Tax Working Group
Te Awheawhe Tāke

Tax Working Group Public Submissions Information Release

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The Chair
Tax Working Group
By email to
submissions@taxworkinggroup.govt.nz

12 October 2018

Dear Sir

KPMG's comments on the Tax Working Group's Future of Tax Interim Report

We are pleased to provide feedback on the Tax Working Group's (the "Group's") Interim Report and commend the Group for the breadth of its analysis in the short time frame since its establishment.

In the interests of time, and for ease of the Group's reference, our feedback on the various issues and recommendations has been marked up directly to *Chapter 18 – Summary of Recommendations*.

We propose to provide separate, more detailed, comments on *Chapter 6 – Capital and Wealth* and *Appendix B – Design Features for extending the taxation of capital gains*.

We would be more than happy to elaborate on any of our feedback (please contact John on [1] or Darshana on [1]

Yours sincerely

[1]

John F Cantin
Partner

[1]

Darshana Elwela
Partner

Summary of TWG Recommendations

The Group has discussed many issues over the past six months. Yet there is also much to do before the presentation of the Final Report in February 2019.

Already, however, the Group has identified a range of opportunities to improve the fairness, balance, and structure of the tax system.

This chapter summarises the decisions and recommendations emerging from the Group's work to date. It also notes area where further analysis is contemplated.

The Group's views on these issues are by no means final, and feedback is welcome. Together, we can shape the future of tax.

Capital & Wealth

6.1 The Group is still forming its views on the best approach towards extending the taxation of capital income. Only once such an extension is designed can a meaningful comparison take place between different options and the status quo. Appendix B sets out the Group's initial thinking on further design features of broad-based taxation of capital income. The Group will work toward its ultimate recommendations in the Final Report.

KPMG Comment: We propose to provide separate detailed comments on this Chapter and Appendix B of the Interim Report.

Retirement Savings

The Group recommends that the Government:

7.1 Remove ESCT on the employer's matching contribution of 3% of salary to KiwiSaver for members earning up to $48,000 per year.

7.2 Reduce the lower PIE rates for KiwiSaver funds by five percentage points each.

7.3 Consider ways to simplify the determination of the PIE rates (which would apply to KiwiSaver).

The Group will give further consideration to the taxation of savings in the Final Report, in light of its broader conclusions on the tax system.

KPMG Comment: In principle, we are supportive of the Group's recommendations. However, we consider that any changes need to have regard to the total package of recommendations.

In particular, we note that decisions here will impact on some of the design considerations under Chapter 6 as they relate to extending taxation of capital income to PIEs.

Also, we note that not all KiwiSaver Funds can apply different PIRs (for example, the 28% rate is applied by defined benefit PIEs) and that some Retirement Schemes are not PIEs. The Group should consider how the benefits of the proposed tax changes for lower income savers applies in these situations.

Housing Affordability

8.1 The Group's work on housing affordability is closely linked with its work on the taxation of capital income. The Group will have particular regard to housing market impacts as it finalises its recommendations regarding capital income.

KPMG Comment: This will be covered in more detail in our proposed detailed analysis of Chapter 6 and Appendix B. In principle, we agree with the Group's interim conclusion that the tax system is unlikely to be the dominant driver of house prices (and correspondingly tax reform is unlikely to have a material impact on the housing market).

Environmental & Ecological Outcomes

9.1 There is significant scope for the tax instruments to play a greater role in delivering positive environmental and ecological outcomes in New Zealand. Environmental tax instruments can be a powerful tool for ensuring people and companies better understand and account for the impact of their actions on the ecosystems on which they depend.

9.2 Taxes are not well suited to all environmental problems and regulation will still be a better approach for dealing with some issues. The Group has prepared a draft framework identifies a range of criteria and design principles for environmental taxes to be effective. Environmental taxation and regulation should be considered together for positive outcomes.

