

## PART THREE

# Improving compliance



- 86% customer satisfaction
- 97% satisfaction with advisory services
- \$787 million assessed audit discrepancies
- \$120 million increase in debt under instalment



# Our compliance model

Our compliance model helps us to meet our desired future by understanding the factors that influence taxpayer decisions and behaviour, and their impact on compliance attitudes and the response required.

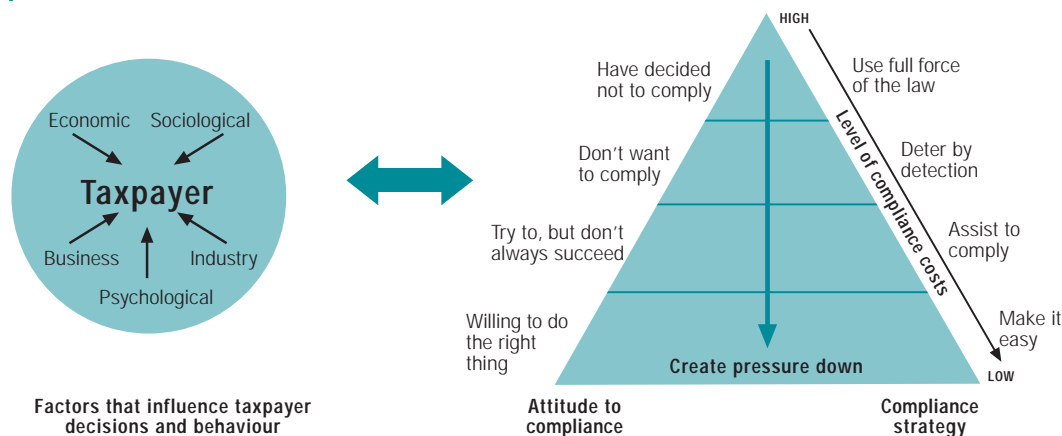
The model promotes a more tailored, responsive approach to taxpayers and recognises the external factors that influence taxpayer compliance attitudes and behaviours. The model is a reflection of compliance generally and therefore can apply equally to the payment of child support and student loan repayments.

One of the concepts behind the compliance model is the tax system and administration being designed to facilitate compliance among the majority of taxpayers who do, or who aim to, comply with the law. But at the same time the design must ensure that appropriate sanctions apply for deliberate non-compliance.

The thinking behind our compliance model is aiding us to deliver services in a way that strengthens community confidence in Inland Revenue. It is helping us to think about how to make it easier to contact us, to tailor our services and address non-compliance.

The following sections show how we apply the compliance model thinking to our activities in 2003–04.

**Figure 10 – Our compliance model**



# Making it easy to comply

Most taxpayers and social assistance customers' attitude to compliance is that they are willing to do the right thing. By Inland Revenue making it easy for taxpayers to meet their obligations and receive their entitlements we are more likely to achieve higher levels of compliance. Creating an environment conducive to compliance also builds the community's confidence in Inland Revenue.

Nearly everyone in the community is an Inland Revenue customer, for various reasons: they operate businesses, earn salary and wages, make student loan repayments, or are entitled to family assistance or child support. Therefore we already have a large customer base, but it is also growing fast.

**Figure 11 –  
Our customer base**

Tax type	Customers as at 30 June 2004	Increase over the past 4 years
Income tax	5,769,480	13%
GST	591,037	12%
PAYE	185,951	9%
Child support	285,738	8%
Student loans	465,642	41%

To meet our customers' expectations we need to understand their needs and the nature of the changes to our customer base. For example, there is a high rate of turnover in the GST taxpayer base, with over 72,000 taxpayers registering for GST and over 36,000 deregistering in the past year. New customers and customers changing their circumstances can require a greater level of contact and resources than customers whose circumstances are stable.

Some of this turnover is caused by:

- business life-cycles—for example, businesses may start or end, change their tax status, or change their employment status
- economic growth
- migration

- expected growth and turnover, for example in the student loan scheme where borrowers either start or finish repaying their loans.

To manage our taxpayers and other customers we need to be able to:

- respond to current demand, while planning for projected future demand
- provide more online and self-help services to customers
- continue to improve our processes to make compliance easier for our customers.

