



National Audit Office

Reducing Costs in HM Revenue & Customs

Methodology

JULY 2011

Methodology

Study Scope

1 This report is one of a series on how different departments are implementing their cost reductions. Our examination is based on the premise that securing value for money from cost reductions involves more than just implementing planned cuts and that expenditure cuts should generate long term efficiency savings. Uniform top slicing of budgets or indiscriminate cost-cutting can leave an organisation unprepared for future challenges and at risk of building up higher costs in future. We assessed the information underlying the cost reduction plans, using a framework of good practice. In applying the framework, we have also used our detailed knowledge of HMRC from our previous work, including our audit of the financial accounts.

2 The Spending Review covers the four year period to 31 March 2015 and HMRC's cost reduction plans continue to evolve. Our examination is based on the information available in May 2011. As HMRC is only near the start of implementing its cost reduction measures, we would expect to report on its progress at regular intervals over the timescale of the Spending Review. This is an opportune time, however, for the National Audit Office to examine the progress against the following criteria:

- a** The need to fully understand how costs are incurred at present and their relationship to service delivery value.
- b** A clear vision of how the organisation can be restructured to reduce unnecessary costs in the future.
- c** A clear plan for how this vision can be achieved.

Framework

3 Drawing on our previous financial and value for money work, we prepared a short guide for departments in 2010 on the key principles of structured cost reduction. Using this guide, and publications from many other organisations in both the private and public sector we produced a framework for good practice in delivering cost reduction initiatives (see **Figure 1**). With the help of consultants Deloitte and Amtec, we used this framework to assess HMRC's plans.

Figure 1

National Audit Office framework for cost reduction initiatives

Understanding objectives, costs, outputs and benefits

<p>1 Has the Department identified and prioritised its objectives and outputs/outcomes?</p>	<p>1.1 Does the Department agree and understand its objectives, outputs and outcomes for the next five years?</p> <p>1.2 Has the Department prioritised its objectives and outputs?</p>
<p>2 Does the Department currently cost each output/outcome related to its objectives, accurately apportioned from quality standing information on administration costs?</p>	<p>2.1 Does the Department identify and analyse costs for all its outputs/outcomes, over time?</p> <p>2.2 What is the process for assurance and scrutiny of costings to ensure they are accurate and timely?</p> <p>2.3 How well does the Department understand the fixed and variable elements of its costs?</p> <p>2.4 Does the Department know the unit costs of delivery outputs/outcomes and how this changes as a result of other factors?</p> <p>2.5 What process does the Department use to apportion its financial reporting data to its management reporting data?</p>
<p>3 Does the Department separately cost its processes and link them to outputs/outcomes? Does the Department identify and understand the main cost drivers of its processes and distinguish between fixed and variable elements?</p>	<p>3.1 Is it clear what the main cost drivers are for outputs, outcomes and processes?</p> <p>3.2 Does the Department understand what its processes are and their contribution to the business?</p> <p>3.3 How good is the Department's understanding of how process costs change in response to changing levels of throughput?</p> <p>3.4 Does the Department use the process cost information to identify opportunities for savings?</p> <p>3.5 Has the Department broken the costs down by function, role, rank, grade, location, structure?</p>
<p>4 Does the Department (at management board and other decision-making levels) monitor performance of its outputs/outcomes in terms of cost, quality and level of service? Does it use this information to manage its business?</p>	<p>4.1 Is there evidence that the management board recognise the importance of costing information of processes, outputs and outcomes in running the Department?</p> <p>4.2 Is there sufficient information available to enable the management board to understand fully the (fixed and variable) cost of outputs/outcomes?</p> <p>4.3 Has the Department set baselines for the cost, quality and level of service of each output/outcome?</p> <p>4.4 How does the Department monitor performance of its outputs/outcomes against baselines for cost, quality and level of service?</p> <p>4.5 How does the Department's management board hold budget holders to account for their performance against budgets?</p> <p>4.6 Is there sufficient transparency and frequency of reporting on the costs of each output/outcome throughout the organisation?</p>

5 Is the Department aware of the barriers to the costing of its processes and outputs/outcomes? Is it overcoming these barriers?

5.1 What are the obstacles to achieving information of sufficient quality/timeliness on the cost of processes/outputs/outcomes and the relationship between funding and processes/ outputs/outcomes?

5.2 Does the Department fully understand its deficiencies in cost information?

5.3 Is there an improvement plan which addresses gaps identified in its costing information?

Making Cost Reduction plans

6 Has the Department built robust evidence-based cost reduction strategies?

6a Has the Department tied its planning together into a coherent strategy?