9.3 In the short term, there may be benefits in expanding the coverage of the Waste Disposal Levy, and for reassessing waste and landfill disposal externalities to see if higher rates are warranted. There could also be benefits from strengthening the ETS and advancing congestion charging. Over the

medium term, there could be benefits from greater use of tax instruments to address challenges in both water pollution and water abstraction. Addressing Māori rights and interests in fresh water should be central to any changes. In the longer term, new tools could allow for an expanded role for environmental taxes to address other challenges such as biodiversity loss and impacts on ecosystem services.

KPMG Comment: We agree with the broad direction of the recommendations made. We do plan to consider the draft framework further however.

Corrective Taxes

The Group:

10.1 Recommends that the Government review the rate structure of alcohol excise with the intention of rationalising and simplifying it.

10.2 Recommends that the Government prioritise other measures to help people stop smoking before considering further large increases in the tobacco excise rate.

10.3 Recommends that the Government develop a clearer articulation of its goals with regard to sugar consumption and gambling activity.

KPMG Comment: We agree with the recommendations as far as they relate to the efficacy of the tax system in driving behavioural responses (and potentially resulting in adverse outcomes for lower income households). We agree that non-tax alternatives (including regulatory responses) should be considered alongside tax policy.

International Income Tax

The Group:

11.1 Supports New Zealand's continued participation in OECD discussions on the future of the international tax framework.

11.2 Recommends that the Government be ready to implement an equalisation tax if a critical mass of other countries (including Australia) move in that direction.

11.3 Recommends that the Government ensure, to the extent possible, that our double tax agreements and trade agreements do not restrict our taxation options in these matters.

KPMG Comment: Consistent with our submission on the background paper, we consider this particular area to be a difficult one. We understand the view that a new international consensus needs to be developed. However, this will not be a straight-forward process due to competing national interests and domestic political pressures.

We reiterate our comments that attribution of profit based on user value may not particularly advance New Zealand's ability to tax cross-border transactions. We further note our comments that accepting a "user value" based rationale to tax for digital services makes it, on a principled basis, difficult to resist applying that concept to taxing goods. Anecdotally, other countries have already started to adopt this approach which means that New Zealand's export sector is at risk of foreign income taxation. New Zealand should consider carefully its support for "user value" based income tax approaches.

We also note that both an equalization tax and user value based taxes do not appear to take into account that losses may have been made and could continue to be made by multinational groups.

We note the Group's intention that New Zealand DTAs and trade agreements not restrict New Zealand taxation (should that be the right answer). However, in the current environment such agreement may not be readily obtained in practice.

We also note that the recommendation in 11.1 is supported by a conclusion that a foreign multinational operating in the digital economy has a potential competitive advantage due to its favourable New Zealand taxation profile. This appears to us to contradict the conclusions in the charities chapter (Chapter 16) which supports the view that a business will simply maximise its return. (I.e. the charitable tax concession does not result in charities' trading operations undercutting non-charities business rivals - see paragraph 13 of that Chapter). We have not considered the detailed analysis in supporting papers prepared for the Group but, in principle, using the same analysis, the competitive advantage may not in fact be due to any "tax concession" allowed under current rules. The reason for change must be found in other arguments.

GST

The Group:

12.1 Recognises the significant public concern regarding GST, but does not recommend a

reduction in the rate of GST. This is because lowering the GST rate would not be as effective at targeting low- and middle-income families as either:

— Welfare transfers (for low income households); or

— Personal income tax changes (for low and middle income earners).

12.2 Does not recommend the removal of GST from certain products, such as food and drink, on the basis that the GST exceptions are complex, poorly targeted for achieving distributional goals, and generate large compliance costs.

KPMG Comment: Consistent with our earlier submission on the submissions background paper, we agree with both of these recommendations.

12.3 Believes there is a strong in-principle case to apply GST to financial services, but there are significant impediments to a workable system. The Government should monitor international developments in this area.

12.4 Does not recommend the application of GST to explicit fees charged for financial services.

KPMG Comment: We note that both of these recommendations, while supported, continue to mean that boundary issues will arise so that the "in source" and other biases remain. We consider that these problems should be included on the Tax Policy Work Programme albeit "as a watching brief and as time allows".