To respond to current demand, in addition to the services offered on our websites in 2003–04, we handled:

- 4.888<sup>11</sup> million phone contacts, plus 1.878 million calls to INFOexpress, our automated phone service
- 1.647 million correspondence contacts, including 177,293 electronic contacts
- 176,623 personal appointments at our offices on tax, family assistance and student loan matters
- 933,316 child support contacts.

To make it easier for people to request information we successfully introduced natural language speech recognition technology into our INFOexpress self-service phone line. This lets callers request information with their voice, rather than having to use the touch tone keypad on their telephone. Since the service started in late February 2004, there has been a substantial increase in the number of successfully completed requests for stationery, compared to the previous touch tone service.

<sup>11</sup> This figure is not directly comparable with last year's figure as we have established that the reporting of our customer contact telephone volumes in the Information Services Output Class has been over-reported previously by approximately 3.6% due to the way a programme has interpreted information from another database.



*Bernadette (Bernie) Miller*

**TUANZ Call Centre Team Leader of the Year**  
Bernadette (Bernie) Miller, Team Leader at Christchurch Call Centre, was awarded the Team Leader of the Year award at the TUANZ (Telecommunications Users' Association of New Zealand) Contact Centre Awards in June 2004.

Maire Murray, Team Leader from the Wellington Call Centre was also a finalist.

The TUANZ awards recognise excellence and exceptional achievement within New Zealand contact centres. They are the industry's opportunity to acknowledge individuals and contact centres who have made a significant contribution to their organisations and in doing so, have added to the professionalism of New Zealand contact centres.

"Bernie's award highlights the capability and professionalism of staff within Inland Revenue's call centres", says Geoffrey Frost, National Manager Call Management.

"We had two team leaders nominated for this award—the only organisation to have more than one staff member nominated for this award category. This reflects the high capability of people within our call centres."

"I was thrilled to be nominated and really proud to take the award. It's great to represent an organisation that is first-rate in its call centre technology and customer service," says Bernie.

"I really appreciate Inland Revenue's commitment to leadership development and providing opportunities to staff who want to expand on their existing skills."



**Wellington  
Customer Service  
Representative  
Dion Scott**

### Consistently satisfied customers

The majority of our customers receive service through our five call centres, and their efficient and effective operation is vital for ensuring customer satisfaction remains high.

Our Customer Service Representatives (CSRs) are on the front line of service delivery. The efficiency and professionalism of our CSRs is often what our customers remember about their experiences with Inland Revenue.

CSR Dion Scott says working in the call centres is always challenging.

“Helping taxpayers work through any problems they may have and reaching a solution is a great feeling, and giving them information to help their compliance is really rewarding.

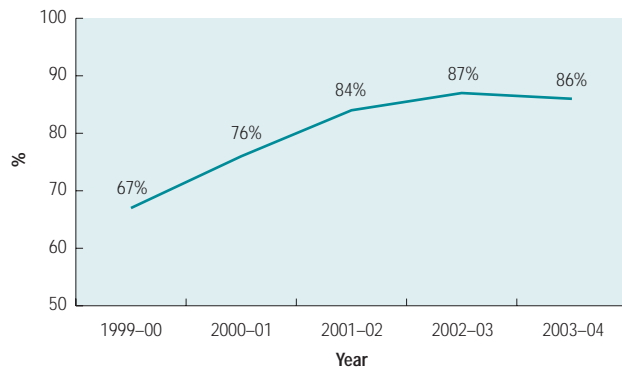
“Getting positive feedback from happy customers is fantastic and it makes dealing with the challenges of the role worthwhile.”

Feedback from the year included numerous examples such as: “Every time I ring the tax department I find it a pleasure to deal with you because you are so helpful. People always complain and run you down, but I have always found it a pleasure.”

### Quality of our service

We regularly survey our large and dynamic customer base to measure how well we are delivering our services. Our customer satisfaction level was 86% for the year ending June 2004. The results from our call centres were higher again, with 87% overall satisfaction, and 96% of tax agents satisfied with their call centre service. An additional measure of the quality of our service is that 90.5% of surveyed customers had their enquiry answered in one call to an Inland Revenue call centre.

