

Regulatory Impact Statement

Changes to the tax administration of investment income information

Agency Disclosure Statement

This Regulatory Impact Statement has been prepared by Inland Revenue. It provides an analysis of options to improve the tax administration of investment income information.

The options considered are intended to reduce compliance costs for recipients of investment income and administrative costs for Government, while improving the administration of investment income to ensure that taxpayers' tax obligations and social policy entitlements are calculated more accurately during the year. The changes are also likely to reduce compliance costs for payers of investment income that make payments to small numbers of recipients as they will be able to shift from paper returns to digital filing. Payers of investment income that make payments to large numbers of recipients are expected to have systems change costs initially and may have some ongoing cost increases, however, options to improve their ability to administer withholding taxes and to reduce some costs going forward have also been included in the options. The options were developed in the context of the wider tax policy framework of a clear and coherent broad-base, low-rate tax system.

A key gap in the analysis is that Inland Revenue is not able to accurately forecast the administrative and compliance cost impacts of these proposals. Indications of the direction and order of magnitude of the impacts have been provided where appropriate. A further gap in the analysis is that Inland Revenue does not hold sufficient data to fully analyse the benefits of the proposals. For example, Inland Revenue does not know how many people receive dividend income and social policy payments, or how many people receive non-locked in PIE income and social policy payments.

None of the policy options restrict market competition, impair property rights, reduce incentives for small businesses to operate, or override fundamental common law principles.



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Reader's guide to this Regulatory Impact Statement

This document covers a number of discrete proposals which have been grouped into two themes – 'getting it right from the start' and 'compliance and administration costs'. Within these two themes are a significant number of proposals.

To manage this large number of topics we have shifted the detailed analysis of each theme, and the component proposals within that theme, out of the Regulatory Analysis section and into two appendices.

The body of the Regulatory Impact Statement (RIS) still contains an overview of the options considered but the detailed analysis of the costs, benefits, impacts and recommendations is contained in the corresponding appendix. Within the overview tables the following symbols are used:

- ✓✓ Significantly better than the status quo
- ✓× Better than the status quo
- ×× Worse than the status quo

The consultation section of the RIS provides a summary of our consultation approach with the feedback received on each proposal set out in the corresponding appendix.

STATUS QUO AND PROBLEM DEFINITION

Inland Revenue's transformation programme

1. The Government's objective for the revenue system is for it to be as fair and efficient as possible in raising the revenue required to meet the Government's needs. For taxpayers the tax system should be simple to comply with, making it easy to get right and difficult to get wrong. It should serve the needs of all New Zealanders, put taxpayers at the centre and help them from the start, rather than when things go wrong.
2. The shift to digital and greater globalisation has reshaped how businesses and individuals interact and connect, and their expectations of government.
3. Businesses are increasingly using software packages to automate processes and reduce their compliance burden. Businesses have consistently ranked tax as their highest compliance priority, and it often contributes the most to their overall compliance burden. Compliance costs could be reduced by making better use of businesses' everyday processes and systems to meet tax obligations. Enabling businesses to spend less time on tax and more time on running their business will support Government's wider goals of building a more competitive economy and delivering better public services.
4. The amount of income New Zealanders earn from savings and investments is likely to grow over the coming years as the population is aging. People tend to accrue capital as they grow older and then become more reliant on their capital producing investment income as they leave the workforce.
5. There are a large number of payers of investment income, often making payments to small numbers of recipients. For example, 92% of the 16,600 interest payers who filed interest certificates with Inland Revenue for the 2015 tax year filed less than five certificates and 570,000 of the 573,000 registered companies in New Zealand as at 21 April 2016 had between one and ten shareholders. In contrast to this, some of the payers of investment income making payments to large numbers of recipients make payments to hundreds of thousands of recipients.
6. To protect the Government's ability to collect sufficient revenue to keep providing services, it is important that New Zealand's revenue system keeps pace with change and is as efficient as possible. The fiscal challenges associated with an ageing population and associated demand for high quality healthcare and other services will add impetus to the need for a highly efficient and responsive revenue system. To meet these challenges, Inland Revenue requires a fundamental shift in the way it thinks, designs, and operates.
7. The Government has agreed to change the revenue system through business process and technology change. A digitally-based revenue system, simplified policies, and better use of data and intelligence to better understand customers will simplify how services are delivered and change how customers interact with the revenue system.
8. Having a good overall revenue system means having both good policies and good administration. While the policy framework is fundamentally sound, there is an opportunity to review current policy, legislative and administrative settings as levers to help modernise the revenue system and ensure it is responsive to global changes.
9. There is no doubt that Inland Revenue's computer systems (known as FIRST) need replacement to improve resilience and agility. They have reached the end of their life and are

not sustainable in the medium to long term. The FIRST systems are aging, extremely complex, very difficult and costly to maintain, and inflexible. Since FIRST was implemented, a number of income-related social policies have been added to the platform. Implementing social policies within a platform designed for tax administration has added layers of complexity and risk to Inland Revenue's business processes and technology infrastructure. This in turn limits the department's ability to respond to government policy priorities.

10. However, Business Transformation is far more than just updating a computer system. Rather, it is a chance to fundamentally improve the tax administration system with a view to:

- Helping customers get it right from the start;
- Making it harder to get into debt, and easier to get out;
- Lowering the cost of engaging with the tax system; and
- Embedding tax in existing business systems.

11. This RIS outlines options for improving the tax administration system as it relates to the provision of income information from investment. Income from investment refers to interest, dividends, portfolio investment entity (PIE) income and income distributed by Māori authorities.

PROBLEM DEFINITION

Getting it right from the start

12. Inland Revenue wants to make it easy for taxpayers to get their tax obligations right the first time and wants to be proactive in helping them to do that. Addressing errors after the event imposes significant costs on both Inland Revenue and the taxpayer. It is more effective and efficient to consider what can be done to enable taxpayers to get their tax obligations and social policy entitlements correct during the year, in other words, to get it right from the start. This will reduce the chance of taxpayers having a tax or social policy debt at the end of the year, or from paying too much tax or not receiving their full social policy entitlement during the year. There are two issues with the administration of investment income that impede Inland Revenue's ability to help customers get it right from the start.

Issue one: detail and frequency of investment income information

13. Currently, Inland Revenue does not receive sufficiently detailed and frequent information about the investment income that taxpayers earn and the tax withheld or paid on that income. For interest and portfolio investment entity (PIE) income, Inland Revenue doesn't receive information about the income taxpayers earned and the tax deducted from that income until after the end of the tax year. For dividends, Māori authority distributions and interest income that is exempt from RWT or subject to the approved issuer levy (AIL), Inland Revenue doesn't receive information about the amounts received by recipients at all, unless it is specifically asked for.

14. This affects Inland Revenue's ability to ensure taxpayers' tax and social policy obligations/entitlements are correct during the year. For example, if Inland Revenue does not know how much investment income a taxpayer earns during the year, it will not be in a position to advise the taxpayer of the appropriate withholding rate to use. Further, it reduces Inland Revenue's effectiveness in ensuring a taxpayer's social policy entitlements, such as working for families, are correct during the year. Taxpayers who have not paid the correct tax or received the correct social policy entitlements during the year will need to square up at the

end of the year, resulting in a debt or refund. Often taxpayers are unaware of these obligations, resulting in Inland Revenue paying out more in social policy entitlements than it otherwise should and taxpayers paying less tax and social policy obligations than they should. Under the current rules it is also easier for taxpayers to ignore their tax and social assistance obligations, for example, by not declaring dividend income in their tax returns. As Inland Revenue gets no detailed recipient information on this type of income, it would be difficult to identify and correct this.

Issue two: Identifying information

IRD numbers

15. Inland Revenue is not able to attribute income to a taxpayer if Inland Revenue does not have the taxpayer's IRD number. Data shows that 20% of the end of year interest certificates that Inland Revenue receives do not include an IRD number. This means that this interest income will not be taken into account for tax and social policy purposes – potentially resulting in the IRD paying too much in social policy entitlements and/or the taxpayer paying too little in social policy obligations.

Date of birth information

16. Another problem preventing Inland Revenue from helping taxpayers get it right from the start is that Inland Revenue does not have sufficient information to confirm some taxpayers' identities. In order to be able to ensure income is allocated to the correct taxpayer, Inland Revenue needs the taxpayer's date of birth information in some circumstances¹. Obtaining date of birth information would also enable Inland Revenue to associate information received from other Government agencies (for example, Customs information on passenger movements) with the correct taxpayer.

17. Having date of birth information will also help other Government agencies to use information that Inland Revenue shares with them by enabling them to match the information with the "customer" information in their own systems.

Joint accounts

18. Inland Revenue is only provided with one IRD number for a joint bank account. The reporting of income information for joint investments lacks IRD number information for owners other than the owner treated as the primary owner by the investment provider. All the income from that account is allocated to the owner whose IRD is associated with the account. The joint account owners then may need to file tax returns to correct their tax positions.

¹ Date of birth information may be necessary to identify taxpayers where two or more taxpayers have the same name, where no IRD number or an incorrect IRD number has been provided or where a change of name or address has occurred.

Identifying information for recipients of income subject to AIL and income that is treated as exempt

19. Inland Revenue does not receive any information on the recipients of income subject to AIL or that is treated as exempt, so is unable to check that the payment of AIL or the exempt treatment is appropriate.

Compliance and administration costs

20. Inland Revenue wants to minimise the costs that taxpayers face complying with the tax system, as well as the costs to the government of administering the tax system. Greater use of electronic and internet-based technology is a key enabler to achieve these objectives. The Government also wants to leverage existing business processes – for example by aligning the provision of information with the payment of the income and the withholding of the tax. The following problems with the current system result in increased compliance and administration costs.

Compliance costs for recipients of investment income

Filing tax returns

21. The current process of filing a tax return can be cumbersome as taxpayers are required to gather information about the interest, dividends and Māori authority distributions they have received from payers during the year and include it in their tax return.

Selecting a withholding rate

22. Currently, taxpayers need to have an indication of the income they will earn in the tax year in order to select an appropriate withholding rate. Often taxpayers will select a withholding rate and forget to change it as their circumstances change (or they may not realise that their income has reached a threshold that requires a higher tax rate), resulting in under or over taxation. Having to work out the appropriate withholding rate, update it as circumstances change, and file a tax return wherever an incorrect rate is used, entails significant compliance costs for taxpayers. This is a particular issue for PIE investments as usually the amount of tax paid by the PIE is a final tax.

Social policy

23. Because Inland Revenue does not receive information throughout the year about the investment income of individual taxpayers, it is not able to calculate social policy payments during the year to reflect this income. This necessitates the need for an end of year square-up, which often results in hardship for people who have amounts to repay, or who received too little during the year when they needed the assistance.

Compliance costs for payers of investment income

End of year tax certificates

24. Payers of resident withholding income are currently required to provide end-of-year tax certificates to the recipients of the income – such as year-end interest certificates and PIE investor statements. These certificates set out the amount of income earned and tax deducted, which recipients can then include in their tax return. Providing these certificates imposes

compliance costs on payers of investment income which may be unnecessary if that information was already held by Inland Revenue and able to be viewed by the taxpayer.

Certificates of exemption

25. Taxpayers holding certificates of exemption (“COEs”) from RWT are entitled to be paid interest and dividends without having any tax deducted by the payer. The holder of the COE is required to provide a copy to the relevant withholder and must inform the withholder if their COE is cancelled. Cancellations and issues of COEs in the previous quarter are published in the New Zealand Gazette each quarter. Taxpayers exempt under Acts other than the Income Tax Act 2007 and the Tax Administration Act 1994, for example the Education Act, are entitled to an exemption without needing to obtain a COE.

26. The current exemption process involves compliance costs for payers as they need to:

- receive exemption certificates from taxpayers;
- check the appropriate New Zealand Gazette to see if the taxpayer’s certificate has been cancelled; and
- assess whether the customer can appropriately claim to be exempt under non-tax legislation.

27. The New Zealand Gazette listing is only published quarterly so may lead to delays in recognizing a COE has expired and can also show a COE as expired even though it has been renewed from the first day of the following quarter. This frustrates payers of investment income and can lead to customer complaints where the renewed COE is removed because the Gazette list shows it has been cancelled.

Compliance costs for payers and administrative costs for Inland Revenue

Electronic filing

28. A number of withholding returns are paper based (with no option of electronic filing). For those returns that are able to be filed electronically, there is no electronic filing threshold to require payers of a certain size to file electronically. Paper filing is slower, more expensive in terms of compliance costs for taxpayers and administrative costs for Inland Revenue and more prone to errors.

Error correction

29. Currently, payers of investment income are able to correct errors in a period by adjusting payments in a subsequent period (i.e. if a payer does not withhold enough tax from a payment of interest, it can withhold more tax from the next payment of interest). However, the ability to correct errors in subsequent periods is limited – for example, there is no ability to correct errors between tax years, or even during tax years for dividends where the error resulted in an underpayment of tax. The inability to correct errors in subsequent periods results in increased compliance costs as in order to correct the error, returns must be re-filed.