12.5 Recognises that there is active international debate on financial transaction taxes, which should be monitored, but does not recommend the introduction of a financial transactions tax at this point.

KPMG Comment: We agree particularly as substitution is likely to mean that such taxes are ineffective.

The Group has already reported to Ministers on the issue of GST on low-value imported goods, and the Government is advancing that work.

Personal Income & The Future of Work

The Group:

13.1 Will provide recommendations regarding the rates and thresholds of income tax in the Final Report in February 2019.

KPMG Comment: We note that the Group's work and recommendations will interact with the work of the Welfare Expert Advisory Group as any reductions in tax rates and/or increasing tax thresholds will impact effective marginal tax rates for those in the transfers systems.

13.2 Supports Inland Revenue's efforts to increase the compliance of the self-employed, particularly an expansion of the use of withholding tax as far as practicable, including to platform providers such as ride sharing companies.

KPMG Comment: Our preference (see 15.3) is for increased third party reporting of income as the effect of expenses is likely to make it difficult to set "one size fits all" withholding tax rates. More flexible withholding rate setting rules will add to compliance costs.

13.3 Supports the facilitation of technology platforms to assist the self-employed meet their tax obligations through the use of smart accounts or other technology based solutions.

13.4 Recommends that Inland Revenue continues to use data analytics and matching information to specific taxpayers to identify underreporting of income.

KPMG Comment: we support the enhanced use of technology to improve the "customer" interface for taxpayers. However, it should be noted that not all taxpayers will have access to, or be comfortable using, technology to communicate and interact with Inland Revenue. While this may be a minority of the population (and the proportion can be expected to shrink over time), efforts should be made to ensure that these individuals are able to fully participate in and comply with the "future" tax system.

13.5 Recommends that there be a review of the current GST requirements for contractors who are akin to employees.

KPMG Comment: We understand this recommendation to be focused on contractors who have little if any GST input tax so that there is simply an input tax claim by the payer matched by an output

tax return by the contractor. This recommendation does not account for contractors who may move in and out of such situations. This recommendation also needs to have regard to the outcome of the next recommendation.

13.6 Recommends that the Government seek to align the definition of employee and dependent contractor for tax and employment purposes.

KPMG Comment: It is not clear what the intended effect of this recommendation is. Is it to provide a third category – a "dependent contractor" – compared to the existing employee and contractor status? If so, what is the tax outcome sought for this category? If it is to deem a dependent contractor to be an employee, is it appropriate or fair that such persons would not be entitled to deduct their business costs? Further detail on this is required.

13.7 Recommends additional Government support for childcare costs, but believes this support is best provided outside the tax system.

KPMG Comment: We agree with the recommendation that any support for childcare costs should be outside the tax system.

The Taxation of Business

The Group recommends that the Government:

14.1 Retain the imputation system.

KPMG Comment: We agree with this recommendation.

14.2 Not reduce the company tax rate at the present time.

KPMG Comment: We understand the rationale for this recommendation. However, we note that it is difficult for arguments in favour of, or against, reducing the company tax rate to be conclusively proven.

It is not clear whether the real world effects of the last two company tax rate reductions – such as the observed lack of additional foreign direct investment in NZ – is attributable to the reductions not having an incentive effect, or other factors. For example, many other countries have reduced their business tax rates while implementing the OECD BEPS measures. New Zealand's approach has been to widen the tax base at the same time it has reduced tax rates (and more recently to maintain the company rate while widening the base through BEPS responses). The effective tax rate may not have been comparatively reduced.

14.3 Not introduce a progressive company tax.

KPMG Comment: We agree. However, taxation at the shareholder's rate is theoretically ideal. Further, extending capital income taxation may change the desirability of separate company taxation (as there will be greater opportunity for double tax to arise). We recommend that relaxing the entry criteria and compliance for look-through-companies be considered to allow a choice of partnership or company taxation.

14.4 Not introduce an alternative basis of taxation for smaller businesses, such as cashflow or turnover taxes.

KPMG Comment: Consideration could be given to allowing the Accounting Income Method (AIM) returns and payments to be a final return. This would mean that errors would be corrected in subsequent AIM returns rather than in a wash up end of year income tax return.