**Figure 12 –  
Customer satisfaction<sup>12</sup>**



Child Support services are provided by a specific group within Inland Revenue. It is more challenging to achieve high customer satisfaction ratings with these customers because we are dealing with very emotional issues, often when people are under pressure as a result of a relationship breakdown. This year, 68% of our Child Support customers have been satisfied or very satisfied with the service received, a 2% increase on 2002-03.

<sup>12</sup> Margin of error ± 2%

## Complete, correct, clear and timely responses

We measure the quality of our services by looking at the correctness, clarity, completeness and timeliness of a sample of our responses.

This year, our target was to improve our Child Support results by 5% on last year (from 76.1% to 80%). Our performance increased by 15%, with 87.6% of responses meeting our standards. This increase built on the improvement measures put in place in 2002–03, where we placed emphasis on improving technical advice and resources.

Our target for our tax, family assistance and student loan responses was to improve by 1% on last year's result of 82%. However, our results declined, with 77.5% of responses meeting all of the correctness, clarity, completeness and timeliness standards. The correctness and clarity of our responses to our customers remained at a similar level to last year, but there was a decline in the completeness of our written responses. This does not necessarily mean that customers received an incorrect or incomplete response as our standards refer to not just the answer to the customer, but also to the completeness of our record keeping. During the year we undertook training to raise performance. The training has resulted in 85% of surveyed work meeting the completeness standard at the end of the year.

### Timeliness of our service

Most of our customers contact us through our call centres. Last year we received 4.888<sup>11</sup> million person-to-person telephone contacts and, on average (including our busy periods), answered calls within 2 minutes 44 seconds. Most callers were answered significantly faster than average:

- 52.6% of tax agents calls, 76.7% of employer calls, 59.6% of return and debt collection calls were answered within 20 seconds
- 43.4% of other calls were answered within 60 seconds on non-peak days

- 74.2% of child support calls were answered within 30 seconds on non-peak days.

Our speed to answer child support calls<sup>13</sup> was similar to last year, but with other calls our performance was below 2002–03 and below this year's target. This was primarily caused by call volumes being 21% above forecast on our tax agents', and general lines. A contributing factor was also that, in some cases, information was not sent to customers on the days expected.

During the year we increased our capacity to handle calls by expanding our call centres and by people from our Field Delivery work area assisting during the peak calling period.

The February 2004 floods impacted on our call centres in two ways. We supplied a number of staff to assist the Ministry of Social Development in their contact centres and provided relief in an unprecedented community emergency situation. At the same time, staff numbers were down approximately 30%, as individual circumstances prevented some staff from being at work. Our remaining call centre staff pulled together to ensure the number of calls answered was greater than predicted.

Although our general correspondence volumes also increased by 9%, we maintained similar levels of performance to last year with:

- 83.0% of child support correspondence answered within two weeks
- 88.8% of general correspondence answered within three weeks
- 97.4% of general and 98.2% of child support correspondence answered within six weeks.

<sup>13</sup> Our child support calls are answered outside of our five main call centres by dedicated Child Support staff.

## Strengthening identity requirements for IRD numbers

Although we need to make it easy to comply, we also need to ensure we minimise risk to the revenue base. In July 2004 we strengthened our standards for issuing an IRD number, by setting higher requirements for the proof of identity documents people need to show us to receive an IRD number. This change was made to reduce the risk of IRD numbers being misused.

We are considering further strengthening our ability to test the identity of people. This work is being carried out in line with the “good practice” in the *Evidence of Identity Framework* proposals drafted by the Department of Internal Affairs.



**Inland Revenue at the Wellington Relay for Life event, March 2004**

“Relay for Life” is a 24-hour event, where people walk or run to raise funds for the Cancer Society, honour cancer survivors and remember those who have lost their battle with the disease.

Our people were out supporting the 2004 event. Karyn McLean, Senior Communications Advisor, who organised and ran in the Wellington event, said: “It was great to be involved in such a worthwhile event. By participating we show the ‘human face’ of the department and support for our community.”