30. Errors also impose a monetary cost on investment income payers as they often bear the cost where they have under-withheld from a taxpayer in error, but will refund the taxpayer the money where they have over-withheld in error. Further, UOMI is payable to Inland Revenue at 8.27% pa on underpayments of tax, but receivable from Inland Revenue at 1.62% on overpayments.

31. Payers of investment income currently report summary information by period that matches the payment that they are making. This makes the correction of errors more difficult as an amount needs to be added or subtracted from a subsequent period in the event of an error. Some payers of investment income resolve this by calculating a year-to-date total and then deducting previous payments to determine their current payment obligation.

OBJECTIVES

32. The main objective of the options is to simplify the tax system by making it easy to comply, and difficult not to, through making better use of investment income information to improve the administration of tax and social policy. The criteria against which the options have been assessed are:

- (a) **Fairness and equity:** to support fairness in the tax system, options should, to the extent possible, seek to treat similar taxpayers in similar circumstances in a similar way.
- (b) **Efficiency of compliance and administration:** the compliance cost impacts on taxpayers and the administrative costs to Inland Revenue should be minimised as far as possible.
- (c) **Sustainability of the tax system:** options should collect the revenue required in a transparent and timely manner while not leading to tax driven outcomes and enable the efficient administration of the social policies administered by Inland Revenue.

33. These criteria are weighted equally.

34. There are no social, environmental or cultural impacts associated with the recommended changes.

REGULATORY IMPACT ANALYSIS

35. Officials have developed options to address the above issues. These options have been organised under the themes described in the problem definition section, and are summarised below. Further detail on these problems and their associated options is contained in the appendices at the end of this document.

Getting it right from the start

Information on income

More income information - options:

36. At present Inland Revenue does not receive investor level income information in relation to dividends, taxable Maori authority distributions and income that is exempt or subject to AIL. The following options were considered in relation to Inland Revenue obtaining more information from investment income payers. Further detail is contained in appendix A.

Options	Analysis against the objective and criteria
Option 1 – Status quo	Doesn't meet the main objective
Option 2 – payers to provide taxpayer specific information on the amount of income earned and tax withheld (if any) for dividends and taxable Maori authority distributions. This information will continue to be required for PIE income and interest.	<p>Meets the main objective</p> <p>Fairness & equity: ✓✓ Compliance and administration: ✓× Sustainability: ✓✓</p> <p>Overall comment: Significant improvement on status quo</p>

Recommendation

37. Option 2 was recommended over the status quo as receiving this information would help Inland Revenue make it easier for taxpayers to comply with their tax obligations by prepopulating tax returns, more accurately determining social policy entitlements during the year, and correcting withholding tax rates.

Identifying information for recipients of income subject to AIL and income that is treated as exempt

38. The following options were considered for obtaining the identity of recipients of exempt income or income subject to AIL. These options are further considered in appendix A.

Options	Analysis against the objective and criteria
Option 1 – Status quo.	Doesn't meet the main objective
Option 2 – Identifying information obtained for exempt income and income subject to AIL.	<p>Meets the main objective</p> <p>Fairness & equity: ✓✓ Compliance and administration: ✓× Sustainability: ✓✓</p> <p>Overall comment: Significant improvement on status quo</p>
Option 3 – Identifying information obtained for exempt income and income subject to AIL, but carving out any information already provided under AEOI.	<p>Partially meets the main objective</p> <p>Fairness & equity: ✓✓ Compliance and administration: ×× Sustainability: ✓×</p> <p>Overall comment: Improvement on status quo</p>

Recommendation

39. Option 2 was recommended over the status quo as receiving this information would help Inland Revenue ensure that the AIL and exemption regimes were being used appropriately. It would also enable Inland Revenue to proactively contact taxpayers incorrectly using these regimes to help them to get it right.

40. Option 3 was not recommended as investment income payers were clear during consultation that they wanted the information they provided under the withholding tax regimes to be kept separate from the information they provided under the FATCA and AEOI regimes. The investment income payers also noted that there were some types of investments and investors that they were not required to report on under those regimes so the income provided would be likely to be incomplete if used for other purposes.

Frequency - options:

41. At present investor level income information, if required, is provided on an annual basis after the end of the relevant tax year. In order to fully realise the benefits mentioned above (paragraph 37), Inland Revenue needs to receive information more frequently than it does now. The options for provision of more frequent information are summarised below and outlined further in appendix A.

Options	Analysis against the objective and criteria
Option 1 – Status quo	Doesn't meet the main objective
Option 2 – provision of the information in the month following the month in which the income was paid.	<p>Meets the main objective</p> <p>Fairness & equity: ✓✓</p> <p>Compliance and administration: ✓x</p> <p>Sustainability: ✓x</p> <p>Overall comment: Improvement on status quo, but a significant impact on PIEs.</p>
Option 3 – provision of the information on the 20 th of the month following the quarter in which the income was paid for interest, dividends and taxable Maori authority distributions. Provision of PIE information remains at the end of the year (although by 15 May rather than 31 May for non-locked in PIEs and interest ² as well as 6 monthly reporting of PIRs for all PIEs). Provision of details for recipients of interest income treated as exempt to be required yearly.	<p>Meets the main objective</p> <p>Fairness & equity: ✓✓</p> <p>Compliance and administration: ✓x</p> <p>Sustainability: ✓x</p> <p>Overall comment: Significant improvement on status quo, but potentially limits options for the future administration of social policy.</p>

² Note that for interest this will be a transitional measure, as from 1 April 2020 monthly reporting of taxpayer specific information will be required.

Options	Analysis against the objective and criteria
<p>Option 4 – provision of the information on the 20th of the month following the month in which the income was paid for interest, dividends and taxable Maori authority distributions. Provision of PIE information remains at the end of the year (although by 15 May rather than 31 May for non-locked in PIEs and interest³ as well as 6 monthly reporting of PIRs for all PIEs). Provision of details for recipients of interest income treated as exempt to be required yearly.</p>	<p>Meets the main objective</p> <p>Fairness & equity: ✓✓</p> <p>Compliance and administration: ✓x</p> <p>Sustainability: ✓✓</p> <p>Overall comment: Significant improvement on status quo</p>

Recommendation

42. Option 4 was recommended over the other options as:

- Obtaining more frequent information will make it easier for taxpayers to comply with their tax affairs – it would enable Inland Revenue to prepopulate taxpayers’ tax returns, adjust their social policy entitlements/obligations and work out the appropriate tax rate for them. It would also provide greater scope for reforming the administration of social policy.
- It strikes a balance between benefits and compliance cost by not requiring additional information from PIEs given the complexity of the systems changes that PIEs would need to make in order to provide information monthly and the limited utility of the PIE information during the year.⁴
- Monthly information was preferred over quarterly information for the reasons set out in paragraph 108 in appendix A.
- Bringing forward the year end detailed information for PIE income (and for interest income until interest information begins being reported monthly) will enable this information to be pre-populated at the end of the year before the personal tax summary process is completed. This means the income will be associated with the taxpayer and they will be able to see it in their online tax records. While PIE income is not included in taxable income unless the PIR selected by the investor is too low, it can be relevant for social policy and for calculating the appropriate PIR for future periods.

Identifying information

IRD numbers - options:

43. In order to encourage tax compliance, the following options were considered for increasing the provision of IRD numbers. More detailed analysis is contained in appendix A.

³ Note this is a transitional measure as explained in the above footnote.

⁴ Due to the volatile nature of PIE income and because a large amount of PIE income (locked-in) is not relevant for social policy purposes – see paragraphs 92 and 93.

Options	Analysis against the objective and criteria
Option 1 – Status quo.	Doesn't meet the main objective
Option 2 – 45% non-declaration rate for all investment income types.	<p>Meets the main objective</p> <p>Fairness & equity: ✓✓</p> <p>Compliance and administration: ✓x</p> <p>Sustainability: ✓x</p> <p>Overall comment: Improvement on status quo</p>
Option 3 – 45% non-declaration rate just for interest income. For PIEs, provision of an IRD number will be required to open a new account (subject to limited exceptions – see appendix A).	<p>Partially meets the main objective</p> <p>Fairness & equity: ✓x</p> <p>Compliance and administration: ✓✓</p> <p>Sustainability: ✓✓</p> <p>Overall comment: Improvement on status quo</p>

Recommendation

44. Option 3 was recommended over option 2 as it better balances the compliance costs imposed on the investment income payers with the level of non-declaration. As PIE non-declaration is a much smaller problem than interest non-declaration the requirement to provide an IRD number when initially making an investment will cap the level of non-declaration at around 2% (there will be work done to match IRD numbers to these non-declared investors by PIEs and Inland Revenue to further reduce the level of non-declaration).

45. Applying a 45% non-declaration rate for PIEs would also add complexity to the tax system. Non-declared recipients would need to file tax returns in order to get excess tax refunded (PIE tax is usually a final tax). In addition, PIE losses give rise to tax credits at the investors' PIRs. A non-declared investor would get credits for any losses at 45% but, because they would be able to file a tax return, should not pay more than 33% tax on their PIE income.

46. We have not recommended a 45% non-declaration rate for dividends or Maori authority distributions due to capability concerns and because we are unable to determine the extent of the non-declaration problem in relation to these types of income until after we begin to receive detailed recipient information. This makes it very difficult to make a satisfactory analysis of the compliance cost versus the benefit at this stage.

47. Inland Revenue will work with payers of interest income to identify the IRD numbers of non-declared investors prior to the introduction of the increased non-declaration rate

Date of birth information - options:

48. The following options were considered in relation to Inland Revenue obtaining date of birth information from investment income payers. Further detail is contained in appendix A.

Options	Analysis against the objective and criteria
Option 1 – Status quo.	Doesn't meet the main objective
Option 2 – Date of birth to be provided if held by payer.	Partially meets the main objective Fairness & equity: ✓✓ Compliance and administration: ✓✓ Sustainability: ✓x Overall comment: Improvement on status quo
Option 3 – Date of birth requested by Inland Revenue where it is needed to data match.	Partially meets the main objective Fairness & equity: ✓✓ Compliance and administration: xx Sustainability: ✓x Overall comment: Improvement on status quo
Option 4 – Date of birth is required to be provided by the payer.	Doesn't meet the main objective Fairness & equity: ✓x Compliance and administration: xx Sustainability: xx Overall comment: Worse than the status quo

Recommendation

49. Option 2 was recommended over the other options as it does not impose excessive compliance costs on payers of investment income by requiring them to provide information they do not hold. Further, it improves Inland Revenue's ability to confirm taxpayers' identities by requiring date of birth information they do hold to be provided to Inland Revenue. Date of birth information is already collected by payers as part of "know your customer" processes for anti-money laundering purposes.

50. Option 3 was not recommended as:

- It would be likely to involve significant ad hoc data requests as no IRD number is provided for 20% of interest certificates, which would require investment income payers to go back through their customer records.

- It would also involve additional administrative costs for Inland Revenue as it would add a further step of identifying the recipients that date of birth was needed for and requesting it from the various investment income payers.

51. Option 4 was not recommended as it would require investment income providers to collect additional information from a significant number of their longer term customers. This would be likely to be a very expensive process and would be unlikely to have a high level of success. If date of birth information was absolutely required this would then mean that investment income providers would either be non-compliant or would have to withdraw services from a number of their customers. While the option would be likely to get more information for Inland Revenue it would not be fair, simple or cost effective.

Joint accounts - options:

52. Options for allocating income between owners of a joint investment are outlined below and described further in appendix A.

Options	Analysis against the objective and criteria
Option 1 – Status quo.	Doesn't meet the main objective
Option 2 – The investment income payer splits the income and tax among the owners according to their ownership proportions, and passes this information on to IR, as well as details of each owner (i.e. name, address, IRD number and date of birth).	Meets the main objective Fairness & equity: ✓✓ Compliance and administration: ✕✕ Sustainability: ✓✓ Overall comment: Improvement on status quo
Option 3 – The investment income payer informs IR that the taxpayers are operating a joint account, and provides income and identifying information on to IR. IR pre-populates their income by splitting the income and any tax credits evenly between the owners.	Partially meets the main objective Fairness & equity: ✓✓ Compliance and administration: ✓✕ Sustainability: ✓✕ Overall comment: Significant improvement on status quo

Recommendation

53. Option 3 was recommended over option 2 as option 2 would impose significant compliance costs to require payers of investment income to obtain the ownership proportions from joint account owners. It would also cause system difficulties as investment income payers would need to split the calculations of the withholding tax on the income. Ownership proportions could also change during periods creating even more system difficulties. Investment income payers were also concerned that having to manage this would likely to cause them to have customer relationship problems.

Compliance and administration costs

Compliance costs for taxpayers who are recipients of investment income

54. The compliance costs for the recipients of investment income are impacted by a number of the proposals discussed earlier in this document. Getting more information more frequently will allow Inland Revenue to associate the investment income with the recipients and will enable Inland Revenue to pre-populate the recipient's tax records (see paragraphs 37 and 42).