14.5 Consider other measures to reduce compliance costs. Depending on the fiscal position, these measures could include:

- Increasing the $2,500 threshold for paying provisional tax to $5,000-$10,000.
- Increasing the $10,000 year-end closing stock adjustment to $20,000-$30,000.
- Increasing the $10,000 limit for the automatic deduction for legal fees, and potentially expanding the automatic deduction to other types of expenditure.

KPMG Comment: Adjustments to these thresholds appear reasonable to reduce compliance costs. Other areas the Group may wish to consider is, for example, increasing the FBT exemption threshold for unclassified fringe benefits, which is currently $300 per employee per quarter (up to $1,200 per annum) and $22,500 across all employees annually.

14.6 Not change the thresholds around fixed assets.

14.7 Retain the 17.5% rate for Māori authorities.

14.8 Extend the 17.5% rate to the subsidiaries of Māori authorities.

14.9 Consider technical refinements to the Māori authority rules, as suggested by submitters, in the Tax Policy Work Programme.

KPMG Comment: The recommendation to extend the 17.5% tax rate to subsidiaries of Māori authorities is consistent with our submission on the background paper and welcome.

The Integrity of the Tax System

The Group recommends:

15.1 A review of loss-trading, potentially in tandem with a review of the loss continuity rules for companies.

KPMG Comment: These recommendations appear to be focused particularly on trusts. We consider that further work is required and that this should be undertaken through the Tax Policy Work Programme. (The Group's timetable and processes do not allow sufficient time to consider the problem, if any, and to determine an appropriate solution.)

For companies, a "reasonable to conclude a change in shareholding is not to trade tax losses" test or threshold should be considered for loss continuity purposes. We note that it is common for overseas mergers and acquisitions to occur without any thought as to availability of New Zealand tax losses. (Often, New Zealand is only a minor part of a global transaction.) Although the same shareholders would not benefit from the tax losses, the target of the rules, inappropriate loss trading is not occurring. The result is a potential "windfall" to the Government, from forfeiture of tax losses. To ensure such as test can be practically applied by taxpayers, it is important that the circumstances for application of the rule should be clear. For example, it should not require a section BG 1 type analysis to be undertaken for the rule to be applied (or not applied, as the case may be).

We also do not favour a "same business" test as the Australian experience suggests that this is narrowly construed by their tax authorities, giving little real benefit as an alternative. That does not fit with the need for New Zealand businesses to be agile.

15.2 That Inland Revenue have the ability to require a shareholder to provide security to Inland Revenue if: (i) the company owes a debt to Inland Revenue; (ii) the company is owed a debt by the shareholder; and (iii) there is doubt as to the ability/and or the intention of the shareholder to repay the debt.

KPMG Comment: The last of these three requirements is likely to be difficult to legislate and will be subjective in its application by Inland Revenue. It will lead to disputes.

We are not convinced of the need for specific measures outside the current requirements, which we agree could be better enforced. That suggests that Inland Revenue should be using the information it collects, or can access, for targeting enforcement action. Currently liquidators and receivers are able to recover overdrawn shareholder current accounts for repayment to all creditors, subject to existing priorities and securities. This is an appropriate mechanism to manage overdrawn shareholder current accounts. Further powers to the Commissioner are not required, in our view.

Allowing Inland Revenue to take a secured position against the shareholder potentially deprives the company of money and allows the Commissioner to indirectly take a preference over and above existing statutory preferences available to Inland Revenue.

We further note that a shareholder unable to repay a current account is at risk of the financial arrangement rules deeming taxable income to arise. If Inland Revenue takes enforcement action against the company, so that it is liquidated, it will have the ability to seek redress from the shareholder as the result of the remission of the debt giving rise to taxable income (if it is not repaid).

15.3 Further action in relation to the hidden economy, including:

- An increase in the reporting of labour income (subject to not unreasonably increasing compliance costs on business).
- A review of the measures recently adopted by Australia in relation to the hidden economy, with a view to applying them in New Zealand.
- The removal of tax deductibility if a taxpayer has not followed labour income withholding or reporting rules.

