Tax Working Group Information Release

Release Document

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taxworkinggroup.govt.nz/key-documents

This paper has been prepared by a member of the Tax Working Group for consideration by the whole Tax Working Group.

The advice represents the preliminary views of the member who prepared the paper and does not necessarily represent the views of the whole Group or the Government.

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Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

[2] 9(2)(a) - to protect the privacy of natural persons, including deceased people.

Where information has been withheld, a numbered reference to the applicable section of the Official Information Act has been made, as listed above. For example, a [1] appearing where information has been withheld in a release document refers to section 9(2)(a).

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

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Collection Challenges

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[2]

Size of the (reported) problem

Table 1: Overdue tax debt

OVERDUE TAX DEBT AS AT 30 JUNE ($ MILLION)

Debt type	2013	2014	2015	2016	2017	Change since 2016 (%)
Working for Families Tax Credits	371.8	406.6	334.8	224.6	193.4	(13.9%) ↓
Goods and services tax (GST)	1,873.9	1,775.5	1,527.5	1,369.5	825.6	(39.7%) ↓
Income tax	2,365.7	2,519.6	2,653.0	2,562.4	1,556.1	(39.3%) ↓
KiwiSaver	22.5	33.3	29.4	24.9	26.5	6.4% ↑
Other tax	121.6	121.8	115.9	69.7	80.0	14.7% ↑
Pay-as-you-earn (PAYE)	586.8	613.9	492.4	428.9	309.7	(27.8%) ↓
Total	5,342.3	5,470.7	5,153.1	4,680.0	2,991.3	(36.1%) ↓

We manage both early and aged debt more effectively, particularly irrevocable debt, in line with our strategy to deal with what cannot be collected appropriately, this year we wrote off $1.8 billion of irrecoverable and aged debt.

Source: IRD Annual report 2017

Why should the TWG make recommendations about collections

Our terms of reference:

- A tax system that is efficient, fair, simple and collected.
  …
- An overall tax system that operates in a simple and coherent manner.

Why should the TWG make recommendations about collections

Politics: Getting everyone to pay assessed tax is supported by all New Zealanders.

Fairness: Firm action against those who seek to not pay assessed tax is consistent with everyone's sense of fairness, horizontal equity and it promotes voluntary compliance.

Revenue: There is a lot of revenue to be raised, without changing any fundamental tax policies.

Productivity: Many business don't pay tax because they don't make enough money. This is both misapplication of capital and unfair competition to tax compliant businesses.

Collections is going to get harder

"Compliance pressures and opportunities" in discussion paper *Preparing the Tax System for the Future* (meeting #4).

Comments by officials

This clearly is an important area with potential implications for the continuing effectiveness of revenue collection. Unlike some issues, it does not pose conceptual issues, but puts strain on current tax collection mechanisms. As such, reacting to it falls within the mandate of Business Transformation and the Commissioner of Inland Revenue more generally. The question is whether this is an area that the Group would wish to consider or whether it falls within the business as usual for the IRD.

Coherence in tax rates does not equal coherence in collections

Individuals:	Tax system is good at collecting PAYE. Beyond that, there is more scope for abuse.
Companies:	Easy to incorporate. There has been a prolific rise in the number of companies, most of which are closely held. Limited liability is supposedly conditional upon proper compliance with company law, but the tools to enforce against bad behaviour are difficult.
Trusts:	Use of trusts is widespread. Far removed from original purposes. Seen by many people as a way to "get away with" undesirable behaviour.

Leakages

- NZ's tax system taxes all these entities, but ability to collect against companies, trusts and hybrid company/trust structures rely upon non-tax legislation.
- Increase in (reported) debit current account balances is an example. Perfectly legal (probably), but a way to
  (a) avoid the last 5% or, (b) even worse, avoid paying the company the same, so company can use it to pay its assessed tax.
- Increase in debit current account balances is also explicable by the fact that the business just doesn't make enough money to pay a living wage to its shareholders/directors, and also pay taxes.

