

POLICY AND STRATEGY

Tax policy report: Taxpayer advocate recommendation from the TWG

Date:	13 December 2018	Priority:	Medium
Security level:	In Confidence	Report number:	IR2018/762

Action sought

	Action sought	Deadline
Minister of Revenue	Agree to the recommendation Refer a copy of this note to the Minister of Finance	18 December 2018

Contact for telephone discussion (if required)

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13 December 2018

Minister of Revenue

Taxpayer advocate recommendation from the TWG

Purpose

1. This note briefs you on the recommendation from the Tax Working Group (TWG) in their interim report to establish an independent taxpayer advocate service. It also provides further information about what Inland Revenue currently does for small and unrepresented taxpayers, and seeks direction from you as to how you would like the recommendation from the TWG to be progressed by officials.
2. In their interim report, the TWG recommended the establishment of a taxpayer advocate service in response to a perceived concern about taxpayers not receiving the assistance they might require in dealing with Inland Revenue, particularly in the formal disputes process. The TWG noted:

The Group has also considered a proposal to establish a taxpayer advocate service that would assist certain taxpayers – such as low-income earners, small businesses and, individuals with English as a second language – in disputes with Inland Revenue. The advocate could play multiple roles, including the provision of advice, and facilitation and mediation services.

The Group believes that a taxpayer advocate could play a valuable role in the fair resolution of tax disputes. The service would need to be functionally independent from Inland Revenue in order to serve as a credible advocate for the taxpayer in dispute, but it might be able to draw on back-office support from Inland Revenue. The Group suggests the structure of a Departmental Agency would be most appropriate. It would be contained within Inland Revenue and report directly to the Minister of Revenue, rather than the Commissioner of Inland Revenue.

The Group recommends that the Government establish a taxpayer advocate service to assist with the resolution of tax disputes. The Group is also currently considering the merits of a truncated dispute resolution process for small disputes.

Extent and nature of the problem

3. The New Zealand tax system is premised on voluntary compliance and self-assessment. In practice this means that taxpayers file tax returns based on their understanding of how the tax laws apply to their circumstances.
4. Inland Revenue's approach to supporting taxpayers in understanding their tax obligations is to provide a broad range of advice products. These are described below. The formal disputes process (in the Tax Administration Act 1994) becomes relevant where taxpayers are unable to agree with Inland Revenue about the application of tax laws to their circumstances.
5. The extent and nature of the problem the TWG are seeking to address in their recommendation for an independent taxpayer advocate service is not immediately clear. Inland Revenue has received submissions noting that taxpayers are "burnt off" by the current formal disputes process because of the costs associated with it - largely the cost of obtaining external representation. This point was raised in a joint submission from the New Zealand Institute of Chartered Accountants (now Chartered Accountants Australia and New Zealand) and the New Zealand Law

Society to Inland Revenue in 2008. Following this submission and a discussion document, a number of operational changes were made to the formal disputes process. These changes are described in paragraphs 14 and 15.

Advice and assistance for small and unrepresented¹ taxpayers

6. Inland Revenue provides a broad range of advice products. These range from general advice (eg booklets and guides) through to taxpayer-specific advice (eg advice from the call centre, written guidance or in person). In addition to this, Inland Revenue provides several other services to small business in particular and these are outlined in the appendix. All this advice is provided to small taxpayers without charge.
7. One of the principles underpinning Inland Revenue's Business Transformation programme is that Inland Revenue should help taxpayers get things right from the start. This involves engaging with taxpayers at the right time to ensure taxpayers are best placed to accurately self-assess.
8. Disputes generally arise when Inland Revenue is reviewing a taxpayer's tax returns and the department identifies positions taken in tax returns that are inconsistent with Inland Revenue's view of the law. These issues may become subject to the formal disputes process if earlier agreement between the taxpayer and Inland Revenue is not possible.
9. As part of the Business Transformation policy work we noted that binding advice is difficult to obtain for small and unrepresented taxpayers, as the costs associated with obtaining a binding ruling from Inland Revenue can be quite significant. The Taxation (Annual Rates for 2018-19, Modernising Tax Administration, and Remedial Matters) Bill proposes that, starting 1 October 2019, the binding rulings regime will be more accessible to small-to-medium sized taxpayers, through a cheaper, more straightforward process which will not necessarily require the involvement of someone with specialist tax expertise to help complete the application forms.