KPMG Comment: See our comment under 13.2. We agree with these recommendations.

15.4 That Inland Revenue continue to invest in the technical and investigatory skills of its staff.

15.5 Further measures to improve collection and encourage compliance, including:

- Making directors personally liable for arrears on employee GST and PAYE obligations (as long as there is an appropriate warning system).

KPMG Comment: In the circumstances at issue, it is not clear why the directors of such companies are

not currently liable for trading when insolvent and why they would not be prohibited from running companies for a period of time as a result. There already appears to be available enforcement options to achieve the desired policy objectives.

Inland Revenue has sufficient tools at their disposal to monitor and enforce compliance, including liquidating companies that are indebted. Therefore, we doubt the need for additional or specific rules.

We understand the rationale for the Group's recommendations in respect of employee tax deductions and GST given these amounts are effectively held "on trust" by business. And with the move to "pay day" reporting from 1 April 2019, where a business's PAYE liabilities will need to be calculated and reported to Inland Revenue within 2 working days of the payroll run, there appears to be a stronger argument as businesses should be aware of their tax obligations earlier and therefore the requisite cash flow to meet those obligations.

- — Departure prohibition orders
- — An alignment of the standard of proof for PAYE and GST offences.

15.6 The establishment of a single centralised Crown debt collection agency to achieve economies of scale and more equitable outcomes across all Crown debtors.

KPMG Comment: This recommendation in 15.6 appears sensible but it would appear to require consistent interest and penalties regimes (so that the relevant agency is indifferent to which debt is treated as collected or written-off).

We also consider that thought should be given to the incentives that this may, or may not, create for a relevant agency to either hold or transfer a debt. (For example, would a write-off of tax debt be measured against the debt collection agency's targets or Inland Revenue's collection KPIs?)

While such a system sounds sensible, administering debt within a single database that covers "whole of Government" debt will create challenges and may require significant capital investment and restructuring of current systems, processes and institutional structures to deliver. A cost benefit analysis should be undertaken to properly consider the merits of such an agency.

Charities

The Group:

16.1 Believes the Government should periodically review the charitable sector's use of what would otherwise be tax revenue, to verify that intended social outcomes are being achieved.

16.2 Supports the Government's inclusion of a review of the tax treatment of the charitable sector on its tax policy work programme, as announced in May 2018.

16.3 Notes the income tax exemption for charitable entities' trading operations was perceived by some submitters to provide an unfair advantage over commercial entities' trading operations.

KPMG Comment: See our earlier comment at 11.3 regarding the different conclusion reached at paragraph 22 in this Chapter. As both types of entities can be reasonably expected to have similar objectives with regard to their business activities, it is not clear why a charity would not use its tax concession as a competitive advantage but a multi-national group could. (I.e. if they are both profit maximising businesses, they should each seek the greatest return the market will allow.)

16.4 Notes, however, the underlying issue is the extent to which charitable entities are accumulating surpluses rather than distributing or applying those surpluses for the benefit of their charitable activities.

16.5 Recommends the Government consider whether to apply a distinction between privately-controlled foundations and other charitable organisations.

16.6 Recommends the Government consider whether to amend the deregistration tax rules to more effectively keep assets in the sector, or to ensure there is no deferral benefit through the application of these rules.

16.7 Recommends the Government review whether it is appropriate to treat some not-for-profit organisations as if they were final consumers, or, alternatively, to limit GST concessions to a smaller group of non-profit bodies such as registered charities.

KPMG Comment: The support for recommendation 16.7 (at paragraph 28) contradicts the "no competitive advantage" statements at paragraph 22.

It is not obvious why the statement at paragraph 22 should be true for income tax but not true for GST.

We further note that this conclusion assumes that not-for-profits' non-taxable activities subsidise their business activities. (This is because a not-for-profit is entitled to additional GST input tax for its non-taxable activities. Its input tax for its business activities should be the same as for its competitors.) This is the reverse of what would be expected – that the not-for-profit would use its business activities to subsidise its non-GST taxable activities.

