



Office of John Wright MP

Parliamentary Undersecretary to the:
Minister of Economic Development
Minister of Industry and Regional Development
Minister of Revenue
Minister of Racing

Media Statement

24 May 2000

For immediate release

Tax law on compliance and penalties to be reviewed

The Government today announced the terms of its review of the tax law relating to taxpayer compliance and penalties.

Revenue Under-secretary John Wright said the review would assess how well the legislation is achieving its objectives.

"The compliance and penalty legislation in the Tax Administration Act has four main aims," Mr Wright said. "It should deter non-compliance with the law, be understandable and fair, be flexible yet consistent, and be administered consistently.

"The review will look at how well the legislation does that, and identify areas where improvement is needed.

"The legislation, which came into effect in 1997, sets out the obligations of taxpayers and the tax standards they are expected to meet. It prescribes standard penalties across all taxes and duties for not complying with the law.

"The new legislation replaced a collection of tax rules that had built up over many years. The rules had gaps in coverage and were inconsistent in their application. For example, some actions attracted a penalty for certain kinds of taxes but not for others, while there were major inconsistencies in the size of penalties for similar defaults.

"Now that the new legislation has had three years to bed in, it is timely to review it.

"A further incentive is to respond to criticism of aspects of the legislation, mainly that it is too harsh or lacking in flexibility. For this reason the review will pick up on the relevant recommendations of the 1998 report of the Committee of Experts on Tax Compliance, and last year's report of the Finance and Expenditure Committee's inquiry into the powers and operations of Inland Revenue. Both inquiries made valuable contributions to understanding where the legislation could be improved.

"Changes inspired by their recommendations form part of a recently introduced taxation bill. They include the reduction of the incremental penalty for late payment from 2 percent to 1 percent, and the extension of relief provisions to all taxes, both of which introduce greater lenience and flexibility into the administration of the legislation.

"The public will be able to have its say on any changes arising from the review well before they are drafted into legislation. A discussion document seeking public submissions on proposals is planned for February of next year," John Wright said.

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Terms of reference for the review of the compliance and penalties legislation

The review is to assess how well the compliance and penalties legislation is achieving its objectives, which encompass being:

1. effective in deterring non-compliance and encouraging remedial action;
2. understandable and fair, and perceived as such;
3. appropriately flexible and consistent; and
4. consistently administered.

The review will identify areas where improvements can be made to better achieve the objectives of the compliance and penalties legislation.

In relation to the objectives above, the review will consider the following issues:

Effective in deterring non-compliance and encouraging remedial action

- Whether there has been any change in compliance behaviour caused by the new legislation.
- Whether a past record of “good behaviour” should be taken into account when deciding whether to impose a penalty, and if so how; whether the Inland Revenue Department needs to exercise a greater degree of flexibility when applying shortfall penalties; whether shortfall penalties should apply when it is determined that the taxpayer has made an inadvertent error.
- Whether the legislation sets standards clearly. For example, what constitutes “lack of reasonable care” or “unacceptable interpretation”? How late filing penalties, late payment penalties and shortfall penalties are applied, including whether the levels of late filing penalty are appropriate given the different taxpayer groups. Whether the rates of shortfall penalties are appropriate, by being fair while deterring non-compliance and encouraging remedial action. Whether the standards imposed on agents are appropriate.
- In relation to sections 16 and 17 of the Tax Administration Act 1994, whether:
 - Section 17 should be amended to deem the records of an offshore entity controlled by a New Zealand resident to be under the control of that New Zealand resident.
 - Section 17 should be amended to remove the words “necessary or relevant”.

