review its current suite of key performance indicators and performance measures to ensure that by 2016-17: a) KPIs clearly demonstrate the extent to which OSR is efficient and effective in optimising tax revenue b) KPIs are aligned to, and can more clearly demonstrate the achievement of, organisation objective and goals as per OSR 2021 c) there is a clearer hierarchy of KPIs and measure to ensure that achievement of lower-level performance measures contribute to the achievement of higher level KPIs and organisation goals d) operational, business unit, branch and program plans each have measures to hold managers accountable for performance	Accepted	OSR agrees with this recommendation and has a process already underway to review its current suite of KPIs and align them with our strategic plan, OSR 2021. However, we believe our current performance management framework has served a purpose in providing the OSR Executive and business units with a sound basis for evaluating the effectiveness and efficiency of the organisation across different tax revenue streams. This in turn enables effective decision-making regarding priorities, resource allocation and risk management. While our current performance management framework provides a reasonable view of performance, we recognise a number of areas where it can be improved. This includes the potential to incorporate the outcomes from the tax gap research and to better align the framework with our strategic plan, OSR 2021. Action is underway to strengthen this area. We agree that the specific focus areas identified in this recommendation will strengthen our performance management framework and will be incorporated as clear design criteria for redesign work underway. While we acknowledge the opportunities for improvement identified in the report, we believe that: • a broad range of measures are already in place across the tax programs to provide an understanding of performance across a range of effectiveness and efficiency considerations • these measures receive a high degree of attention from the Executive Director and OSR leadership team through various governance and management processes • these measures are being used to drive operational and planning decisions at the divisional, business unit and branch level. We also note that OSR's current range of measures allows us to effectively compare performance with other revenue collection agencies. The redesign work will take account of the need to continue to benchmark our performance against other revenue agencies.

Recommendation	OSR Response	Comment
4. OSR should enhance its governance and accountability arrangements with the Office of Finance and Services through: a) a framework agreement with the Office of Finance and Services that formalises and clarifies expectations, roles and responsibilities of each party, including to ensuring efficiency and effectiveness in tax collection b) improving the quality of monthly OSR management reporting to OFS with key performance indicators which demonstrate OSRs efficiency and effectiveness in tax collection.	Partially accepted	OSR is not a separate legal entity and the need for a separate agreement over and above the Executive Director's performance agreement remains unclear. That said, OSR will draft a framework agreement for consideration by the new Secretary of the Department of Finance, Services and Innovation (DFSI) by 30 September 2015. We agree with the recommendation to improve the quality of OSR management reporting and will discuss it with the new Secretary of DFSI, when appointed, and agree the necessary changes. As a division of OFS we note that reporting standards for OSR are primarily a matter for the DFSI leadership to determine.
5. OSR should publish more performance information publicly on its efficiency and effectiveness, such as in the Office of Finance and Service annual report or on its own website.	Accepted	OSR takes evidence based performance transparency and accountability very seriously. Our organisational culture is at ease with transparency and proud of achieving good performance. OSR will publish a "Year in Review" document on its website by 31 August each year providing an overview of performance for the previous financial year focusing on efficiency and effectiveness.

Appendix 2: About the audit

This audit examined the efficiency and effectiveness of tax collection by the Office of State Revenue (OSR), a division of the Office of Finance and Services. It examined efficiency and effectiveness by looking at the performance framework used by OSR to measure and report on its efficiency and effectiveness.

The ability of an organisation to optimise its efficiency and effectiveness is enhanced by the degree to which it has a performance framework that allows it to:

- analyse the value of its various operations and activities in contributing to desired organisational outcomes (effectiveness)
- understand the relationships between resources invested and output/outcomes achieved (efficiency)
- set meaningful objectives, goals standards and targets around the key drivers of organisational efficiency and effectiveness and hold managers at all levels accountable for delivering improved efficiency and effectiveness
- evaluate the success of key programs and initiatives

Scope

The audit examined:

- the agency's overall performance framework and high-level performance measures
- major specific taxation streams to examine how the performance framework extends down through the organisation to divisional managers and line managers. This included the performance measures that apply at each level (and their adequacy to contributing to efficiency and effectiveness), performance data that are available, and how (or if) performance data is used to inform decision making.