# Tailored services meeting needs

A vital part of improving compliance is providing services that assist people who want to comply. Our compliance model promotes a more tailored, responsive approach to taxpayers and recognises the external factors that influence customers' compliance attitudes and behaviours. This year we have been further tailoring our services to improve compliance, and further build community confidence.

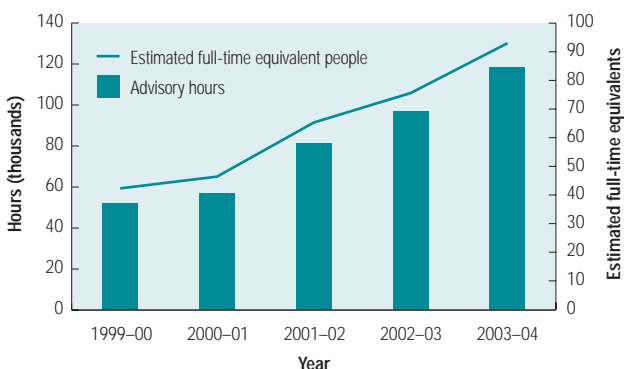
## Advisory services

We have had a range of advisory services operating in different communities since the early 1990s. These cover:

- Business Tax Information Officers for small and medium sized businesses
- Agent Account Managers for tax agents
- Community and social policy liaison officers for child support and other social assistance work
- Māori Community Officers providing services to Māori.

Advisory officer work includes assisting individual tax agents and businesses, carrying out general education seminars in schools, and taking part in *Heartlands* agencies in rural communities. This year, 93<sup>14</sup> people delivered a total of 118,150 hours in advisory visits to the community. The increase of 127% since 1999–00 reflects our increased focus on working with the community.

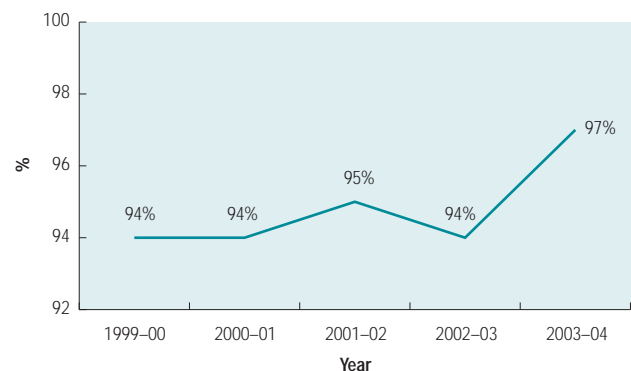
Figure 13 –  
Advisories



Our customers have consistently been very satisfied with the quality of our advisory services, with the 97% customer satisfaction rating this year, up 3% on 2002-03.

<sup>14</sup> Full-time equivalents. Some advisory roles are full-time positions. In other cases, the function may be carried out as part of a wider job description.

Figure 14 –  
Advisory services customer satisfaction



During 2003–04, we continued to focus on delivering our services to communities and undertook other initiatives to strengthen our focus. The following are some specific examples.

## Tax agents

Tax agents play an important role in ensuring the tax system works effectively by helping taxpayers understand and meet their tax obligations. We receive 74%<sup>15</sup> of income tax returns from agents on behalf of their clients.

We have both tailored and increased our focus on tax agents and their representative groups. Our call centres give priority to tax agents' calls and received over 900,000 calls from agents in 2003–04.

In 2002–03 we enhanced our Agent Account Manager role. These positions work with tax agents to improve compliance and encourage uptake of self-help services such as *look at account information service* and natural voice recognition.

<sup>15</sup> Excludes salary and wage earners.



**Andrew Minto (right), National Manager Operational Strategy and Design (OSD), at the 2003 ICANZ Conference. OSD is the business unit responsible for managing Inland Revenue's relationship with ICANZ and tax agents**

Colin MacDonald (Deputy Commissioner, Business Development and Systems) and Robin Oliver (Deputy Commissioner, Policy) spoke at the 2003 ICANZ Tax Conference. This provided an excellent opportunity to continue to develop Inland Revenue's relationship with the Institute.