55. Pre-populating the investment income information will reduce the compliance costs of the recipients of investment income by removing the need to gather their various end of year tax certificates and any dividend statements and Maori authority distribution statements received during the year in order to complete their tax return. This would make it easier for them to get their tax position right.

56. More frequent information will also enable Inland Revenue to pro-actively correct withholding tax rates being used by recipients during the income year. This will help to reduce the size of the recipient's tax bill or refund at the end of the year by making sure they are on an appropriate tax rate during the year.

57. The pre-population of investment income information will also enable Inland Revenue to make more informed adjustments to recipients' social policy entitlements (getting information more frequently will be particularly helpful if changes are made to reduce the calculation period for social assistance).

Compliance costs for payers of investment income

End of year tax certificates – options:

58. It would be unnecessary to require payers of investment income to provide end of year certificates to their customers outlining the amount of income the customer had earned and the tax that had been withheld from that income if Inland Revenue was able to make this information available to the customers. Options for removing end of year tax certificates are outlined below and analysed further in appendix B.

Options	Analysis against the objective and criteria
Option 1 – Status quo.	Doesn't meet the main objective
Option 2 – Remove the requirement for all investment payers to provide end of year interest certificates to their customers. Payers would still need to provide shareholder dividend statements, PIE investor statements and Māori authority distribution statements to their customers.	Meets the main objective Fairness & equity: ✓ x Compliance and administration: ✓✓ Sustainability: ✓ x Overall comment: Improvement on status quo

Options	Analysis against the objective and criteria
<p>Option 3 – Remove the requirement for payers to provide end of year interest certificates to customers who have provided their IRD number. Payers must still provide shareholder dividend statements, PIE investor statements and Māori authority distribution statements to their customers (preferred).</p>	<p>Meets the main objective</p> <p>Fairness & equity: ✓ x Compliance and administration: ✓✓ Sustainability: ✓✓</p> <p>Overall comment: Improvement on status quo.</p>

Recommendation

59. Option 3 was recommended over option two as requiring payers to provide end of year interest certificates to customers who have not provided their IRD number is important as it notifies the taxpayer that they are on the non-declaration rate and to file a return (thus helping them to pay the correct amount of tax).

60. Removing the requirement for payers to provide interest certificates to customers who have provided their IRD numbers will reduce compliance costs for payers and was considered appropriate on the basis that Inland Revenue would prepopulate the information onto the taxpayer’s myIR account. In addition, where the interest is paid by a bank, the customers will usually be able to see their interest information on their bank statements or on internet banking services provided by the bank. It was not considered appropriate to remove the requirement to provide this information for other investment income sources such as dividends, because the receipt of the income is sporadic and the taxpayer won’t necessarily know when they are going to be receiving the income.

Certificates of exemption – options:

61. In order to reduce compliance costs for payers of investment income, the following options have been considered for improving the process of checking whether a taxpayer has a valid certificate of exemption from withholding tax. These options are explored further in appendix B.

Options	Analysis against the objective and criteria
<p>Option 1 – Status quo</p>	<p>Doesn’t meet the main objective</p>
<p>Option 2 – Inland Revenue establishes a certificate of exemption database</p>	<p>Partly meets the main objective</p> <p>Fairness & equity: ✓✓ Compliance and administration: ✓ x Sustainability: ✓ x</p> <p>Overall comment: Improvement on status quo</p>

Options	Analysis against the objective and criteria
Option 3 – Inland Revenue establishes a certificate of exemption database and requires recipients exempt under other acts to obtain a certificate of exemption.	<p>Meets the main objective</p> <p>Fairness & equity: ✓✓ Compliance and administration: ✓x Sustainability: ✓✓</p> <p>Overall comment: Significant improvement on status quo</p>

Recommendation

62. Option 3 was recommended as it would allow payers of investment income to easily ascertain whether a taxpayer was entitled to an exemption from RWT, representing a significant improvement over the status quo. Option 2 would be an improvement on the status quo but would have less of an impact on compliance costs than option 3 as investment income payers would still need to work out whether recipients claiming exemptions under other Acts should be treated as exempt.

Compliance costs for payers and administrative costs for Inland Revenue

Electronic filing – options:

63. To increase electronic filing of investment income returns, the following options are proposed. These options are summarised further in appendix B.

Options	Analysis against the objective and criteria
Option 1 – Status quo	
Option 2 – compulsory for all, with the ability to apply to the Commissioner for an exemption (preferred).	<p>Meets the main objective</p> <p>Fairness & equity: ✓x Compliance and administration: ✓✓ Sustainability: ✓✓</p> <p>Overall comment: Significant Improvement on status quo</p>
Option 3 – Online filing compulsory for large payers only (i.e. those with more than a certain number of recipients they pay investment income to).	<p>Meets the main objective</p> <p>Fairness & equity: ✓✓ Compliance and administration: ✓✓ Sustainability: ✓x</p> <p>Overall comment: Improvement on status quo</p>

Recommendation

64. Option 2 is recommended for the following reasons:

- It would ensure that everyone, other than those who are genuinely unable to access digital services, files online. Electronic filing is a very important enabler of the Business Transformation.
- Statistics show that the majority of companies only have one or two shareholders, and the majority of interest payers only file one or two certificates (see appendix B for further detail), so compulsion is important or else there is a risk that a significant number of paper returns will be filed.
- Currently most of the withholding tax returns must be filed on paper. It is likely that a significant number of investment income payers would simply continue to file on paper if they were not compelled to file digitally.

Error correction – options:

65. In order to reduce compliance and administrative costs, the following options have been considered for improving error correction mechanisms:

Options	Analysis against the objective and criteria
Option 1 – Status quo	
Option 2 – Unlimited error correction for all investment income types during a tax year, error correction subject to a threshold of the greater of \$2,000 or 5% of annual tax liability (for the tax type in question) for correction between tax years. Tax subject of an error will be treated as due in the period in which it is corrected, resulting in no UOMI or penalties.	<p>Meets the main objective</p> <p>Fairness & equity: ✓✓</p> <p>Compliance and administration: ✓✓</p> <p>Sustainability: ✓✓</p> <p>Overall comment: Improvement on status quo</p>

Recommendation

66. Option 2 is recommended as it provides a flexible method for error correction that will reduce compliance and administrative costs, and will not punish payers where they have made a genuine error.

Error correction (period reporting) – options:

67. As part of improving the ability to correct errors, the following options in regards to reporting requirements were considered:

Options	Analysis against the objective and criteria
Option 1 – Status quo	
Option 2 – Year-to-date reporting	<p>Meets the main objective for some types of investment income</p> <p>Fairness & equity: ✓✓</p> <p>Compliance and administration: ✓✓</p> <p>Sustainability: ✓✓</p>

	Overall comment: Significant improvement on status quo
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68. Option 2 is recommended for interest and PIE income because year to date reporting will work well for income types that tend to accumulate across the year such as interest income and PIE income however it will be less appropriate for income that occurs sporadically.

69. Option 1 (i.e. period by period reporting) is recommended for dividends and Maori authority distributions as these are likely to be one-off or sporadic transactions rather than accumulating returns across the income year.

CONCLUSION

70. The recommended options under the above themes enable improved service delivery to individuals and lay a foundation for subsequent improvements to social policy. They do this while recognising that ‘one size cannot fit all’ and while maintaining New Zealand’s broad base low rate tax framework. They also enable compliance cost savings for recipients of investment income and payers of investment income to small numbers of recipients while officials recognise that the recommended options will give rise to some increased compliance costs (largely up-front costs) for payers of investment income to large numbers of recipients. The recommended options also enable administrative costs savings,

CONSULTATION

71. Several forms of consultation have been undertaken in developing the options outlined in this statement.

72. In June 2014, Inland Revenue, the Treasury and Victoria University hosted a conference entitled *Tax administration for the 21st Century*. The conference explored options for making tax easier through reducing both compliance and administration costs, while balancing increased voluntary compliance against the core tax policy objectives of raising sufficient revenue and ensuring fairness and efficiency. The main points made by attendees were to give people the ability to self-manage their tax affairs through improved services and more flexible legislative frameworks, the importance of involving businesses and others in the design of the rules and processes, the need to ensure that there is an overall net benefit to society of the changes not just a cost shift from Inland Revenue to businesses, and to ensure the continued maintenance of the current tax system whilst the reforms occur.

73. Following this conference the Government issued *Making Tax Simpler – a Government green paper on tax administration* which outlined the scope and direction of the review of the tax administration, and sought feedback on the problems taxpayers face with the current system. At the same time the Government released *Making Tax Simpler – Better Digital Services a Government discussion document* which identified the key role envisaged for digital services in the modernised tax administration system.

74. Feedback on these two documents informed *Making Tax Simpler – Investment income information: a Government discussion document* which was released for public consultation in early July 2016. In addition to the discussion document an on-line forum was established and companies were notified of the consultation and encouraged to provide feedback. Over

60 comments were made to the online forum and 32 written submissions were received. This public feedback has informed the development of the options presented in this statement.

75. The main theme from submissions was that the proposals to receive more frequent investment income information lacked justification. While submitters were supportive of providing the additional information, many submitters felt that there would be minimal benefit in adjusting social policy payments on a monthly basis given the low amount of investment income people receive, and the lumpy nature of investment income. Almost all submitters said that the benefits would be significantly outweighed by the compliance costs that the provision of more frequent information would impose. Many submitters were in favour of reporting the information annually, or quarterly if a more frequent reporting requirement were to be introduced. The themes raised in the submissions were not typically sector specific but instead similar themes were raised by a number of submitters. The main exception to this was that most of the banking industry was strongly of the view that 3 years implementation time from the date of enactment was needed to implement the changes.

76. The submissions received were largely from investment income payers, advisory firms and industry organisations. The major benefits of this project are expected to flow to the recipients of investment income. As such the tenor of the submissions may not reflect the wider reaction to the proposals.

77. More detailed feedback from consultation is provided in the appendices.

DATA TO ADDRESS FEEDBACK FROM CONSULTATION

78. The below data highlights the benefits of the proposals:

- In 2015 the interest income of at least 185,000 individuals was not taken into account for working for families purposes.⁵ This resulted in the government paying out more in social policy entitlements than necessary - the exact impact of this cannot be quantified given WFF abatement rates depend on numerous factors.
- It is estimated that \$21 to 27 million of income tax per annum is forgone due to interest income not being correctly returned as income. This would be identified if the interest income was pre-populated.

IMPLEMENTATION

79. It is proposed to include the recommended options in a bill to be introduced in February 2017. The proposals will apply from the following dates:

⁵ Based on 27,000 families who reported any investment income compared with the files from interest payers which showed 239,000 individuals (assuming just 2 individuals per family received interest income) received interest income and WFF. The number of people not declaring their investment income is likely to be higher than this given we are comparing families who declared their investment income (i.e. includes interest, dividends and some PIE income etc.) versus individuals earning interest income and receiving WFF. These figures also exclude the recipients of interest income that have not provided their IRD numbers to their interest payers. If taxpayer specific information on dividends were collected, the level of non-declaration would be more apparent.

- 1 April 2018 - PIEs will be required to obtain the IRD number of new investors or alternatively a self-certification that they are non-resident and do not have an IRD number.
- 15 May immediately following the end of the tax year will be the due date for filing the current detailed interest and PIE income information (excluding “locked in” schemes) for tax years beginning on or after 1 April 2018.
- 1 April 2020 is the recommended application date for:
 - Investment income payers (other than PIEs) to provide detailed recipient information on the 20th of the month following the month in which the income is paid.
 - Investment income payers to include date of birth information (if held) in the detailed recipient information they provide.
 - Joint ownership information to be provided by investment income payers.
 - AIL and exempt recipient information to be provided.
 - 45% non-declaration rate for interest income.
 - Inland Revenue to provide a database of valid certificates of exemption.
 - Recipients of investment income to have a certificate of exemption to be exempt from withholding taxes on investment income.
 - Removal of the legislation containing the requirement to provide end of year tax certificates to customers.
 - Changes to allow errors relating to prior years to be corrected in the next return (for errors meeting thresholds), as well as improvements to error correction during an income year.
- Investment income payers will be able to elect to begin filing detailed recipient information on a monthly basis from 1 April 2019.

80. When introduced to Parliament, a bill commentary would be released explaining the amendments, and further explanation of their effect would be contained in a *Tax Information Bulletin*, which would be released shortly after the bill receives Royal assent.

81. Inland Revenue would administer the proposed changes. The proposals will have a range of administrative implications for Inland Revenue from needing to be able to process the information that is received to analysing the information and being able to proactively use the information to adjust tax rates. The proposed changes will also improve compliance, support the ability to make future changes to the social policy regime and enable Inland Revenue to reduce the time taken by Inland Revenue staff to complete tasks by better associating income information with each taxpayer’s tax records. Overall the proposed changes are expected to reduce administration costs for Inland Revenue.

MONITORING, EVALUATION AND REVIEW

82. Inland Revenue will monitor the outcomes of the changes pursuant to the Generic Tax Policy Process ("GTTP") to confirm that they match the policy objectives. The GTTP is a multi-stage policy process that has been used to design tax policy in New Zealand since 1995.