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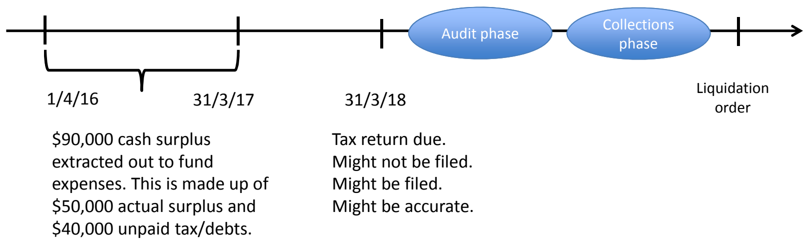
Leakages

Time:



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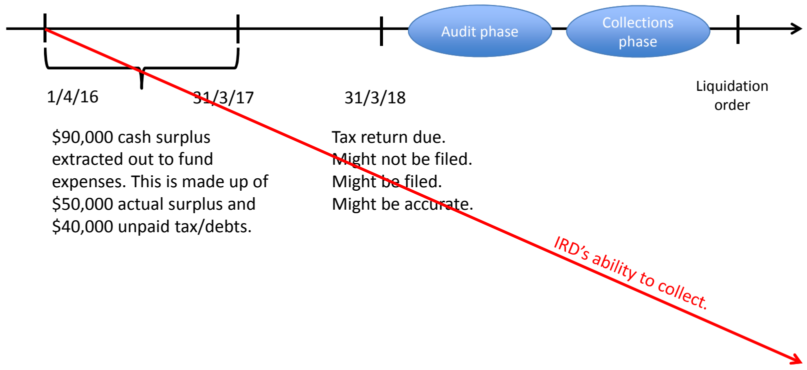
Leakages

Time:



Leakages

- Non-filing and inaccurate tax returns remain a significant problem.
- Complicated structures for small business (company, trust, corporate trustees, and so on). Harder to pin responsibility on individuals.
- Debtor-friendly liquidators remains a significant problem, even if IWG's recommendations are adopted.

> Unfortunately too many providers of insolvency services fall well short of the standards of integrity and skill that the New Zealand public is entitled to expect. There are self-interested practitioners who overcharge for their services or carry out unnecessary work in order to obtain larger fees. There are 'debtor-friendly' liquidators who fail to comply with their statutory duty to protect the interests of creditors (eg by turning a blind eye when directors have taken assets out of a company prior to liquidation at undervalue or even at no value at all). This problem is particularly evident in relation to small and medium-sized companies.

Source: IWG report 1

Leakages

- The Courts are starting to cut back compensation.

> Third, within the causation inquiry, we record that the IRD would be the largest beneficiary of a compensation order. It was NZNet's second largest creditor after Mr Johnston. The liquidators' undisputed evidence was that the company owed $173,303 to the IRD when Mr Johnston assumed office as a director. The IRD had taken no steps to recover this growing debt for over a year. Instead it was apparently content to continue sitting on its rights, allowing NZNet's indebtedness to escalate with accrued penalties to $386,322 over the next two years without enforcing the company's compliance with its statutory requirements to pay PAYE and GST.
>
> There is an irony in the liquidators' complaint that Mr Johnston should have moved earlier when the company's second largest creditor was guilty of the same inaction. The IRD's failure to act is unexplained and inexplicable; if it had acted much earlier its claimed loss would have been reduced accordingly. The IRD contributed significantly to its own losses.

Grant v Johnston [2016] NZCA 157 at [93] and [94].

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Ideas worth investigating

- Greater use of existing legal framework.
- Provide IRD special powers:
  - Director penalty notices (Australia).
  - Departure prohibition orders (Australia).
  - Withholding obligation of debit current account balances (in line with GST filing?).

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Ideas worth investigating

- Remove "intent to evade" element from GST offence, as is the case with PAYE.
- Increase criminal penalty for failing to file returns and/or make non-filing an infringement offence.
- Give CIR ability to look through to shareholders/directors for non-payment of PAYE and GST (Companies Act already has such provisions against insolvent/illegal removals of capital).

Ideas worth investigating

- Disallow trusts to be registered for tax, and/or enhance rules for personal liability for tax.
- Trust Fund Recovery Penalty (USA).
- USA law on piercing the corporate veil – it is a lot easier than in NZ.

WE LISTEN.
WE ACT.
WE GET RESULTS.

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