Audit exclusions

The audit excluded:

- the impact of legislation and regulation on the OSR
- the efficiency and effectiveness of tax collection for taxpayers
- the efficiency and effectiveness of debt recovery.

Audit approach

To address the above criteria and above focus areas the audit team utilised the following audit procedures.

Interviews with:

- selected managers, teams and individuals at all levels of OSR with responsibility for tax revenue collection related activities.
- selected officers with responsibility for data collection, analysis report compilation, and human resources / development
- officers from selected tax revenue collection agencies at both State and Federal levels
- officers from DFS, Treasury and other key stakeholder agencies

Literature review of:

- better practice performance frameworks/guidance for tax collection, including tax revenue related targets/goals/ benchmarks/standards, key performance indicators, performance measures etc.
- performance benchmarking with comparable tax collection agencies.

Document review and analysis of:

- relevant policy, guidelines and legislation
- relevant planning documents at all organisational levels
- service level agreements
- officer employment/ performance agreements
- routine and ad hoc performance reporting at all levels of the organisation
- evaluations reports
- internal audit plans and reports
- minutes of performance monitoring meetings
- any relevant past reviews/reports (internal or external) examining OSR efficiency and effectiveness/ taxation revenue management, collections etc
- any past reviews and reports on OSRs performance framework for tax revenue collection
- client and staff surveys
- other relevant documents identified during the course of the audit

Agency selection

The Office of State Revenue (OSR) collects almost $20 billion annually for the NSW Government. Despite its crucial role in collecting revenue for the State, it has not been subject to a performance audit for several years, making it timely to conduct this performance audit at this time.

Audit selection

We use a strategic approach to selecting performance audits which balances our performance audit program to reflect issues of interest to Parliament and the community. Details of our approach to selecting topics and our forward program are available on our website.

Audit methodology

Our performance audit methodology is designed to satisfy Australian Audit Standards ASAE 3500 on performance auditing, and to reflect current thinking on performance auditing practices. Our processes have also been designed to comply with the auditing requirements specified in the *Public Finance and Audit Act 1983*.

Acknowledgements

We gratefully acknowledge the co-operation and assistance provided by the NSW Office of State Revenue. In particular we wish to thank our liaison officers and staff who participated in interviews and provided material relevant to the audit

Audit team

Andrew Hayne and Gordon Eastwood conducted the performance audit. Kathrina Lo provided direction and quality assurance. Xin Yin Ooi provided technical assistance.

Audit cost

Including staff costs and overheads, the estimates cost of the audit is $290,000.

Appendix 3: Productivity assessment – compass method

The following assessment is a method devised by the Audit Office to identify productivity trends in public service agencies. The methodology uses both publicly and internal key performance information to identify productivity trends. The methodology consists of two parts:

1. **Productivity trends** – the 'compass' is a tool used to help identify productivity trends. The compass consists of four quadrants:

   First quadrant – this is the region where there is an increase in physical productivity associated with a decrease in quality. In this case we are unable to conclude with certainty the trend in productivity because we are unable to compare the magnitude of changes.