16.8 Recommends the Government consider whether the issues identified in Chapter 16 have been fully addressed or whether further action is required, following the conclusion of the review of the Charities Act 2005.

The Administration of the Tax System

The Group:

17.1 Strongly encourages the Government to release more statistical and aggregated information about the tax system (so long as it does not reveal data about specific individuals or corporates that is not otherwise publicly available).The Government could consider further measures to increase transparency as public attitudes change over time.

17.2 Encourages Inland Revenue to publish or make available a broader range of statistics, in consultation with potential users, either directly or (preferably) through Statistics New Zealand.

KPMG Comment: We agree with these recommendations. In KPMG's submission on the Neutralising Base Erosion and Profit Shifting (BEPS) Act and the multi-lateral instrument to amend Double Tax Agreements for BEPS related changes, the lack of information and research on the potential size of the BEPS problem in NZ (and therefore whether the legislative response was appropriate) was highlighted. Our submission to have this issue researched properly was not taken up by Officials or the Select Committee. If more tax information was released by Inland Revenue, external researchers may be able to provide more and better analysis of the tax system and potential gaps.

17.3 Encourages Inland Revenue to collect information on income and expenditure associated with environmental outcomes that are part of the tax calculation.

17.4 Recommends that any further expansion of the resources available to the Ombudsman include consideration of provision for additional tax expertise within the Office, and possibly support to manage any increase in the volume of complaints relating to the new Crown debt collection agency proposed by the Group.

17.5 Recommends the establishment of a taxpayer advocate service to assist with the resolution of tax disputes.

KPMG Comment: We agree with recommendation 17.5 but note that consideration should be given to a broader taxpayer advocate role, rather than simply relating to resolution of disputes. The role should also encompass improving the operation of tax administration in New Zealand through recommendations to Inland Revenue and Government.

17.6 Recommends the use of the following principles in public engagement on tax policy:

- Good faith engagement by all participants.
- Engagement with a wider range of stakeholders, particularly including greater engagement with Māori (guided by the Government's emerging engagement model for Crown/Māori Relations).
- Earlier and more frequent engagement.
- The use of a greater variety of engagement methods.
- Greater transparency and accountability on the part of the Government.

KPMG Comment: We agree with the above recommendations. However, we note that good tax policy is subject to political considerations and non-tax objectives. The Government's proposed rental loss ring fencing rules, announced before the 2017 General Election, is a case in point. The consultative document on the detailed design of these rules reflects the difficulty of trying to fit this policy within the established tax policy framework. (We refer to the confusing reference to "speculators", in the document, as the target of loss ring-fencing, when we would expect such investors to already be taxable on their gains, so loss ring-fencing is not required).

While Government, rightly, is able to set tax policy priorities as it sees fit in our constitutional democracy, this may not always align with principles

of good tax policy, if other considerations take precedence. This will always be a factor.

We understand the need to broaden public engagement on tax, but engagement depends on interest, expertise, time and importantly the availability of funding. Often those most affected will not have the expertise, time or funding to engage or engage effectively. The Group should consider solutions to the funding question, in particular, to enable broader participation.

A particular problem with lack of expertise is that the engagement will not be well targeted so that the problem and solutions may be mis-identified so that the engagement may not be efficient. An example may be the recent Oxfam press release on New Zealand tax (not) paid by multinational pharmaceutical companies and the need for Inland Revenue to respond to provide contextual information on these entities' positions.

This problem is compounded by a general lack of knowledge of our tax system and its principles. This has arguably been exacerbated by the current "non-filing" model for individuals, a number of whom have no regular interaction with the tax system (and have not had for a number of years). We note this is proposed to change for some, but not all, with the legislative proposals in the Modernising Tax Administration Tax Bill currently before Parliament. Education will be key to those proposals.

Consideration should also be given to whether recommendations can be made on the role of Government in educating New Zealanders on New Zealand's tax system and the basics of how and who pays tax.

17.7 Notes the need for the Treasury to play a strong role in tax policy development, and the importance of Inland Revenue maintaining deep technical expertise and strategic policy capability.