Colin MacDonald spoke on the tax profession's changing interface with Inland Revenue. He outlined that as the tax system changes, the roles that Inland Revenue and the tax profession have continue to evolve.

The changing external environment impacts on our tax system. In response, Inland Revenue is working on strategies such as creating an environment that promotes compliance, and streamlining and simplifying tax processes. Changes in outside influences provide opportunities to take a fresh look at how we do things.

Robin Oliver spoke on "Taking a fixed tax position in a changing world: a personal perspective". He pointed to the need for tax advisors to take into account the prospect of legislative change, when giving advice to their clients. He noted that as a general policy, governments have been reluctant to have retrospective legislation but this was sometimes justified.

Robin outlined the considerations officials are likely to take into account when advising ministers on whether a legislative change should apply in the future or retrospectively, and whether to include provisions that protect the position taken by taxpayers under the existing law.

This year we have seen an improvement in the income tax filing rates by tax agents. By 31 March 2004, 93.35% of agents' income tax returns for the 2003 tax year had been filed. This compares to 92.31%, and 90.48% for the previous two years. Agent Account Managers have been particularly focusing on agents with poorer compliance records.

To continue to improve our services to agents this year, some of our staff spent a few days with a range of agents, from large city agents to small, sole-trader rural agents. This enabled our staff to gain an insight into the day-to-day practices of tax agents so we can improve the design of our services from a commercial perspective.

We have a longstanding and valuable relationship with tax agents through the Institute of Chartered Accountants of New Zealand (ICANZ). We discuss issues with them of mutual interest, and take part in their presentations to members around the country.

A recent example of us working with the private sector for better overall outcomes is our work with farmers and their tax advisors to reach a clearer understanding of the tax treatment of the costs incurred in converting farms to dairying. Uncertainty arose in relation to expenditure on farm conversion costs. This followed Inland Revenue confirming an initial view that when farms are converted to dairying, the cost of re-grassing and re-fertilising are capitalised and therefore needed to be depreciated.

Agreement has been reached with ICANZ on the important issue of the treatment of prior year expenditure on re-grassing and re-fertilising. However, there is some outstanding work in regard to the amortisation rate<sup>16</sup> to apply to this expenditure. Also, discussions are ongoing on the application date of this agreement.

Working closely with the Institute contributes to the development of good tax policy advice through the

<sup>16</sup> An example of this is when a new milking shed was put on a farm's books as a capital item and its value was discounted by 6% a year—a process known as amortisation—while all the associated costs of grassing and spreading fertiliser were expensed in the first year.

generic tax policy process and robust administrative systems that reflect an understanding of how the industry operates, its concerns and the requirement to collect tax. Initiatives such as the joint development of best practice guidelines continue to strengthen this valuable partnership.

## Corporates

Our Corporates group deals with the tax affairs of corporate taxpayers, high wealth individuals and other specialist taxpayer groups. This includes ensuring tax obligations have been met for companies with an annual turnover above \$100 million, companies whose industry is governed by specialist taxation legislation, or large companies who have non-resident ownership.

About 100 of New Zealand's high wealth individuals and their associated entities have their tax affairs administered by Corporates. High wealth individuals are taxpayers who have assets above \$50 million, or display certain high-risk attributes such as involvement in aggressive tax arrangements.



**Spyros Papageorgiou,**  
Group Manager  
Corporates, appointed  
in late 2003

Corporates Group Manager Spyros Papageorgiou says that while corporate taxpayers make up only 0.19% of taxpayers they generate over 45% of revenue assessed.

“We are dedicated to strengthening our people and organisational capability to provide a better service to corporate taxpayers. In the 2003 Budget, Corporates received additional funding to address the emerging tax risks associated with aggressive and international tax arrangements of large corporates and high wealth individuals,” says Spyros.

“By ensuring we have people with highly specialised technical and legal skills, appropriate tools and techniques, and by using international expertise, we will ensure this sector is fully complying with its tax obligations.”

## Industry partnership with small businesses

We are working with small businesses in a number of ways, including policy initiatives, improved processes and through our Business Tax Information Officers. We have improved the targeting of these advisories and also taken part in the Small Business Day series of seminars run by the Ministry of Economic Development.