6a.1 In considering strategic cost reduction, has the Department used an analytical framework to understand how best to influence cost levers and drivers?

6a.2 Has the Department used the analytical framework to assess how to influence cost drivers for an optimal result?

6a.3 Does the Department understand the levers it can use to influence costs and how they interact with each other?

6a.4 Has the Department fully appraised options for cost reductions and selected ones with the best scope to maximise value for money?

6a.5 Has the Department identified the skills, capabilities and capacities needed to carry out cost reductions plans?

6a.6 Does the Department have a plan to address any gaps in skills, capabilities and capacities?

6b For individual cost streams/ processes, has the Department built a robust evidence based plan?

6.b.1 Do individual plans contain:

- a clear vision of the intended benefits of the programme;
- a clear understanding of the resources, budget and timetable for delivery of the intended benefits; and
- clear expectations for milestones and performance indicators.

6b.2 Has the Department fully appraised options for cost reductions and selected ones with the best scope to maximise value for money?

6c Has the Department engaged with its staff in appraising and selecting options?

6c.1 How does the management board ensure all key stakeholders are bought into delivering against the improvement plan?

6c.2 What incentives are there for staff to innovate and reduce costs, and do staff understand their role in the success of change programme (for example through personal objectives)?

6c.3 To what degree are accountabilities and responsibilities for cost performance clearly understood throughout the Department?

6c.4 How are front-line staff involved in identifying potential areas for efficiency savings?

6c.5 Is the leadership team strong and visible, and drives the required change?

6c.6 Has the Department taken steps to change culture and behaviour as well as processes?

Delivering cost reductions

7 For tactical efficiency savings: does the Department use robust techniques to optimise resources in its current business model?

7.1 Has the Department identified and executed quick and low risk cost reductions?

7.2 Does the Department benchmark the costs of its activities (internally across business units, geographical area and function as well as externally with comparable organisations) and use the results to improve its performance or increase productivity?

8 For strategic cost reduction: Are the Department's longer term cost reduction plans on track?

8.1 Is the Department monitoring progress centrally in terms of risks and effects?

8.2 Is the work joined up with the tactical efficiency savings work?

9 Does the Department measure its cost reductions and savings accurately, using agreed HM Treasury/National Audit Office criteria, and measure their wider impacts in service delivery and for other government departments?

9.1 Is the Department measuring savings using the agreed criteria?

9.2 Is the Department measuring the wider impact of its cost reduction plans on its service delivery and on other government departments?

9.3 Does finance test claimed savings against available financial information?

9.4 Does the Department have an explicit baseline against which to measure savings?

Methodology

4 We collected evidence between December 2010 and May 2011. The key methodologies used were:

- semi-structured interviews;
- document review;
- financial/quantitative data analysis;
- literature review;
- external assistance; and
- previous National Audit Office work.

Semi-structured interviews

5 We conducted semi-structured interviews with a range of staff at HMRC. We explored:

- HMRC's operational goals and the supporting strategic planning;
- the way HMRC identified potential Spending Review savings;
- HMRC's understanding of its cost base and how this relates to its processes;
- the planning of its Spending Review cost reduction programme; and
- the delivery arrangements for this programme, including how HMRC will deal with variations from plans.

Document review

6 We reviewed planning papers, including submissions to senior HMRC officials and correspondence with HM Treasury, to understand how the cost reduction initiatives were identified and selected.

7 We reviewed the outline business cases for selected investment projects to test if cost reduction measures were based on a robust assessment of the costs, benefits and risks. We also reviewed how HMRC intends to achieve cost savings in its business areas. In addition, we reviewed the capabilities, systems and processes underlying the plans using our framework of good practice.

8 We reviewed HMRC's leadership and governance arrangements for implementing its cost reduction measures, along with the arrangements for managing the overall cost reduction programme.

Financial and quantitative analysis

- 9** We analysed planning documents to understand:
- the profiles of investment funding, cost reductions and benefits;
 - the impact of projected inflation on cash allocations; and
 - the key investment projects.

Literature review

10 We reviewed private sector literature and research to identify the key critical success factors that are required for successful delivery of cost reduction programmes. We identified lessons learnt and good practice tips from other cost reduction programmes.

External assistance

11 We commissioned consultants Deloitte and Amtec to develop a good practice framework for cost reduction and to provide advice on how to apply it to HMRC.

Previous National Audit Office work

12 We drew upon our previous value for money reports of HMRC, which are available on the National Audit Office website (www.nao.org.uk/publications); and our observations on HMRC's annual accounts, which may be viewed with the accounts through the HMRC website (www.hmrc.gov.uk).