83. The final step in the process is the implementation and review stage, which involves post-implementation review of legislation, and the identification of remedial issues. Post-implementation review is expected to occur around 12 months after implementation. Opportunities for external consultation are built into this stage. Any necessary changes

identified as a result of the review would be recommended for addition to the Government's tax policy work programme.

84. Also, as part of Inland Revenue's business transformation programme a benefit management strategy has been developed and endorsed. The programme costs and benefit estimation approach is outlined in Appendix G of the November 2015 Programme Update and Detailed Business Case. The benefit management strategy provides the framework for managing benefits within the programme, and:

- defines benefit components;
- details how programme benefits will be quantified and measured;
- documents how progress will be tracked; and
- describes what governance arrangements will be in place.

85. Both internal and external stakeholders will be actively involved in the on-going assessment of timeframes, benefits identification and benefits realisation for each stage of the transformation programme.

APPENDIX A – GETTING IT RIGHT FROM THE START

86. In order for Inland Revenue to help taxpayers get their tax obligations right the first time, Inland Revenue needs:

- More frequent and in some cases more detailed information on the investment income the investor receives; and
- Identifying information where Inland Revenue is unable to establish the taxpayer's identity.

Status quo and problem definition – detail and frequency of investment income information

87. Currently, payers of investment income are required to deduct resident withholding tax (RWT) from interest and dividends when they are paid, and pay the RWT to Inland Revenue on the 20th of the following month. For PIEs, tax is generally paid to Inland Revenue at the end of the month following the month that an investor exits the PIE, or the month following the end of the year for all other investors.

88. These payments are due on the same date that payers of investment income must provide summary information to Inland Revenue. This summary information shows the total investment income paid and RWT/PIE tax deducted by the payer.

89. Information on each recipient, such as the income earned by the recipient and the tax withheld from that, isn't provided until:

- after the end of the tax year for interest subject to RWT or non-resident withholding tax (NRWT) and portfolio investment entity (PIE) income; or
- not at all for dividends, Māori authorities distributions and interest that is exempt or subject to AIL.

90. The provision of infrequent or in some cases no information means that Inland Revenue is unable to:

- Pre-populate tax returns and personal tax summaries – currently information is received by Inland Revenue too late (or not at all) to pre-populate tax returns. Anyone filing a tax return has to gather information about the interest, dividends and Māori authority distributions they have received from payers during the year and include it in their tax return. Taxpayers with multiple investments can end up with dozens of different tax certificates that they need to keep track of to understand their tax position. This is time consuming and, if information is missed out, can result in incorrect returns being filed. Payers provide the same information to their customers (and for interest to Inland Revenue) that the customers in turn provide to Inland Revenue if they file a tax return, which is inefficient.
- Accurately determine people's social policy entitlements/obligations during the year – social policy entitlements/obligations are based on estimates of income the taxpayer expects to receive for the relevant year. At the end of the year once the taxpayer's income is finalised, the taxpayer needs to perform a square-up. This imposes compliance costs on taxpayers and may also result in hardship for people who have

amounts to repay, or who did not receive their full entitlement during the year. Further, people can find it difficult to estimate their taxable income (which is the basis for their social policy calculations) as the amounts treated as taxable income for some types of income may be different from the actual return on investment. For example, for PIE funds invested solely in New Zealand shares the income for tax and social policy purposes does not reflect the return on investment because capital gains on shares are not income for tax purposes, resulting in taxpayers who use 'return on investment' as a measure of income overestimating their income. Often recipients of investment income are not informed of their taxable income until after the end of the tax year. As they have to estimate income before the start of the tax year for social policy purposes they may have to rely on the information they received for the year 2 years before the year they are making their estimate for. Because Inland Revenue does not receive income information during the year, it cannot adjust the taxpayer's social policy entitlements/obligations where the taxpayer's actual income is different from their estimate.

- Proactively correct errors and withholding tax rate choices – At the moment, a large proportion of taxpayers have tax withheld at the incorrect rate.⁶ It is not uncommon for taxpayers to select a withholding rate and forget to change it as their circumstances change. For the majority of tax types, taxpayers can square this up at the end of the year. However, for PIEs it is especially important to ensure the correct rate is being used. This is because if a taxpayer has selected a higher rate than their correct rate, the excess tax withheld cannot be refunded. If a lower rate is selected, the income must be included in the taxpayer's tax return and taxed at their marginal rate. This may result in more tax being paid than if the correct PIR had been selected as the top PIR is 28%, compared to the top marginal tax rate of 33%. As Inland Revenue does not receive investment income information during the year, it is unable to help taxpayers work out the appropriate tax rate for them, resulting in taxpayers being over or under-taxed.
- Redesign the social policies that it administers – social policy schemes are currently based on estimates of annual income (i.e. working for families), or income from previous tax years (i.e. child support). It would be much better if these schemes could use shorter calculation periods and could be based on the actual income the taxpayer receives.

Feedback from consultation – detail and frequency of investment income information

91. Submitters were generally supportive of providing more detailed information to Inland Revenue, however took issue with providing it more frequently. The majority felt that the costs of providing this information quarterly or monthly would outweigh the benefits. The general consensus was that as the majority of people do not receive much investment income,

⁶ In the 2015 tax year, 33% of taxpayers who filed an IR 3 or PTS had RWT withheld at a higher rate than their marginal tax rate, whereas 45% had RWT withheld at a lower rate. Of those taxpayers who did not file a return or PTS, 38% had RWT withheld at a higher rate than their marginal rate, and 37% had RWT withheld at a lower rate than their marginal tax rate.

the social policy benefits would be minor.⁷ Many submitters favoured providing the information annually as is the case now, or quarterly if a more frequent reporting requirement were to be introduced.

92. The provision of more frequent information for PIEs was especially controversial as many felt that reporting it on a more frequent basis would result in significant compliance costs but would not result in any meaningful social policy adjustments. PIE income can be volatile due to unpredictable movements in exchange and interest rates, and lumpy investment returns can mean that it can fluctuate from large positives to large negatives from month to month. Taking this income into account for social policy purposes would result in regular amendments to entitlements, making it difficult for people to budget and resulting in more work for the agencies responsible for managing social assistance. Further, given the nature of the PIE tax regime, taxpayers may have income for tax and social policy purposes despite not actually receiving any income⁸, or where they were in losses.⁹

93. Submitters also outlined that wholesale PIEs and locked in PIEs should be exempt from the requirements to provide more frequent information, given there would be no social policy benefit in obtaining this information.¹⁰

Options on obtaining more detailed investment income information

94. Two options have been considered for addressing the problem and achieving the main objective. The options are:

- Option 1: Status quo.
- Option 2: Require payers of investment income to provide taxpayer specific information to Inland Revenue (officials' preferred option).

Option 1 – status quo

95. Under this option the information provided by payers of investment income would remain unchanged.

Assessment against objective and criteria – option 1

96. The status quo does not meet the main objective as currently Inland Revenue is unable to prepopulate investment income in tax returns, determine social policy entitlements or proactively correct tax rates with reference to the investment income earned by the taxpayer (as the information is received too late or not at all depending on the tax type). The status

⁷ Statistics show that the average amount of investment income a taxpayer with some form of social policy obligation or entitlement receives is \$539 a year. This figure does not exclude income from locked in PIE funds such as KiwiSaver, which are excluded from social policy calculations, however, it does exclude any non-declared income that should be included in social policy calculations.

⁸ Due to the accrual nature of the financial arrangement rules and the foreign investment fund regime.

⁹ Foreign shares held by a PIE are taxed at 5% of their opening market value, regardless of whether the share price has gone up or down.

¹⁰ Clients of wholesale PIEs are not individuals, and locked-in PIE income is not taken into account for social policy purposes.

quo has not been assessed against the criteria as it is the option against which all other options are assessed.

Option 2 – require the provision of taxpayer specific information (preferred)

97. Under this option, payers would be required to provide the following information to Inland Revenue:

Payer of investment income	Information that will be required in the future	Information already provided that will continue to be required
Banks and other payers of interest	The same information as currently required.	Banks already provide the following information about individual taxpayers who are not exempt from RWT or have income subject to AIL: <ul style="list-style-type: none"> • The income earned • The tax withheld.
PIEs	The same information that is currently required.	Like banks, PIEs already provide individual taxpayer information regarding income earned and tax paid.
Companies	Information about individual recipients regarding income earned and tax withheld, including any imputation credits attached to dividends. Currently Inland Revenue only receives summary information from companies (i.e. total dividends paid and tax withheld for all taxpayers, not broken up by taxpayer).	Only summary information is provided.
Maori authorities	Similar to companies, except instead of dividend and imputation credit information, information will be required on Māori authority distributions and any Māori authority credits attached to those distributions.	Only summary information is provided.

98. As shown in the above table, only some investment income payers would be required to provide more information. The key change proposed for all payers of investment income is how frequently that the information will need to be provided (see the next section).

99. Note that this table does not cover all the information that payers of investment income would need to provide. They would also need to provide information to help Inland Revenue identify the recipient of the income (such as date of birth, IRD number, name and address). This is discussed in the identifying information section at paragraph 109. Detailed recipient information will also be required for income that is exempt or subject to AIL. As obtaining

this information is more about determining the identity of the taxpayer in order to determine whether the payment or AIL/exempt income is appropriate, as opposed to using the information for tax and social policy purposes, it has been discussed under the identifying information section.

Assessment against objective and criteria – option 2

- Main objective: This option meets the main objective as receiving taxpayer specific information helps Inland Revenue make it easier for taxpayers to comply with their obligations, for example, by prepopulating tax returns, more accurately determining social policy entitlements and proactively correcting tax rates. It also creates opportunities for the Government to consider how best to deliver and administer social assistance.
- Fairness & equity: This option represents a significant improvement on the status quo as it makes it easier for Inland Revenue to proactively correct people's tax rates and determine their social policy entitlements. This ensures that more people are taxed at a rate appropriate for them, and receive the correct entitlements – reducing the disadvantage that people unaware of the tax rules face in dealing with the tax system.
- Efficiency of compliance and administration: This option represents a partial improvement on the status quo. While it would help to reduce the compliance costs of taxpayers by prepopulating tax returns and more accurately determining social policy entitlements/obligations, the provision of more information would increase compliance costs for investment income payers at least initially while systems were set up. There is not expected to be any significant long-term increase in compliance costs as they are providing information they already hold. For Inland Revenue this change would reduce administrative costs as more income information would be able to be automatically associated with the recipient's tax record. Inland Revenue expects be able to process the additional information for minimal cost due to the work being undertaken in the Business Transformation programme.
- Sustainability of the tax system: This option represents a significant improvement on the status quo as it would improve Inland Revenue's ability to ensure tax and social policy payments were correct the first time around.

Options on obtaining more frequent investment income information

100. Four options have been considered for addressing the problem and achieving the main objective. The options are:

- Option 1: Status quo.
- Option 2: Payers to provide investment income information in the month following the month in which the income was paid – this is aligned with the process of paying the income and withholding tax and for monthly filers will occur at the same time as summary returns are currently provided.
- Option 3: Payers to provide investment income information by the 20th of the month following the **quarter** in which the income was paid for interest, dividends and taxable Maori authority distributions. Provision of PIE information remains at the end of the year (although by 15 May rather than 31 May for non-locked in PIEs and

interest¹¹ as well as 6 monthly reporting of PIRs for all PIEs). Payers of interest income that has been treated as exempt must provide recipient information yearly. Payers of interest income that are required to remit tax to Inland Revenue less often than quarterly will be required to provide information to Inland Revenue on a quarterly basis but will still remit the tax less frequently.

- Option 4: Payers to provide investment income information by the 20th of the month following the **month** in which the income was paid for interest, dividends and taxable Maori authority distributions. Provision of PIE information remains at the end of the year (although by 15 May rather than 31 May for non-locked in PIEs and interest as well as 6 monthly reporting of PIRs for all PIEs). Payers of interest income that has been treated as exempt must provide recipient information yearly. Payers of interest income that are required to remit tax to Inland Revenue less often than monthly will be required to provide information to Inland Revenue on a monthly basis but will still remit the tax less frequently.

Option 1 – status quo

101. Under this option, the frequency that payers of investment income would be required to provide information to Inland Revenue would not change. This means that taxpayer specific information would not be provided to Inland Revenue until after the end of the tax year (for interest and PIE income) or not at all (for dividends, Māori authorities distributions and interest that is exempt or subject to AIL).

Assessment against objective and criteria – option 1

102. The status quo does not meet the main objective as information is not received often or early enough to enable Inland Revenue to help people to get their tax right from the start (i.e. tax returns cannot be prepopulated and social policy entitlements and tax rates cannot be proactively corrected during the year). Furthermore, it means that the Government cannot reconsider how best to administer and deliver social assistance. The status quo has not been assessed against the criteria as it is the option against which all other options are assessed.

Option 2 – month following the month the income was paid

103. Under this option, detailed investment income information would be provided to Inland Revenue on the 20th of the month following the month the income was paid for interest, dividends and Maori authority distributions¹², and the end of the month for PIE income.