The formal disputes process

10. The formal disputes process was introduced following the recommendations of the Richardson Committee in 1994. The purpose was to reduce the number of disputes by promoting an "all cards on the table" approach that would encourage the prompt and efficient resolution of tax disputes, promote early the identification of issues and ensure any litigation was well prepared for. The formal disputes process ensures that there is full and frank communication between the parties in a structured way within statutory time limits.
11. The formal disputes process is used as a last resort where taxpayers disagree with Inland Revenue about a substantive tax matter which cannot be resolved through the usual processes (ie in discussions with the relevant areas of Inland Revenue involved with the taxpayer's issue).
12. Inland Revenue does not assist taxpayers with the formal disputes process beyond providing information about matters of process (which includes the recent updating of the Inland Revenue website on disputes to make the process easier to understand) and the independent approaches adopted in the facilitation and adjudication phases. This is because of the potential conflict of interest involved.

¹ Unrepresented in this context refers to a taxpayer that does not engage the services of an accountant or tax advisor to help them manage issues that may arise with Inland Revenue. Measuring the number of unrepresented taxpayers is difficult as often taxpayers will only engage the services of an accountant or tax advisor when they are faced by an issue with Inland Revenue they need help with.

13. The formal disputes process starts with a notice of proposed adjustment (“NOPA”) and is followed by a notice of response (“NOR”) and a facilitated conference, after which the respective parties issue their statements of position (“SOP”) setting out the facts and arguments relevant to their case. Inland Revenue reviews the case through its independent Adjudication function and the taxpayer is usually issued with a reassessment if the review is in Inland Revenue’s favour. The taxpayer can then start challenge proceedings in either the Taxation Review Authority (TRA) or the High Court.
14. Several enhancements were made to the formal disputes process in 2010, including the introduction of facilitators to the conference phase. Facilitators are experienced, independent Inland Revenue staff who have not been directly involved in the dispute. The facilitation process has been positively received.
15. The other main change in 2010 was to provide clear administrative guidance about where the Commissioner, to reduce compliance costs for taxpayers, would agree to have a dispute “truncated” so that the full process did not need to be followed. Automatic agreement to truncation under the guidelines occurs when a dispute involves tax of less than \$75,000. This means that for smaller disputes only one exchange of disputes documentation is required, followed by a facilitated conference. After the conference, the taxpayer can choose to take the case to court.
16. However, there is no easy answer to reducing costs associated with the formal disputes process for small and unrepresented taxpayers because it deliberately demands engagement between taxpayers and Inland Revenue. Further, the process requires identification of the facts and arguments to support understanding and resolution of the issue, and taxpayers will generally wish or need to be represented.
17. Statistically, we note that the number of cases that make it to the formal disputes process is quite low. On average over the past three years, the number of NOPAs issued was close to 500 per annum. The number of NOPAs reflects the fact that the Commissioner must issue a NOPA in order to reassess a taxpayer’s self-assessment and that taxpayers who have failed to file a return (and accordingly have been issued with a default assessment by the Commissioner) must respond to the default assessment using the NOPA process. The number of cases that involve a dispute about how the law applies to a particular tax question is therefore considerably less than 500.
18. Post the NOPA stage, approximately 75 percent of cases are resolved following the conference stage, and more through the later disputes stages, such that only 50 to 70 disputes a year proceed to the adjudication stage and become eligible for possible challenge to the TRA or High Court.
19. A reason for a low number of cases subject to the formal disputes process could be because a significant number of cases can be resolved using other processes (such as Inland Revenue explaining the application of tax law or policy to the taxpayer’s circumstances and/or the use of settlements). An underlying reason for this improved ability to resolve issues might be the risk-based audit approach adopted by Inland Revenue, meaning that Inland Revenue’s resources are likely to be applied to more serious cases of non-compliance where the taxpayer’s arguments are often weaker.