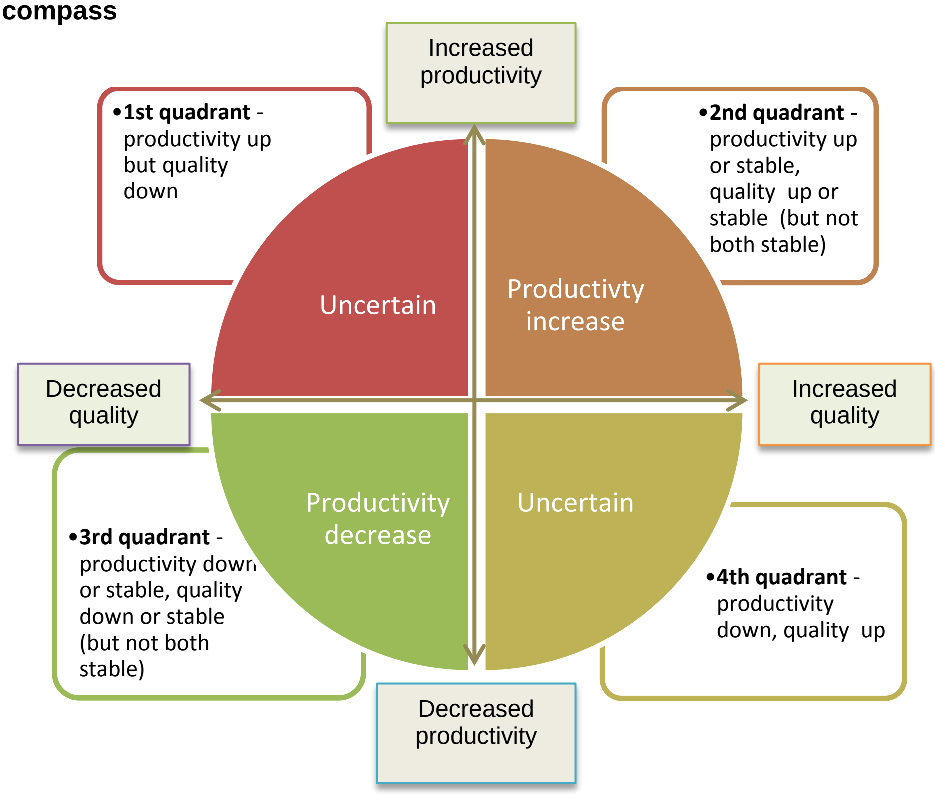
   Second quadrant – this is the region where there is an increase in, or stable, physical productivity associated with an increase in, or stable quality (but not both stable). An agency falling into this quadrant would mean that we can conclude with certainty that overall productivity has increased.

   Third quadrant – this is the region where there is decrease in, or stable, physical productivity associated with a decrease in, or stable quality (but not both stable). In this case we can conclude with certainty that overall productivity has declined.

   Fourth quadrant – this is the region where there is an increase in physical productivity associated with a decrease in quality. In this case we are unable to conclude with certainty the trend in productivity because we are unable to compare the magnitude of changes.

Where both physical productivity and quality are stable over time, then productivity is constant.

Productivity compass



2. **Efficiency trends** – it is also important to understand how productivity trends are related to costs. For this reason efficiency trends are also considered. Efficiency is defined as the average cost per unit of output. Nominal costs are deflated to arrive at the real cost trends over time.

Appendix 4: Indices and data used for calculating efficiency and productivity

Component to assess efficiency	Source data
Revenue from land tax, payroll tax and duties (dollars)	• Revenue data from OSR's financial accounting system (Masterpiece) and annual report results
Cost to collect land tax, payroll tax and duties (dollars)	• Cost to collect data from OSR
Revenue adjustment for economic factors	Land tax and duties: • Residential property price growth calculated from Australian Bureau of Statistics data Payroll tax: • GDP growth calculated from Australian Bureau of Statistics data
Cost to collect adjustment for salary growth	• Growth in average weekly earnings for public sector employees, calculated from Australian Bureau of Statistics data

Component to assess productivity	Source data
Physical output of OSR's staff	Internal OSR data
Full time equivalent of OSR's staff with primary responsibility of tax collection	Full time equivalent by business units from Finance branch of OSR, with non-tax staff taken out. Only two years are available: 2006–07 and 2013–14.

Increases in indices – used to deflate revenue and cost (per year)				
	2009–10	**2010–11**	**2011–12**	**2012–13**
Payroll tax (NSW State Final Demand)	1%	4%	2%	2%
Duties (Sydney residential price index)	14%	6%	-3%	5%
Land tax (Sydney residential price index)	14%	6%	-3%	5%
Cost to collect (Average Weekly Earnings of public sector)	4%	6%	4%	2%

Note: All indices are estimated using data from Australian Bureau of Statistics.