Industry Partnership was established two years ago to address non-compliance relating to cash transactions and to improve relationships with industries. The businesses involved are mainly small and medium sized. Identifying common problems and reasons for non-compliance in an industry, and acting on those issues effectively across the industry is a key focus for this initiative.

The teams actively follow up issues for the partnered industries, and use education and assistance as well as detection and deterrence to improve compliance levels. We identify issues for follow up in a number of ways, including input from the industry groups which we have entered into a relationship with.

We have relationships with 14 groups to address compliance issues in the cash economy. We started with two industry groups, painters and decorators and electrical contractors in May 2002.

Since then, we have formed a further 12 relationships with industry groups representing agricultural contractors, home-based entrepreneurs, taxis, hairdressers and beauty therapists, collision repairers, automotive repairers, plumbers, long-distance coach drivers, carpenters, plasterers, gardeners and landscapers and the creative arts, with another planned for early 2004–05.

Industry Partnership continues to trial new approaches, such as a tactical campaign conducted with fruit pickers and contractors in the Hawke's Bay region, using media coverage of prosecutions as a starting point. An Industry Partnership team mailed orchardists in the area, then visited more than 115 orchards, providing information and advice on filing returns and paying taxes. This was supported by posters and leaflets, an 0800 number and classified advertising.

We have received positive feedback from the industries involved, for example Don Fraser, Chief Executive of the New Zealand Master Painters Association said "At our conference ...several happy situations were recounted where people had problems and had rung the Industry Partnership and had them solved very quickly and amicably... All the feedback we've had has been positive ...there was some apprehension of course when we decided we were going to have an industry partnership with Inland Revenue, but that was dispelled very early on by people visiting the various associations, and once you get a few good experiences coming out, good news travels quite fast."

(See also *debt* and *audit* sections for Industry Partnership results.)

## Addressing the needs of Māori customers

During 2003–04 we undertook a number of activities to develop our ability to address the needs of Māori customers, including the:

- implementation of the Māori authorities legislation, which was supported by the delivery of training seminars for Māori authorities around the country. An assessment of these seminars showed that those people attending found them useful.
- introduction of our Māori Language Plan (Tuia ki te reo), reflecting the Government's Māori Language Strategy Te Rautaki Reo Māori. Implementing the initiatives in Tuia ki te reo will help us to develop our long-term capability to design and deliver appropriate services that meet the needs of the Māori community. During the year, we celebrated Māori Language Week, as a way of getting our staff to have a go at speaking te Reo Māori and understanding Māori culture. This is a practical contribution to the development of our capability to deliver services to our Māori customers.
- development of an integrated strategy for addressing Māori tax and social support programme delivery needs. This will incorporate improved service delivery mechanisms and developing of our internal capability (such as the development of our capacity to provide services in te Reo Māori, as necessary). The development of this strategy will continue into the 2004–05 year.

## Cross-government initiatives

As a government agency, we need to work closely with other government departments on community initiatives. The most significant example of this is our work with the Ministry of Social Development on *Working for Families*—see more on this topic under *Implementing key government initiatives*. Other examples include:

- *Heartlands* agencies with a variety of other government departments
- working with other agencies to help alleviate tax difficulties arising from flooding
- cross-government strategies such as the New Zealand Disability Strategy, Positive Ageing and the Statement of Government Intentions for an Improved Community–Government Relationship.

Inland Revenue plays an active role in delivering services at *Heartlands* agencies, with 6,832 taxpayers and other customers being responded to during these agencies in 2003–04. We see our attendance at these agencies as an important part of our relationship building with those rural communities. They also ensure that people who live in their communities can access our tax and social support programme information. Attendance at *Heartlands* centres is also a part of our response to building strong relationships with the community, including tangata whenua organisations.



The team from Palmerston North Office who worked with central North Island flood victims

Back row, standing, left to right: Keith Jacob, Rhys Mohi, Wayne McNae, Vicki Cronin, Christine Jourdain, Pauline Brungar. Front row, seated, left to right: Sue Jex, Charmaine Ratima, Lynette Fischer, Hine Manuel, Paula Bedford, Philippa McNae, Dorothy Sushames, Lynne Hutchins

## Working with affected communities during the February 2004 floods

Inland Revenue staff showed outstanding commitment and dedication during the peak of the floods in the central North Island.