Assessment against objective and criteria – option 2

- **Main objective:** This option meets the main objective as receiving information earlier would make it easier for taxpayers to comply with their tax obligations.

¹¹ 15 May end of year reporting for interest is a transitional measure to get the information earlier to facilitate pre-population until monthly reporting comes in from 1 April 2020.

¹² Note that currently summary information on Maori authority distributions is not provided until after the end of the tax year.

- **Fairness & equity:** This option represents a significant improvement on the status quo as all taxpayers are treated equally and a reasonable time period is given to provide the information.
- **Compliance & administration:** This option represents a partial improvement on the status quo as providing this information monthly to Inland Revenue would reduce compliance costs for recipients and administration costs for Inland Revenue, however, it would necessitate extensive upfront system changes for larger payers. It would be especially burdensome on PIEs to report investor level information monthly, as opposed to only when an investor exits the fund. This is because PIEs' systems are only set up to perform tax calculations at the end of the year for non-exiting investors and run a number of year end processes at the same time. Running monthly tax calculations would necessitate a significant system redesign to decouple the tax calculations from the other year end processes.
- **Sustainability of the tax system:** This option represents a partial improvement on the status quo. While receiving information more often improves Inland Revenue's ability to ensure customers get their tax affairs right from the start, the volatility of PIE income means that more frequent adjustments to social policy entitlements to take into account this income would be unhelpful.

Option 3 – quarterly tailored approach

104. Under this option, payers of investment income would be required to provide information on the 20th of the month following the **quarter** in which the income was paid for interest (including interest subject to AIL), dividends and taxable Maori authority distributions. PIE information would not have to be provided until the end of the year (although by the 15th of May as opposed to 31 May for PIEs where the funds are not locked in). All PIEs would be required to provide Inland Revenue with the PIRs of their investors every 6 months. Payers would be required to provide contact details yearly for recipients of income that was treated as exempt.

105. PIEs were excluded from the monthly reporting requirement because the volatile nature of PIE income (see paragraph 92) means that taking this income into account on a regular basis would be unhelpful. Another factor to take into account is the fact that PIE income from locked in PIEs such as KiwiSaver funds are not taken into account when calculating social policy obligations and entitlements. In addition, a number of PIEs have included their tax calculation in their year-end processes so would need to redesign these processes in order to run the tax calculation more frequently.

106. The requirement to provide yearly recipient information for recipients of income that has been treated as exempt is to allow Inland Revenue to check that this treatment was appropriate.

Assessment against objective and criteria – option 3

- **Main objective:** This option meets the main objective as receiving information earlier would make it easier for taxpayers to comply with their tax obligations.
- **Fairness & equity:** This option represents a significant improvement on the status quo. Whilst PIEs will have less onerous reporting obligations, this is warranted given the issues outlined in paragraphs 92 and 93.
- **Compliance & administration:** This option represents a partial improvement on the status quo as it will reduce compliance costs for recipients and administration costs for

Inland Revenue. However, providing this information more frequently would result in an upfront cost to change systems, although is not expected to result in significant ongoing compliance costs given payers are providing information they already hold.

- Sustainability of the tax system: This option represents a partial improvement on the status quo as receiving the information more frequently better allows Inland Revenue to prepopulate tax returns and adjust social policy obligations. However, receiving information quarterly would mean that adjustments to social policy would be made on a 3 month lag (see further explanation in paragraph 108) compared to receiving the information monthly.

Option 4 – monthly tailored approach (preferred)

107. Under this option, payers of investment income would be required to provide information on the 20th of the month following the month in which the income was paid for interest (including interest subject to AIL), dividends and taxable Maori authority distributions. PIE information would not have to be provided until the end of the year (although by the 15th of May as opposed to 31 May for PIEs where the funds are not locked in). All PIEs would be required to provide Inland Revenue with the PIRs of their investors every 6 months. Payers would be required to provide contact details yearly for recipients of income that was treated as exempt.

Assessment against objective and criteria – option 4

- Main objective: This option meets the main objective as receiving information earlier would make it easier for taxpayers to comply with their tax obligations.
- Fairness & equity: This option represents a significant improvement on the status quo as taxpayers in similar circumstances are treated in similar ways – i.e. companies would no longer receive preferential treatment as they would be required to provide taxpayer specific info at the same time as interest payers.. Whilst PIEs will have less onerous reporting obligations, this is warranted given the issues outlined in paragraphs 92 and 93.
- Compliance & administration: This option represents a partial improvement on the status quo. Providing this information more frequently would result in an upfront cost to investment income payers making payments to large numbers of recipients as they will need to make changes to their systems. The ongoing compliance costs for these payers to large numbers of recipients are not expected to be material given payers will use their systems to generate the information. This will, however, depend on whether automatic checks and reconciliations are built into the systems or continue to be done manually as is the case now. Investment income payers making payments to small numbers of recipients will be likely to have reduced compliance costs as they will be able to file their returns digitally. Administrative costs will also reduce.
- Sustainability of the tax system: This option represents a significant improvement on the status quo as the frequency of the receipt of the information under this option would best help customers get it right from the START.

Monthly vs quarterly argument

108. Monthly reporting is favoured over quarterly reporting for the following reasons:

- Quarterly reporting would limit Inland Revenue's ability to redesign how social policy is delivered as it makes it more difficult to align income received with any potential changes to social policy income calculation periods.
- Quarterly reporting will result in a delay of at least 3 months as the reporting is done after the end of the quarter and the income calculation for social policy is completed before the start of the period – i.e. if social policy was also calculated quarterly the quarter April – June couldn't be part of July's social policy adjustment as the information wouldn't be reported until 20 July and the calculation would have to have been completed by 1 July. With monthly reporting, the information for April and May would have been received and would be taken into account in the July adjustment. Investment income reporting and social policy calculations are based on the 31 March income year so offsetting the quarters would lead to a number of other issues and costly reconciliations.
- The key compliance cost is the initial system changes required to enable more frequent reporting. Provided these changes are made with a view to automating checks and reconciliations as much as possible then the ongoing period by period costs will be significantly less than the costs large investment income payers incur with their current year end processes. One large financial institution noted in their submission that the difference in compliance costs between quarterly and monthly reporting "would be marginal as systems changes would be needed either way".
- Monthly reporting aligns with the business process of paying the tax to Inland Revenue. Currently Inland Revenue receives payments monthly but no detailed information so has no way of knowing who the tax is attributable to until the end of the year. The change would mean that Inland Revenue would get detailed information relating to the payment with the payment.

Status quo and problem definition - Identifying information

IRD numbers/increased non-declaration rate

109. Inland Revenue has difficulty attributing income to a taxpayer if Inland Revenue does not have the taxpayer's IRD number. Around 20% of the interest certificates received by Inland Revenue do not contain the recipient's IRD number. For other income types this is a lot lower – for example only 2% for PIE income.

110. Currently, taxpayers are not incentivised to provide their IRD number to Inland Revenue as the non-declaration rate, the rate that applies to taxpayers who do not declare their IRD number, is too low. The non-declaration rate is:

- 33% for interest, dividends and Māori authority distributions over \$200, and
- 28% for portfolio investment entity (PIE) income.

111. These rates equal the top marginal tax rates for the respective income types. As a result, these rates do not incentivise taxpayers on the top marginal tax rate to provide their IRD number. Further, taxpayers with social policy entitlements or obligations may have much higher effective tax rates (taking into account abatement of entitlements or additional

obligations) and may realise that by not providing their IRD number, it is unlikely that their investment income will be taken into account when social policy entitlements/obligations are calculated. This may mean they receive more social assistance or pay less in child support and student loan repayments than they should.

Example

Laura is a single mother with sole custody of her two children. She earns \$50,000 a year and has a student loan. She invested some money from an inheritance which returns her \$5,000 income a year. She has not provided her IRD number to her investment income payer. As a result, Laura would receive \$1,352 per year more in working for families than otherwise entitled, and pay \$600 less off her student loan per year than otherwise required, if she does not return this income

Date of birth information

112. Currently Inland Revenue receives the recipient's IRD number (if held by the payer), name and address information only as identifying information. Date of birth information can help Inland Revenue determine the IRD numbers of non-declared taxpayers. Some people use multiple spellings or versions of their name and it isn't uncommon for two or more people to have the same name. People can also give incorrect IRD numbers by mistake. Date of birth information can also help to identify these people.

Example

Jenny and her mother Jane have the same surname and live at the same address. Jenny hasn't given her interest payer her IRD number, but her mother has supplied hers. There is a risk that Jenny's investment income could be matched with her mother's Inland Revenue records. Inland Revenue could allocate their income to the right accounts if their dates of birth were provided by their investment providers.

Joint accounts

113. Each of the owners of a joint investment is taxable based on their share of ownership of the investment. It is important to accurately allocate the income to each owner to ensure that their tax and social policy obligations and entitlements are correctly calculated.

114. Currently Inland Revenue is only provided with one IRD number and contact details for a joint account. This makes it hard to allocate income between the owners. Unless all joint account owners file tax returns, tax is withheld at the tax rate chosen by the owner whose IRD number is associated with the account. This can result in the income being over or under taxed where the owners are on different marginal tax rates or an inappropriate rate is chosen.

Example

David and Danielle have a joint account earning \$2,000 income a year. David is on a 33% marginal tax rate, whereas Danielle is on a 10.5% rate. Because David's IRD number is associated with the account, Danielle's share of the income is taxed at 33%, rather than 10.5%, and Danielle has to file a tax return to claim back the additional \$225 tax that is withheld.

Identifying information for AIL and exempt income

115. Inland Revenue does not receive any information on the recipients of income subject to AIL, so is unable to check that the payment of AIL is appropriate. A person may have elected to have AIL apply to their investment when they are a non-resident for tax purposes and may have forgotten to change back to RWT on their return to New Zealand. Getting AIL information will enable Inland Revenue to check whether other information indicates that a recipient being treated as subject to AIL is actually a New Zealand tax resident.

116. Inland Revenue also receives no information on the recipients of exempt income. This means that Inland Revenue is unable to check that recipients of income that is treated as exempt are actually eligible for this treatment. While other proposals such as providing a certificate of exemption database will help payers of investment income to determine whether recipients are validly being treated as exempt, the provision of recipient information for income that has been treated as exempt will enable Inland Revenue to proactively check compliance in this area and advise payers and recipients if exemptions are being invalidly applied.

Feedback from consultation – IRD numbers/non-declaration rate

117. The discussion document proposed raising the non-declaration rate in order to encourage the provision of IRD numbers. While some submitters supported this proposal, the majority of submitters were strongly opposed to this. The main points raised by submitters were:

- The costs to implement the changes would be substantial.
- The 45% rate will be too high for the majority of taxpayers who do not have significant social policy entitlements/obligations to justify a 45% rate. For the majority it would be a penal rate that would punish the unsophisticated.
- The non-declaration rate isn't the solution to what is essentially a data matching problem. A better solution would be to require an IRD number to be provided before the investor could use their account.
- The aim of a withholding tax system should be to achieve payment of the recipient's expected income tax liability on an annual basis – no more. Increasing the non-declaration rate seems contrary to the policy behind business transformation as it would result in more taxpayers filing returns at the end of the year to claim back the excess tax.
- Retirement savings PIEs should not be subject to a 45% non-declaration rate as this type of PIE income is not taken into account for social policy purposes. Further, overpaid PIE tax on retirement savings which are subsequently recovered when the individual files a return would be unlikely to be returned to the taxpayer's retirement account.
- This proposal would increase compliance costs for financial institutions as they would be the first port of call for complaints.
- This proposal shifts the costs of policing IRD numbers from investors and Inland Revenue to payers of investment income.
- Wholesale PIEs should be exempt from applying the increased non-declaration rate as it would be unnecessary for them to incur the cost to build it into their system when it is unlikely to ever apply given the type of investors who invest in wholesale PIEs (i.e. superannuation funds and other sophisticated non-individual investors).

- The non-declaration rate should not apply to investors who legitimately do not require IRD numbers, such as non-residents and exempt persons.
- Taxpayers taxed at the non-declaration rate should not be able to receive PIE losses cashed out at 45%.

Feedback from consultation – date of birth information

118. The provision of date of birth information to Inland Revenue was supported where payers held that information. There was a consensus that this should be a legislative requirement in order to overcome any privacy concerns.

Feedback from consultation – joint accounts

119. Submitters were supportive of providing identifying information of joint account owners where payers of investment income held that information. Payers cautioned that they would be unable to split the income between the joint investors.

Feedback from consultation – AIL and exempt income

120. The majority of submitters did not support providing this information for the following reasons:

- System amendments would be required to provide this information.
- AIL information will be provided under the AEOI reporting requirements when these come into effect.
- The information will not be used for auditing non-compliance, rather than prepopulating returns or adjusting social policy payments, so could be provided annually.