	2008–09	2009–10	2010–11	2011–12	2012–13
Nominal revenue ($m)					
Payroll tax	7,167	7,001	7,235	7,621	7,842
Duties	–	–	5,452	5,521	6,139
Land tax	2,195	2,308	2,294	2,348	2,365
Adjusted revenue ($m)[1]					
Payroll tax	7,167	6,930	6,902	7,151	7,214
Duties	–	–	5,452	5,684	5,997
Land tax	2,195	2,032	1,914	2,016	1,927
Nominal cost to collect ($m)					
Payroll tax	22	24	25	28	30
Duties	–	–	16	17	14
Land tax	52	50	47	47	44
Real cost to collect – base year being 2008–09 ($m)[2]					
Payroll tax	22	23	22	25	26
Duties	–	–	15	14	12
Land tax	52	48	42	41	38
Full Time Equivalent (FTE)					
Payroll tax	165	187	203	216	236
Duties	137	128	134	121	105
Land tax	246	227	205	182	150
Adjusted cost to collect $100					
Payroll tax	0.30	0.33	0.32	0.34	0.36
Duties	–	–	0.30	0.28	0.22
Land tax	2.39	2.34	2.21	2.05	1.97
Productivity score[4]					
Payroll tax	43	37	34	33	31
Duties	30	35	34	39	48
Land tax	9	9	9	11	13

Notes:

1. Revenue dollars are adjusted for economic factors. Base year is 2008–09 for payroll tax and land tax, and 2010–11 for duties.

2. Cost collars are adjusted for wage growth.

3. Efficiency indicator is adjusted revenue divided by real cost to collect.

4. Productivity indicator is adjusted revenue divided by FTE.

'–' Data were not available.

Performance auditing

What are performance audits?

Performance audits determine whether an agency is carrying out its activities effectively, and doing so economically and efficiently and in compliance with all relevant laws.

The activities examined by a performance audit may include a government program, all or part of a government agency or consider particular issues which affect the whole public sector. They cannot question the merits of government policy objectives.

The Auditor-General's mandate to undertake performance audits is set out in the *Public Finance and Audit Act 1983*.

Why do we conduct performance audits?

Performance audits provide independent assurance to parliament and the public.

Through their recommendations, performance audits seek to improve the efficiency and effectiveness of government agencies so that the community receives value for money from government services.

Performance audits also focus on assisting accountability processes by holding managers to account for agency performance.

Performance audits are selected at the discretion of the Auditor-General who seeks input from parliamentarians, the public, agencies and Audit Office research.

What happens during the phases of a performance audit?

Performance audits have three key phases: planning, fieldwork and report writing. They can take up to nine months to complete, depending on the audit's scope.

During the planning phase the audit team develops an understanding of agency activities and defines the objective and scope of the audit.

The planning phase also identifies the audit criteria. These are standards of performance against which the agency or program activities are assessed. Criteria may be based on best practice, government targets, benchmarks or published guidelines.

At the completion of fieldwork the audit team meets with agency management to discuss all significant matters arising out of the audit. Following this, a draft performance audit report is prepared.

The audit team then meets with agency management to check that facts presented in the draft report are accurate and that recommendations are practical and appropriate.

A final report is then provided to the CEO for comment. The relevant minister and the Treasurer are also provided with a copy of the final report. The report tabled in parliament includes a response from the CEO on the report's conclusion and recommendations. In multiple agency performance audits there may be responses from more than one agency or from a nominated coordinating agency.

Do we check to see if recommendations have been implemented?

Following the tabling of the report in parliament, agencies are requested to advise the Audit Office on action taken, or proposed, against each of the report's recommendations. It is usual for agency audit committees to monitor progress with the implementation of recommendations.

In addition, it is the practice of Parliament's Public Accounts Committee (PAC) to conduct reviews or hold inquiries into matters raised in performance audit reports. The reviews and inquiries are usually held 12 months after the report is tabled. These reports are available on the parliamentary website.

Who audits the auditors?

Our performance audits are subject to internal and external quality reviews against relevant Australian and international standards.

Internal quality control review of each audit ensures compliance with Australian assurance standards. Periodic review by other Audit Offices tests our activities against best practice.

The PAC is also responsible for overseeing the performance of the Audit Office and conducts a review of our operations every four years. The review's report is tabled in parliament and available on its website.

Who pays for performance audits?

No fee is charged for performance audits. Our performance audit services are funded by the NSW Parliament.

Further information and copies of reports

For further information, including copies of performance audit reports and a list of audits currently in-progress, please see our website www.audit.nsw.gov.au or contact us on 9275 7100

Our vision

Making a difference through audit excellence.

Our mission

To help parliament hold government accountable for its use of public resources.

Our values

Purpose – we have an impact, are accountable, and work as a team.

People – we trust and respect others and have a balanced approach to work.

Professionalism – we are recognised for our independence and integrity and the value we deliver.

Professional people with purpose

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