Response to the TWG’s recommendation

20. At this stage we do not consider that there is a burning need for an independent taxpayer advocate service as recommended by the TWG. This is because we do not understand the extent to which such a service would resolve the problem perceived by the TWG.

21. Further, as Inland Revenue continues its Business Transformation programme, the way in which it supports and provides advice to taxpayers will change. For example, Inland Revenue's Customer and Compliance Services business groups are now centred around different customer segments (eg micro-business, small-to-medium sized business, significant enterprises). Structuring in this manner will help Inland Revenue better understand the different needs of the different customer segments, and will help Inland Revenue provide better-tailored advice products which should result in less disagreement over substantive tax issues.
22. If Ministers see merit in considering a taxpayer advocate service further we would suggest that officials begin consulting with stakeholders in the New Year to get a better sense of the main problem with the current processes.
23. If Ministers want to pursue this approach, we would report to you early next year on a consultation plan. In this report we would give an undertaking of the size of the job and what policy projects would need to be stopped or slowed down.

Fiscal implications

24. Funding to establish a taxpayer advocate service has been sought as part of a broader budget bid from Inland Revenue. The amount sought is a placeholder at this stage due to the early stage of policy development and advice.

Consultation

25. Treasury was consulted in developing this note.

Next steps

26. We propose to discuss the contents of this note with you at the joint Ministers' meeting on 18 December 2018, and seek guidance as to whether officials should undertake further work in this area.

Recommended action

We recommend that you:

agree to discuss the contents of this note with officials at the joint Ministers' meeting on 18 December 2018.

Agreed/Not agreed

refer a copy of this note to the Minister of Finance.

Referred

Chris Gillion
Policy Manager
Inland Revenue

Hon Stuart Nash
Minister of Revenue
/ / 2018

Appendix: Specific forms of advice for small and unrepresented taxpayers

- a. **New to business** – Advisory seminars targeted at new businesses and new employers that explain new businesses’ tax obligations and introduce new businesses to online resources that Inland Revenue and other agencies provide.
- b. **Right from the Start** – Inland Revenue works to find early issues with filing or calculations and contacts small businesses to help resolve the issues as soon as possible so that they can meet their obligations going forward. This fits in with advice products (plain English guides and websites that explain Inland Revenue’s interpretation of tax laws).
- c. **Online tools** – Several online tools and returns are available that help small businesses meet their obligations. This includes calculators and downloadable resources.
- d. **Workshops** – That show taxpayers how to use Inland Revenue’s e-Services to file returns and make tax payments online, as well as where to find online resources that can be used to help make tax calculations.
- e. **Visits from Community Compliance** – Community Compliance will visit businesses and offer them the opportunity to ask questions or raise issues. The visits are primarily educational, although there is some compliance work carried out after the visit to ensure that the business filings reflect the operations of the business that have been observed (eg checking that PAYE returns are being provided if the business has employees).
- f. **Joint presentations with the Ministry of Business, Innovation and Employment** – Inland Revenue runs a stand at small business roadshows provided by the Ministry of Business, Innovation and Employment. These roadshows provide taxpayers with an ability to ask questions and be shown how to use Inland Revenue’s online tools.
- g. **1 on 1 advisory services** – These are available where customers are struggling with online self-help tools. Community Compliance will visit the small business and walk taxpayers through their obligations, the online tools, and show them how to calculate their liabilities and file returns online.
- h. **Planned and scripted compliance activities** – Community Compliance also run planned and scripted compliance activities that focus on small businesses, typically looking at specific areas of tax that Inland Revenue observes taxpayers struggling with, eg specific help with fringe benefit tax.