Options in relation to obtaining IRD numbers

121. Three options have been considered to make changes to the non-declaration rate to increase the provision of IRD numbers to Inland Revenue. The options are:

- Option 1: Status quo.
- Option 2: 45% non-declaration rate for all investment income types.
- Option 3: 45% non-declaration rate just for interest income. For PIEs a taxpayer would need to provide their IRD number before the PIE would allow them to open an account, but a 45% non-declaration rate would not apply. For companies and Maori authorities, the non-declaration rate would remain at 33% (preferred option).

Option 1 – status quo

122. Under this option the non-declaration rate would remain unchanged.

Assessment against objective and criteria – option 1

123. The status quo does not meet the main objective as the non-declaration rate is too low to encourage taxpayers to provide their IRD numbers. Where Inland Revenue does not have a taxpayer's IRD number, it is unable to help the taxpayer get it right from the start, for example by prepopulating investment income. The status quo has not been assessed against the criteria as it is the option against which all other options are assessed.

Option 2 – 45% non-declaration rate for all types of investment income

124. Under this option, the non-declaration rate would be increased to 45% for interest, dividends, Māori authority distributions and PIE income.

Assessment against objective and criteria – option 2

- **Main objective:** This option meets the main objective as increasing the non-declaration rate to 45% encourages taxpayers to provide their IRD numbers, which helps Inland Revenue simplify the tax system by prepopulating income and proactively correcting withholding rates and social policy payments.
- **Fairness & equity:** This option represents a significant improvement on the status quo as it treats all taxpayers equally. The status quo could be seen as unfair as a 45% non-declaration rate applies to income from salary and wages, but not to investment income.
- **Compliance & administration:** This option represents a partial improvement on the status quo. A 45% non-declaration rate will reduce Inland Revenue's administrative costs in determining a taxpayer's identity, as more taxpayers will provide their IRD number. However, compliance costs will increase for payers who will need to set their systems up to withhold tax at 45%. This is especially burdensome for companies (whose systems are set up to withhold tax at only one rate as all dividends have tax withheld at 33%) and for Māori authorities (due to administrative and system constraints).
- **Sustainability of the tax system:** This option represents a partial improvement on the status quo. While the tax system is more sustainable where income can be allocated to the correct taxpayer, a 45% rate would overtax people who did not have social policy entitlements or obligations and they would be required to file an annual tax return to ensure the income is taxed at the correct rate. It would also increase the complexity of the tax system as non-declared recipients of PIE income would have to file tax returns in order to get the excess tax back. In addition it would mean that PIE losses could get refunded at 45% whereas recipients could file tax returns to ensure their PIE income was taxed at no more than 33%.

Option 3 – 45% non-declaration rate for interest, new account restriction for PIEs (preferred)

125. Under this option, the non-declaration rate would be increased to 45% for interest income. For PIEs a taxpayer would need to provide their IRD number before the PIE would allow them to open an account, but a 45% non-declaration rate would not apply. There would be exceptions for investors that certify they are non-resident, who provide their tax identification number from the country in which they are resident, and who don't have an IRD number. For companies and Maori authorities, the non-declaration rate would remain at 33%.

126. A 45% non-declaration rate was considered appropriate for interest income as 20% of the recipients of this income have not provided their IRD number. Further, interest is the largest form of investment income. Inland Revenue will work with payers of interest income to identify the IRD numbers of non-declared investors prior to the introduction of the increased non-declaration rate.

127. It was not considered appropriate to impose a 45% non-declaration rate on PIE income because:

- The increased compliance costs for payers would not be justified as only 2% of recipients of PIE income have not provided their IRD number.
- It would create issues for retirement savings and losses as identified in feedback received (see paragraph 117).
- It would be inappropriate for wholesale and locked-in PIEs (see paragraph 117).

128. A 45% non-declaration rate was not considered favourable for companies and Māori authorities due to systems constraints (see analysis on option 2). We have not recommended that the provision of an IRD number is a requirement for all new investments in companies as we are unable to determine the extent of non-declaration problem until we receive detailed recipient information. If future data shows non-declaration to be a problem, then a measure will be considered. This will also provide companies with sufficient time to get used to the proposed increased reporting requirements (which will represent a significant change for companies given they currently do not report taxpayer specific information at all), before additional requirements are imposed.

Assessment against objective and criteria – option 3

- Main objective: This option partially meets the main objective as compliance with the tax system is not encouraged for taxpayers with income not subject to the increased non-declaration rate or rule for new accounts (i.e. dividends and Māori authority distributions).
- Fairness & equity: This option represents a partial improvement on the status quo. While it gives preferential treatment to companies and Māori authorities, it does improve non-declaration measures for interest and PIE income.
- Compliance & administration: This option represents a significant improvement on the status quo. While there will be transitional compliance costs for interest payers who need to set up their systems to withhold tax at 45%, Inland Revenue's costs associated with determining a taxpayer's identity will reduce. Payers of other types of investment income will not have increased costs under this proposal.
- Sustainability of the tax system: This option represents a significant improvement on the status quo as the tax system is more sustainable where income, tax and social policy payments can be allocated to the correct taxpayer and where the withholding tax system, as far as is appropriate, withholds tax at a rate that approximates the taxpayer's final tax liability.

Options on obtaining date of birth information

129. Three options have been considered for addressing the problem and achieving the main objective. The options are:

- Option 1: Status quo.
- Option 2: Date of birth information to be provided if held by the payer (officials' preferred option).
- Option 3: Date of birth information is requested from the payer if it is needed by Inland Revenue for data matching.
- Option 4: Date of birth information is required to be provided by payers

Option 1 – status quo

130. Under this option, the current rules would stay the same – that is, investment income payers would not be required to provide their clients dates of birth, even if they held them.

Assessment against objective and criteria – option 1

131. The status quo does not meet the main objective as not receiving date of birth information may hinder Inland Revenue's ability to identify taxpayers – therefore preventing Inland Revenue from helping that taxpayer get their tax affairs correct from the beginning. The status quo has not been assessed against the criteria as it is the option against which all other options are assessed.

Option 2 – date of birth to be provided if held (preferred)

132. Under this option, payers of investment income would be required to provide date of birth information provided it was held by the payer of the investment income. In other words, the payer would not need to actively obtain date of birth information from its customers.

Assessment against objective and criteria – option 2

- **Main objective:** This option partially meets the main objective as receiving date of birth information for some taxpayers will improve Inland Revenue's ability to identify those taxpayers, and therefore put Inland Revenue in a better position to help customers get their tax affairs right from the start. This option does not fully meet the main objective as date of birth information would not be provided in some circumstances where it was needed (i.e. where Inland Revenue needed it to confirm a taxpayer's identity, but it was not held by the payer).
- **Fairness & equity:** This option represents a significant improvement on the status quo as it improves equity by improving Inland Revenue's ability to identify taxpayers.
- **Compliance & administration:** This represents a significant improvement on the status quo as it reduces administrative costs by making it easier for Inland Revenue to identify taxpayers, and has minimal impact on compliance costs as it only asks investment income payers to provide information they already hold.
- **Sustainability of the tax system:** This option represents a partial improvement on the status quo as while date of birth information is received for some taxpayers, it is not received for all taxpayers that it is needed for. While financial institutions collect date of birth information from customers as part of their Know Your Customer processes (anti money laundering), they may not hold date of birth information for customers that began investing with them before these processes were required. The tax system

is more sustainable where income can be matched to the relevant taxpayer, as otherwise the person could be receiving social policy payments that they are not entitled to, or paying less in social policy obligations than required.

Option 3 – date of birth to be provided on request if needed

133. Under this option, payers of investment income would only be required to provide date of birth information (provided it was held by the payer of the investment income) where Inland Revenue identified that it was needed for data matching and made an information request.

Assessment against objective and criteria – option 3

- Main objective: This option partially meets the main objective as Inland Revenue could request and would receive date of birth information for some taxpayers. This would improve Inland Revenue's ability to identify those taxpayers, and therefore put Inland Revenue in a better position to help customers get their tax affairs right from the start. This option does not fully meet the main objective as date of birth information would not be provided in some circumstances where it was needed (i.e. where Inland Revenue needed it to confirm a taxpayer's identity, but it was not held by the payer).
- Fairness & equity: This option represents a significant improvement on the status quo as it treats all investment income payers equally.
- Compliance & administration: This option is worse than the status quo as it requires Inland Revenue to go through additional processes to identify situations where the additional date of birth information is required and then prepare information requests (the date of birth information may not just be useful for Inland Revenue data matching but may also assist with cross Government information sharing which could mean the need for the information was not discovered until sometime later). Investment income payers would then have to process the large information requests (with 20% of interest certificates non-declared the requests would be large). These additional processes would give rise to much higher compliance and administrative costs than requesting the information as part of the regular reporting process.
- Sustainability of the tax system: This option represents a partial improvement on the status quo as while date of birth information is received for some taxpayers, it is not received for all taxpayers that it is needed for. The tax system is more sustainable where income can be matched to the relevant taxpayer, as otherwise the person could be receiving social policy payments that they are not entitled to, or paying less in social policy obligations than required.

Option 4 – date of birth to be provided

134. Under this option, payers of investment income would be required to provide date of birth information. This would mean that the payer would need to actively try to obtain date of birth information from its customers where the payer does not already hold that information.

Assessment against objective and criteria – option 4

- Main objective: This option does not meet the main objective as requiring payers to provide date of birth information even when they did not hold it would make it extremely difficult for payers to comply.
- Fairness & equity: This option is about the same as the status quo as it improves equity by improving Inland Revenue’s ability to identify taxpayers but it is unfair as it makes it extremely difficult for payers to be compliant.
- Compliance & administration: This is worse than the status quo as while it reduces administrative costs by making it easier for Inland Revenue to identify taxpayers, it would have a significant impact on compliance costs as it asks investment income payers to provide information they do not hold and that they would be likely to have great difficulty in getting from some customers.
- Sustainability of the tax system: This option is worse than the status quo as while date of birth information is received for some taxpayers, it is not received for all taxpayers that it is needed for and it makes payers non-compliant. The tax system is more sustainable where income can be matched to the relevant taxpayer, as otherwise the person could be receiving social policy payments that they are not entitled to, or paying less in social policy obligations than required. It is also more sustainable where requirements are reasonably able to be complied with as making ordinarily compliant participants in the tax system non-compliant can negatively affect their willingness to constructively engage with the tax system going forwards.

Options in relation to joint accounts

135. Three options have been considered for allocating income between joint investment owners. The options are:

- Option 1: Status quo.
- Option 2: The investment income payer splits the income and tax among the owners according to their ownership proportions, and passes this information on to Inland Revenue, as well as identifying details for each owner.¹³
- Option 3: The investment income payer informs Inland Revenue that the taxpayers are operating a joint account, and provides details of all account owners. Inland Revenue prepopulates their income based on equal shares (officials’ preferred option).

Option 1 – status quo

136. Under this option there would be no changes. This means that income from a joint account would only be allocated to the owner whose IRD number is associated with the account and each owner would need to file a tax return to square this up at the end of the year.

¹³ As was mentioned above Inland Revenue currently only receives one IRD number for a joint account. IRD numbers and contact information would be required for all owners of the account.

Assessment against objective and criteria – option 1

137. The status quo does not meet the main objective as it imposes an unnecessary requirement on joint account owners to file a tax return. The status quo has not been assessed against the criteria as it is the option against which all other options are assessed.

Option 2 – payer splits by ownership proportion

138. Under this option, the investment income payer would split the income and tax withheld among the owners of the joint investment in accordance with their ownership proportions, and pass this, as well as identifying information for each owner, on to Inland Revenue.

Assessment against objective and criteria – option 2

- **Main objective:** This option represents a significant improvement on the status quo as income and tax would be correctly prepopulated provided joint account owners informed their investment payer of their ownership proportions.
- **Fairness & equity:** This option represents a significant improvement on the status quo as the tax system is more equitable where information is pre-populated for taxpayers. This is because taxpayers who are unsophisticated or who cannot afford a tax agent are not disadvantaged.
- **Compliance & administration:** This option is worse than the status quo as it would impose compliance costs on payers to gather the ownership proportions from the investors and would result in expensive and complicated changes to payers' systems to enable the calculation of tax at split rates.
- **Sustainability of the tax system:** This option represents a significant improvement on the status quo as the tax system is more sustainable where income and tax is prepopulated for taxpayers.

Option 3 – Inland Revenue prepopulates equal shares (preferred)

139. Under this option, the investment income payer will inform Inland Revenue that the taxpayers are operating a joint account, and provide details of all account owners. Inland Revenue prepopulates their income based on the assumption that the investment is held in equal shares. This would be correct for a significant number of joint accounts. Where this is not the case, the investors will need to inform Inland Revenue of their share of income as part of the annual tax return process. As with the status quo, tax would be withheld at one rate, so a square up would be required where the taxpayers were on different marginal rates.

Assessment against objective and criteria – option 3

- **Main objective:** This option partially meets the main objective as the income would be prepopulated correctly where the investment was held in equal proportions (this is the most common ownership proportion). The taxpayers may still have an end of year debt or payment obligation though as tax would still be withheld at one rate.
- **Fairness & equity:** This option represents a significant improvement on the status quo as prepopulating tax returns ensures unsophisticated taxpayers are not disadvantaged.
- **Compliance & administration:** This option represents a partial improvement on the status quo. Compliance costs are reduced relative to the status quo as not all joint investment owners will need to square up at the end of the year. However, owners who do not hold the investment in equal shares or who are on different marginal tax rates will be required to perform a square up.