17.8 Encourages the continuing use of purpose clauses where appropriate and recommends the inclusion of an overriding purpose clause in the Tax Administration Act 1994 to specify Parliament's purpose in levying taxation.

KPMG Comment: We consider there are two broad issues missing from these recommendations. To the extent they do not feature in our previous submission, they arise from considering the Interim Report.

Interpretative certainty

The first is the separation of the tax policy development function (undertaken by Inland Revenue's Policy and Strategy) from the practical application of the law (undertaken by Inland Revenue's Customer Services and the Office of the Chief Tax Counsel).

The tax policy function seeks to develop legislation that meets the policy intent. It provides Commentaries to relevant Tax Bills and follow-up Special Reports and Tax Information Bulletin (TIB) items which describe the legislation and how it is intended to work. Taxpayers can take no comfort from such descriptions.

This is because the role of determining what the legislation actually says and does is with the Customer Services function and, ultimately, the Office of the Chief Tax Counsel. These operational functions can and do take different views of what the legislation actually achieves.

This means that legislative outcomes inconsistent with the tax policy can and do arise. This problem can be compounded because the policy intent is not clearly recorded and described. Although this is largely a historical problem as the Generic Tax Policy Process (GTPP) provides a better trail of the policy development, it remains an issue, particularly if the GTPP is not fully observed.

We recommend that consideration be given to requiring the Commissioner to follow the published policy statements (i.e. TIBs and Special Reports on new legislation) so that her focus is on identifying errors in the legislation and fixing those through GTPP rather than through interpretation. Taxpayers should be free to follow the law as enacted, consistent with the policy intention as described.

The role of the Courts

Ultimately, the Courts play a significant role in the administration of the tax system. The Courts decide the interpretation of tax rules for particular taxpayers and the Commissioner.

In our view, the Courts do not appear well placed to decide tax policy and in fact do not take tax policy into account when making their decisions. There is also a degree of tension between the tax disputes rules and what the Courts appear to consider their role to be. This creates uncertainty regarding taxpayers' and the Commissioner's rights and obligations.

Some examples illustrate.

The courts have been reluctant to apply the evidence exclusion rule in section 138G of the Tax Administration Act. (*Concepts 124* appears to be an example). This appears to be a manifestation of the tension between the tax dispute rules objective of having "all the cards on the table" and the High Court rules seeking to resolve the disputes in the interests of justice. This appears to mean that taxpayers can be "ambushed by the Court" as opposed to "ambushed at Court", which these rules were intended to prevent.

In the *Westpac* case, albeit probably obiter, the Court denied a claim by Westpac on the basis that the evidence it was relying on had not been provided to the Commissioner. The Court concluded it was only able to make a determination based on what the Commissioner had access to (at the time the assessment was made). This was an application of section 138P of the TAA. This contradicts the (later) *Concepts 124* decision. Further, the substantive issue in that case considered detailed evidence which was not all available to the Commissioner at the time of assessment. It is not clear why, even in the context of a single (albeit lengthy) judgement, these different positions can be taken. (Note that this judgement also brings into question the ability and need to have discovery in tax litigation. If the Courts can only decide based on the evidence before the Commissioner, subsequently discovered documents are irrelevant.)

In *Ben Nevis,* the taxpayer sought to raise an alternative argument to the main argument it had taken through the disputes process. The Supreme Court declined to consider this argument in any detail. (We understand the Commissioner did address the taxpayer's alternative argument in detail – it was the Court that decided it was unnecessary to consider that argument.) It issued a very short judgement on the point which, with respect, was not a model of clarity. The result of this has been numerous disputes with the taxpayer seeking to advance the alternative argument. This would not have been feasible, in our view, if the Supreme Court has accepted the taxpayer's ability to raise the argument and dealt with it fully at the time.

In the first two cases, the Commissioner has not been motivated to clarify the position from either a tax policy or practical application of the law perspective. We consider that is not an appropriate position.

We believe the Group therefore needs to also consider the role of the Courts and make recommendations clarifying taxpayer rights and obligations in this part of the disputes process.