- Section 17 should be amended to give the Commissioner the discretion to require that documents requisitioned under that section should be sent to an Inland Revenue office.
 - Section 16 should be amended to allow documents to be removed from premises for copying and to be returned as soon as practicable.
 - Section 16(2) should be amended to clarify that it applies to third parties.
- The method by which use-of-money interest is calculated to determine whether changes which can be made to the interest rates for overpayments and underpayments in order to reduce the differential between the rates are appropriate.
 - Whether there are circumstances that require relief from the use-of-money interest rules.
 - In relation to write-offs, whether there should be a time limit on the reinstatement of a debt; whether, if the present policy continues, the term “write-off” should be replaced by wording that more accurately describes the policy (for example, “provisional write-off”); whether it is necessary for the write-off provisions to be contained in the Inland Revenue Acts.
 - Whether there should be no penalties for voluntary disclosures.
 - The criteria for entering into instalment arrangements, reporting to the Government on the matter.
 - Whether there should be the option of having an annual GST return based on figures from the financial statements, with GST payments during the year being regarded as provisional. In the case of GST returns it may only be when the annual accounts are completed that GST errors are identified. Taxpayers are potentially exposed to penalties.
 - Whether Inland Revenue should be required to reinforce internally and publicly the principle that if a taxpayer (or advisor) has not interpreted the legislation a penalty for unacceptable interpretation cannot apply.
 - Whether there should be penalties on temporary shortfalls.
 - The wider remission powers of the Commissioner in respect of use-of-money interest to cover the situation where the taxpayer did not have the benefit of the use of the funds or no economic benefit was gained; the Commissioner’s split rate approach and its validity.

Understandable and fair, and perceived as such

- Whether the fairness of the penalties provisions is apparent to all taxpayers, and taxpayers that comply can see that those who do not comply are adequately penalised.
- Whether the Government's performance expectations of taxpayers are reasonable.
- Whether the debt hardship and instalment arrangement provisions are adequate and the rules for offsetting overpayments or tax credits against underpayments or tax debits are adequate.
- Whether the Tax Administration Act 1994 should be amended to provide a clear, four-year time bar in relation to all taxes except where the Commissioner of Inland Revenue has reasonable grounds to suspect a return to be fraudulent or wilfully misleading.
- The process by which assessments can be challenged, in particular considering whether a time limit should be placed on the Commissioner of Inland Revenue when addressing a taxpayer's Notice of Response.
- The concept of encouraging the retention, on file, of particulars of tax situations and their rationale if some uncertainty is involved; the issue of requiring disclosure if the tax at risk in a tax position exceeds a specified threshold (such disclosure would be required to be accompanied by sufficiently informative statements on the tax situation at issue and the tax position taken); the role of record keeping versus disclosure to the Commissioner and the appropriate treatment of such disclosure.
- Whether incentives could be provided to taxpayers to ensure that they pay off their debt in the shortest timeframe they can afford. For example, the use-of-money interest rate could reflect the term of the instalment arrangement.
- Whether the remission provisions can be applied to companies.

Appropriately flexible and consistent

- Whether the legislation minimises compliance costs where possible and is consistent with the proposals in the discussion document *Less Taxing Tax*.
- The extent of any lack of consistency in the application of the compliance and penalties legislation, owing to unclear or uncertain legislation.
- Whether there should be more flexibility in considering remission and hardship.

- Whether Inland Revenue should be required to develop an administrative solution to the problem whereby a taxpayer claiming GST in the wrong entity may be harshly penalised, despite there being no economic disadvantage to the Government (or advantage to the taxpayer); whether such administrative measure then requires to be embodied in the law by a suitable legislative change.

Consistently administered

- Whether the penalties legislation and administrative practices complement the efficient operation of the tax system, are practicable and aim to keep compliance and administration costs as low as possible; whether the compliance and penalties legislation is integrated with various initiatives such as Inland Revenue's Audit 2000 and self-assessment projects.
- The extent of any lack of consistency in Inland Revenue administration. A separate report from the Operations Group will be sent to the Government outlining any administrative issues identified and the priorities in finding solutions.

Timeline

The timeline for this review is as follows:

September 2000	Draft paper for discussion on initial policy options
February 2001	Issue discussion document (or similar) for consultation
November 2001	Introduction of bill
April 2002	Implementation