- **Sustainability of the tax system:** This option represents a partial improvement on the status quo. While the tax system is more sustainable where information is prepopulated, a square up will be required if the investors do not own the investment equally, and if they are on different marginal tax rates.

Options in relation to contact details of recipients of income subject to AIL or treated as exempt

Identifying information for recipients of income subject to AIL and income that is treated as exempt

140. The following options were considered for obtaining the identity of recipients of exempt income or income subject to AIL.

Options	Analysis against the objective and criteria
Option 1 – Status quo.	Doesn't meet the main objective
Option 2 – Detailed recipient information obtained for exempt income and income subject to AIL.	Meets the main objective Fairness & equity: ✓✓ Compliance and administration: ✓x Sustainability: ✓✓ Overall comment: Significant improvement on status quo
Option 3 – Detailed recipient information obtained for exempt income and income subject to AIL, but carving out any information already provided under AEOI.	Partially meets the main objective Fairness & equity: ✓✓ Compliance and administration: xx Sustainability: ✓x Overall comment: Improvement on status quo

141. Three options have been considered for obtaining the identity of recipients of exempt income or income subject to AIL. The options are:

- Option 1: Status quo.
- Option 2: The investment income payers provide detailed recipient information for investment income subject to AIL (on New Zealand issued debt) or treated as exempt to Inland Revenue.
- Option 3: Investment income payers to provide detailed recipient information for investment income that is exempt subject to AIL (on New Zealand issued debt), but carving out any information already provided under AEOI.

Option 1 – status quo

142. Under this option there would be no changes. This means that Inland Revenue would not receive any recipient information in respect of investment income that has been subject to AIL or treated as exempt.

Assessment against objective and criteria – option 1

143. The status quo does not meet the main objective as recipients of investment income may be subject to an incorrect tax regime which will result in any tax that is being deducted being deducted at too low a tax rate. The recipients would then be required to file tax returns to correct their tax positions.

Option 2 – payer provides recipient information for investment income subject to AIL or treated as exempt (preferred option)

Under this option, the investment income payer would provide recipient information to Inland Revenue for investment income that was subject to AIL (on New Zealand issued debt) or was treated as exempt. Recipient information would include name and contact detail information, but also the income earned and tax withheld (if any).

Assessment against objective and criteria – option 2 (preferred option)

- **Main objective:** This option meets the main objective as Inland Revenue would be able to use the information to check that the recipients are validly being treated as subject to the applicable tax regime and could proactively inform the payer and the recipient if they were not.
- **Fairness & equity:** This option represents a significant improvement on the status quo as it treats all taxpayers equally.
- **Compliance & administration:** This option represents a partial improvement on the status quo as while it would reduce administrative costs by improving Inland Revenue's auditing function, it would impose some compliance costs on payers to provide the additional information, however, it would be similar information to the information provided for RWT and NRWT and should be able to be gathered using similar processes.
- **Sustainability of the tax system:** This option represents a significant improvement on the status quo as the tax system is more sustainable where taxpayers are taxed under the right tax regimes and at rates that approximate their actual tax liability. By limiting the AIL information to New Zealand issued debt this also means that investment income payers will not be asked for information that they cannot get or would have significant difficulty providing.

Option 3 – payer provides recipient information for investment income that is exempt or subject to AIL (but carving out information required to be provided under AEOI)

144. Under this option, the investment income payer would provide recipient information to Inland Revenue for investment income that was subject to AIL (on New Zealand issued debt) or was treated as exempt, however information already provided under AEOI would not need to be provided again. Recipient information would include name and contact detail information, but also the income earned and tax withheld (if any).

Assessment against objective and criteria – option 3

- **Main objective:** This option meets the main objective as Inland Revenue would be able to use the information to check that the recipients are validly being treated as subject to the applicable tax regime and could proactively inform the payer and the recipient if they were not.
- **Fairness & equity:** This option represents a significant improvement on the status quo as it treats all taxpayers equally.
- **Compliance & administration:** This option is worse than the status quo. During consultation officials were told that determining the information provided under AEOI and only providing the information not provided would entail higher compliance costs than just providing all AIL information. Officials were also told by financial institutions that they did not want to combine the reporting for FATCA and AEOI with the reporting proposals for investment income. As the information is already held by the investment income payer, it would be easier to provide all the information at once.
- **Sustainability of the tax system:** This option represents a significant improvement on the status quo as the tax system is more sustainable where taxpayers are taxed under the right tax regimes and at rates that approximate their actual tax liability. By limiting the AIL information to New Zealand issued debt this also means that investment income payers will not be asked for information that they cannot get or would have significant difficulty providing.

APPENDIX B – COMPLIANCE AND ADMINISTRATION COSTS

145. Inland Revenue wants to minimise the costs that taxpayer face complying with the tax system, as well as the costs to the government of administering the tax system. This is a key theme of Business Transformation as was outlined in the Green Paper. In relation to investment income, the following are areas where compliance and administration costs could be reduced:

Status quo and problem definition - compliance costs for taxpayers

Filing tax returns

146. The current process of filing a tax return is cumbersome as taxpayers are required to gather information about the interest, dividends and Māori authority distributions they have received from payers during the year and include it in their tax return. Taxpayers with multiple investments can end up with dozens of different tax certificates that they need to keep track of to understand their tax position. This is time consuming and, if information is missed out, can result in incorrect returns being filed.

Selecting a withholding rate

147. Currently, taxpayers need to have an indication of the income they will earn in the tax year in order to select an appropriate withholding rate. Often taxpayers will select a withholding rate and forget to change it as their circumstances change (or they may not realise that their income has reached a threshold that requires a higher tax rate), resulting in under or over taxation. This problem is exacerbated for PIE income as tax on PIE income is final. This means that if a rate higher than the correct rate is selected, the tax cannot be refunded. If a lower rate is selected, the income must be included in the taxpayer's tax return and taxed at their marginal rate, which may be higher than the top PIE rate of 28%. For other income types, a tax return must be filed where an incorrect withholding rate is used.¹⁴ Having to work out the appropriate withholding rate, update it as circumstances change, and file a tax return wherever an incorrect rate is used, entails significant compliance costs for taxpayers.

Example

Jack graduated university three years ago. While at university he had a marginal tax rate of 10.5%. This was the rate he used when he set up his bank account and KiwiSaver account. He is now on a 33% marginal rate and has forgotten to update his rate for his bank account and KiwiSaver account (which is a PIE). He must file a tax return to pay the extra tax that should have been withheld from his interest and PIE income. His PIE income will be taxed at 33%, despite the fact that the PIE top rate is only 28%. Depending on the investment income Jack earned, this could result in a sizeable tax bill.

148. Because Inland Revenue does not receive information throughout the year about the investment income of individual taxpayers, it is not able to calculate social policy payments during the year to reflect this income. As a result, a square-up calculation needs to be made at the end of the year when a person's income is finalised. This imposes compliance costs on

¹⁴ Provided the amount of income taxed at an incorrect rate exceeds \$200.

taxpayers and may also result in hardship for people who have significant amounts to repay, or who received too little during the year when they needed the assistance.

Example

Will and Eden have 4 children, earn \$50,000 and \$30,000 a year respectively, and both have student loans. During the year they received and invested a sizeable inheritance which returned them \$10,000 income in the income year. As Will and Eden did not include this income in their estimated income for the year they would have an end of year liability of \$3,592, consisting of \$2,392 working for families repayments and \$1,200 in student loan repayments.

Feedback from consultation – compliance costs for taxpayers

149. Submitters supported in principle the idea to reduce compliance costs for taxpayers by prepopulating returns, proactively advising of withholding rates and adjusting social policy entitlements/obligations. However they noted that a balance should be struck between compliance costs on payers and benefits to taxpayers. Inland Revenue should not strive for a utopia of having every taxpayer's tax and social assistance obligations perfect every time, all of the time. A "close enough is good enough" approach should be taken.

Status quo and problem definition - Compliance costs for payers of investment income

End of year tax certificates

150. Payers of resident withholding income are currently required to provide end-of-year tax certificates to the recipients of the income – such as year-end interest certificates, shareholder dividend statements, PIE investor statements and Māori authority distribution statements. These certificates set out the amount of income earned and tax deducted, which recipients can then include in their tax return. Payers also provide interest and PIE information to Inland Revenue after the end of the tax year. In other words, Inland Revenue receives the same information twice in some instances. This is inefficient. Providing end of year certificates also imposes compliance costs on payers of investment income which would be unnecessary if that information was already held by Inland Revenue and able to be viewed by the taxpayer during the year.

Certificates of exemption

151. Taxpayers holding certificates of exemption ("COEs") from RWT are entitled to be paid interest and dividends without having any tax deducted by the payer. The holder of the COE is required to provide a copy to the relevant withholder and must inform the withholder if their COE is cancelled. Cancellations and issues of COEs in the previous quarter are published in the New Zealand Gazette each quarter. Taxpayers exempt under other Acts other than the Income Tax Act 2007 and the Tax Administration Act 1994, for example the Education Act, are entitled to an exemption without needing to obtain a COE.

152. The current exemption process involves compliance costs for payers as they need to:

- receive exemption certificates from taxpayers;
- check the appropriate gazette to see if the taxpayer's certificate has been cancelled; and

- assess whether the customer can appropriately claim to be exempt under non-tax legislation.

Feedback from consultation – compliance costs for payers of investment income

Feedback from consultation - End of year tax certificates

153. Feedback was mixed on the proposal to remove the requirement for payers to provide end of year tax certificates to interest recipients who had provided their IRD number. About 40% of submitters supported removing the requirement, and the other 60% felt it should stay.

154. A common view was that the end of year tax certificate was necessary to enable taxpayers to verify the information that Inland Revenue held about them. Taxpayers have an obligation to confirm the correctness of their tax position under our self-assessment tax system, and the end-of-year tax certificate enables taxpayers to do that. Without the end of year tax certificate, taxpayers would have to go back to their bank statements to determine this for themselves, which would be significantly more difficult. Some investment income payers also felt that compliance costs would not decrease from removing this requirement as systems had already been set up to provide the certificates. Even if the requirement were removed, investors may continue to request end of year certificates.

Feedback from consultation – certificates of exemption

155. The discussion documents proposed introducing a searchable database of certificates of exemption from withholding tax, to enable payers of investment income to confirm that a customer was entitled to an exemption from RWT. It was also proposed that organisations exempt from RWT under other Acts would be required to apply for a certificate of exemption, and thus would be included on the database.

156. All submitters were in favour of having a certificate of exemption database. Some submitters cautioned that this proposal should not result in the removal of the requirement for investors to send a copy of their certificate of exemption to their investment income provider. Absent this requirement, costs for payers could increase as they would need to check all of their customers against the database to determine whether or not they were entitled to an exemption from RWT. Submitters were also supportive of requiring organisations exempt from RWT under other Acts to apply for a certificate of exemption.

Options – compliance costs for payers of investment income

Options – end of year tax certificates

157. Three options have been considered to reduce compliance costs for payers of investment income through making changes to the end-of-year tax certificate requirements:

- Option 1: Status quo
- Option 2: Remove the requirement to provide end of year interest certificates.
- Option 3: Remove the requirement to provide end of year interest certificates to customers who have provided their IRD numbers.

Option 1 – status quo

158. Under this option, payers of investment income would continue to be required to provide end of year tax certificates to all taxpayers.

Assessment against objective and criteria – option 1

159. The status quo does not meet the main objective as it complicates the tax system by requiring the same information to be provided to Inland Revenue twice. The status quo has not been assessed against the criteria as it is the option against which all other options are assessed.

Option 2 – removal of requirement to provide end of year interest certificates

160. Under this option, the requirement for payers to provide end of year interest certificates to their customers would be removed. Payers would still need to provide end of year certificates to recipients of PIE income, as well as certificates to recipients of dividends and Maori authority distributions when they were paid, and could continue to provide end of year interest certificates if they wished.

Assessment against objective and criteria – option 2

- Main objective: This option meets the main objective as it simplifies the tax system to some extent by removing the provision of duplicated interest income information.
- Fairness & equity: This option represents a partial improvement on the status quo as it treats taxpayers in similar circumstances in similar ways. While this option is inequitable in a sense as payers of dividends, PIE income and Maori authority distributions must continue to provide end of year tax certificates, this is arguably appropriate because the end of year tax certificate acts as a reminder to taxpayers that they have received this income. The regularity of interest income often means the taxpayer is already aware of when they are due to receive the income.
- Compliance & administration: This option represents a significant improvement on the status quo as it reduces compliance and administration costs relative to the status quo as payers of investment income do not need to provide end of year tax certificates to recipients of interest income and Inland Revenue does not receive the same information twice.
- Sustainability of the tax system: This option represents a partial improvement on the status quo. The tax system is more sustainable where costs are reduced, however under this option end of year interest certificates would not be provided to customers who have not provided their IRD number. Providing these certificates is important for these taxpayers as it acts as a reminder to file a return thereby allowing the taxpayer to claim back tax that has been over withheld as a result of the non-declaration rate applying.

Option 3 – removal of requirement to provide end of year interest certificates to customers who have provided their IRD number (preferred)

161. Under this option, the requirement for payers to provide end of year interest certificates to their customers would be removed for customers who had provided their IRD number. Payers would still need to provide end of year interest certificates to customers who had not provided their IRD number, in order to remind them to file a tax return (so that they would not be taxed at the non-declaration rate). Payers would still need to provide end of year

certificates for PIE income and would still need to provide certificates to recipients of dividends and Maori authority distributions when they were paid.

Assessment against objective and criteria – option 3

- Main objective: This option meets the main objective as it simplifies the tax system to some extent by removing the provision of duplicated interest income information where the taxpayer has provided their IRD number to the payer.
- Fairness & equity: This option represents a partial improvement on the status quo as it treats taxpayers in similar circumstances in similar ways. While this option is inequitable in a sense as payers of dividends, PIE income and Maori authority distributions must continue to provide end of year tax certificates, this is arguably appropriate because the end of year tax certificate acts as a reminder to taxpayers that they have received this income. The regularity of interest income often means the taxpayer is already aware of when they are due to receive the income.
- Compliance & administration: This option represents a significant improvement on the status quo as it reduces compliance and administration costs relative to the status quo as payers of investment income do not need to provide end of year tax certificates to recipients of interest income who have provided their IRD numbers, and Inland Revenue does not receive the same information twice.
- Sustainability of the tax system: This option represents a partial improvement on the status quo as the tax system is more sustainable where compliance and administrative costs are kept to a minimum.

Options – certificates of exemption

162. Two options have been considered to reduce compliance costs for payers of investment income by improving the process for checking whether a taxpayer is entitled to be exempt from withholding tax:

- Option 1: Status quo
- Option 2: Certificate of exemption database and require payers exempt under other acts to obtain a certificate of exemption

Option 1 – status quo

163. Under this option, payers of investment income would continue to be required to check the New Zealand Gazette to determine whether a taxpayer's certificate had been cancelled, and would still have to assess a taxpayer's eligibility to be exempt under non-tax legislation.

Assessment against objective and criteria – option 1

164. The status quo does not meet the main objective as the current certificate of exemption process is complicated and hard for payers of investment income to comply with. The status quo has not been assessed against the criteria as it is the option against which all other options are assessed.

Option 2 – certificate of exemption database and require payers exempt under other acts to obtain a certificate of exemption (preferred)

165. Under this option, Inland Revenue would establish a searchable database of certificates of exemption. This would enable payers of investment income to confirm the status of a COE holder via a simple search, and could reduce the risk of people incorrectly claiming RWT exempt status. It would also mean that taxpayers would no longer need to provide copies of their certificates to payers; however, they would still need to inform the payer that they are exempt. Taxpayers exempt under other acts would also be required to apply for a certificate of exemption, so that they were included on the database.

Assessment against objective and criteria – option 2

- **Main objective:** This option meets this objective as it simplifies the tax system by making it easier for investment income payers to determine whether a taxpayer is eligible for an exemption from withholding tax.
- **Fairness & equity:** This option represents a significant improvement on the status quo as all payers of investment income will be able to use the database, and all taxpayers who are exempt will be included on it.
- **Compliance & administration:** This option represents a partial improvement on the status quo. While it would reduce compliance costs for payers of investment income relative to the status quo, it would increase administrative costs for Inland Revenue who would need to administer the database. This increase in administration costs would be likely to be offset as having a database will result in Inland Revenue spending less on auditing whether recipients that are being treated as exempt are entitled to be treated as exempt.
- **Sustainability of the tax system:** This option represents a significant improvement on the status quo as it helps to increase transparency over who is entitled to be treated as exempt.

Status quo and problem definition – compliance costs for payers and administrative costs for Inland Revenue

Electronic filing

166. Further, a number of withholding returns are paper based (with no option of electronic filing). For those returns that are able to be filed electronically, there is no electronic filing threshold to require payers of a certain size to file electronically. Paper filing is slower, more expensive in terms of compliance costs for taxpayers and administrative costs for Inland Revenue and more prone to errors.

Error correction

167. Currently, payers of investment income are able to correct errors during the tax year that arise from the payer withholding too little tax¹⁵. This only applies to interest and income subject to NRWT, not to New Zealand dividends. In relation to errors arising from the payer

¹⁵ Section RA 11 of the Income Tax Act 2007.

withholding too much tax, errors can be corrected during the year for interest, dividends, Maori authority distributions, and income subject to NRWT¹⁶.

168. Payers are not able to correct errors during the year where the payer does not withhold enough RWT from a dividend. Nor are payers able to correct errors between tax years for any type of investment income. The inability to correct errors between years impacts heavily on PIEs, given PIEs generally only pay tax at the end of the year.

169. The current approach to error correction imposes significant compliance costs and administrative costs on Inland Revenue because instead of correcting the error in the next period by reducing or increasing the amount of the withholding, payers must re-file returns from the previous period. Errors also impose a monetary cost on investment income payers as they bear the cost where they have under-withheld in error from a taxpayer, but will refund the taxpayer the money where they have over-withheld in error. Further, UOMI is payable to Inland Revenue at 8.27% pa on underpayments of tax, but receivable from Inland Revenue at 1.62% on overpayments.

170. Currently, investment income payers report information for each individual period (i.e. interest payers provide summary information to Inland Revenue every month). This makes the correction of errors difficult as an amount needs to be added or subtracted from a subsequent period in the event of an error.

Feedback from consultation – compliance costs for payers and administrative costs for Inland Revenue

Feedback from consultation – electronic filing

171. The discussion document sought feedback on options to encourage investment income payers to file online.

172. Submitters were of the view that Inland Revenue should consult with the industry in order to determine an appropriate threshold above which investment payers must file electronically. It was suggested that over time, all information should be provided electronically.

Feedback from consultation – error correction

173. The discussion document proposed that investment income payers should be able to self-correct errors below the higher of:

- a simple dollar value threshold, or
- a percentage threshold based on the amount of withholding tax paid.

174. Submitters were also asked what they felt would be an appropriate threshold.

175. Submitters were supportive of the approach to use both a simple dollar threshold as well as a percentage threshold for correcting errors. The majority felt that there should be no dollar limit on errors that could be corrected during the tax year.

¹⁶ Section RA 12 of the Income Tax Act 2007.

Options – compliance costs for payers and administrative costs for Inland Revenue

Options – electronic filing

176. Three options have been considered to increase the electronic filing of investment income returns:

- Option 1: Status quo.
- Option 2: Online filing compulsory for all, with the ability to apply to the Commissioner for an exemption.
- Option 3: Online filing compulsory for large payers only.

Option 1 – status quo

177. Under this option there would be no threshold or mechanism to compel payers of investment income to file electronically.

Assessment against objective and criteria – option 1

178. The status quo does not meet the main objective as the provision of information via paper channels makes it more difficult for Inland Revenue to prepopulate tax returns and adjust social policy payments.

Option 2 – compulsory for all, with the ability to apply to the Commissioner for an exemption (preferred)

179. Under this option, it would be compulsory for all investment income payers to file electronically, however there would be the ability to apply to the Commissioner for an exemption, for example, where a payer was not able to access digital services or where the costs of electronic filing would be prohibitive.

Assessment against objective and criteria – option 2

- **Main objective:** This option meets this objective as electronic filing enables the provision of more frequent information which facilitates pre-population as well as social policy and tax rate adjustments.
- **Fairness & equity:** This option represents a partial improvement on the status quo. While this option is fair in a sense as all investment income payers are treated equally, it could be seen as unfair as it compels small payers to also file online even though they do not have the same resources at their disposal as large payers.
- **Compliance & administration:** This option represents a significant improvement on the status quo. While this option may involve some upfront compliance costs for payers who have not previously filed electronically, it will reduce compliance costs long term because of the efficiencies of online filing when compared to paper filing (for example, recipient information could be pre-populated in the online form for subsequent returns for payers to small numbers of recipients and the information would be able to be submitted at the touch of a button rather than having to post a form to Inland Revenue). Administrative costs for Inland Revenue will also reduce given the amount of paper forms it would have to process would dramatically reduce.

- **Sustainability of the tax system:** This option represents a significant improvement on the status quo as the tax system is more sustainable where information is received in a cheaper, faster and more efficient manner.

Option 3 – online filing compulsory for large payers only

180. Under this option, it would be compulsory for investment income payers who withhold above a certain amount of RWT a year (i.e. \$50,000) to file electronically.

Assessment against objective and criteria – option 3

- **Main objective:** This option partially meets this objective as electronic filing enables the provision of more frequent information which facilitates pre-population as well as social policy and tax rate adjustments. This option would leave a large number of payers to determine whether they wanted to file electronically or not.
- **Fairness & equity:** This option represents a partial improvement on the status quo as it treats taxpayers in similar circumstances in similar ways. There could be a slight unfairness at the margins of the threshold, but this occurs whenever a threshold is implemented.
- **Compliance & administration:** This option represents a significant improvement on the status quo. This option will result in a reduction of compliance and administration costs when compared to the status quo as it will compel larger payers to file online. However it will not result in as great a reduction as option 2 as there will still be a large number of payers filing one or two certificates.
- **Sustainability of the tax system:** This option represents a partial improvement on the status quo as it ensures more people provide their information to Inland Revenue in a manner that is cheaper, faster and more efficient. The improvement in sustainability is not as great as the improvement under option 2.

Options – error correction

181. Two options have been considered to improve error correction mechanisms for payers of investment income.

- Option 1: Status quo.
- Option 2: Unlimited error correction for all investment income types during the tax year, error correction subject to a threshold of the greater of \$2000 or 5% of the annual tax liability for correction between years.

Option 1 – status quo

182. Under this option there would be no changes to the error correction mechanisms currently available. In other words, there would be no ability to correct errors between years, but some ability to correct errors during the year.

Assessment against objective and criteria – option 1

183. The status quo does not meet the main objective as having to re-file a return in order to correct an error can result in unnecessary complexity. The status quo has not been assessed against the criteria as it is the option against which all other options are assessed.

Option 2 – unlimited error correction during the year, threshold for correction between years (preferred)

184. Under this option, payers of investment income would have no limit on the size of genuine errors that could be corrected in a subsequent period, provided the period in which the error arose and the period in which it was corrected were in the same tax year. Where the error period and the correction period were in different tax years, the error could only be corrected where it was less than \$2000 or 5% of the payer's annual withholding tax liability. Tax payable as a result of a genuine error will be treated as due in the period in which it was corrected. This means that no UOMI or penalties will accrue on the error amount.

Assessment against objective and criteria – option 2

- Main objective: This option meets this objective as more flexible error correction makes it easier for payers of investment income to comply with their withholding obligations.
- Fairness & equity: This option represents a significant improvement on the status quo as all payers of investment income will have the same error correction mechanisms available to them.
- Compliance & administration: This option represents a significant improvement on the status quo as more flexible error correction lowers compliance costs for investment income payers as they do not have to re-file previous periods. This also lowers administrative costs for Inland Revenue as Inland Revenue staff no longer need to process the re-filed return.
- Sustainability of the tax system: This option represents a significant improvement on the status quo as the tax system is more sustainable where payers are able to correct genuine errors easily and without penalty.

Options – error correction (period reporting)

185. In order to improve payers ability to correct errors, the following options in regards to reporting requirements were considered:

- Option 1: Status quo.
- Option 2: Year-to-date reporting

Option 1 – status quo (preferred for dividends and Maori authority distributions)

186. Under this option there would be no changes to the reporting method – payers would continue to report information for the period.

Assessment against objective and criteria – option 1

187. The status quo does not meet the main objective for income that accumulates over time such as interest or PIE income as filing information for each period makes it more difficult for payers of investment income to correct errors. The status quo does however work well for sporadic payments such dividends and Maori authority distributions. The status quo has not been assessed against the criteria as it is the option against which all other options are assessed.

Option 2 – Year-to-date reporting (preferred for interest and PIE income) (preferred)

188. Under this option, payers of investment income would report their information on a year-to-date basis. This means that, for example, reporting for the month of June would include the total reported for the entire tax year (i.e. April to June), as opposed to just the figures for June. This is most applicable to types of income that accumulate over time such as interest and PIE income

Assessment against objective and criteria – option 2

- Main objective: This option meets this objective for interest and PIE income as it facilitates improved error correction, which makes it easier for payers of investment income to comply with their obligations.
- Fairness & equity: This option is about the same as the status quo as payers of investment income in similar circumstances continue to be treated equally.
- Compliance & administration: This option represents a significant improvement on the status quo as compliance costs are reduced for investment income payers where error correction is made easier.
- Sustainability of the tax system: This option represents a significant improvement on the status quo as the tax system is more sustainable where tax compliance is made easier.