## Student loan borrowers

This year we have been focusing on improving the range of options available to student loan borrowers through our websites (see section on *e-government services*) and offering credit card payments. The latter were introduced in May 2004, primarily to make it easier for borrowers who are overseas to make payments against their loans. This is an important initiative as the percentage of non-resident borrowers is slowly increasing from 4.9% in 2001 to 6% of total borrowers at June 2004. However, they are responsible for 58% of the value of overdue repayments.

Between late May and 30 June, nearly 300 payments, with a total value of over \$272,000 had been made using credit cards. Over 70% of these payments were from overseas credit cards. We expect the uptake of the service to increase over the coming months to 1,800 borrowers a month.

We have also continued to deliver advisory information to groups of students at seminars and similar events.

Wellington Service Centre Manager, Mike Hewetson, coordinated Inland Revenue's flood relief response and he applauds the efforts of staff during the emergency. "Our staff actively reached out to the local community to help where possible."

A leaflet urging affected people to contact us as soon as possible was developed in less than 24 hours for distribution to taxpayers and other customers in the affected areas. The Ministry of Social Development set up a government phone line and one-stop-shops in the flooded regions with information on government services.

"We actively supported these initiatives, supplying staff with advice on obligations and entitlements. Staff immediately joined others to support the local one-stop-shops, providing a service no matter where and when it was needed."

Our Policy Advice Division advised government on disaster relief legislation which was introduced and enacted under urgency in March. This gave Inland

Revenue greater flexibility in dealing with business taxpayers who were badly affected by the floods. Positive feedback was received about this advice and the work of our people in the field.

Federated Farmers' President, Tom Lambie stated "Federated Farmers appreciates the tax department's significant support for farmers adversely affected by the storm and its aftermath. We cannot speak highly enough of the department's effort in trying to reach out to individual taxpayers."

Federated Farmers went on to say that an example of Inland Revenue's good work is the speed it responded to the storm. It set up a dedicated team and took a pragmatic approach to dealing with difficulties faced by individual farmers, such as those who lost all financial records.

The lessons we learnt during the February floods are now being used as the basis for our work in supporting people affected by the Eastern Bay of Plenty floods in July 2004.



**Community Liaison Officer Mihaka Panapa on the air with Radio Waatea host Dale Husband**

## Child support

Child Support was recently invited by Ngā Ture Kaitiaki ki Waikato Community Law Centre to appear on their regular Radio Waatea segment over a period of six months to present information on a variety of child support topics.

Community Liaison Officer, Mihaka Panapa, joins radio host Dale Husband on Wednesdays between 9.30 and 10.30 am, once a month, covering general information for paying parents, custodians, and anyone with an interest in child support.

The law centre, based in Manukau, runs an outreach service that is partly provided on community radio, where it aims to give relevant law-related information to listeners. Radio Waatea is a community station with Auckland-wide coverage, for a mostly Māori audience, but which also reaches the wider community.

It has been an excellent opportunity for Child Support to raise community awareness about child support, as well as interact with specific community groups through their own existing, well-supported forums.

“It’s been a great experience—an excellent way for us to talk directly to our community and raise awareness of some very practical aspects of child support,” Mihaka explains. “People will hear helpful information for themselves, and for family and friends. It has helped increase our visibility in the community and given clear, specific information to listeners.”

We have two pilot schemes under way to make it easier to meet child support obligations and for custodial parents to know when payments have been made. We are trialling text messaging payment reminders to paying parents. We plan to extend the trial to custodial parents to notify them that the payment has been made. Each pilot programme will run for three months and the findings from these will be incorporated into the service.

## Understanding our customers

Over the year we have been improving our analytical capability so we will better understand our customers and their behaviours. The outcome of this work will allow us to:

- be more customer-based in our thinking so we can provide better services by using approaches tailored to our different customers
- understand our customers better so we can make better and more effective decisions on ways of improving voluntary compliance.

# Focusing audits on long-term compliance

An important part of the community having confidence in the tax administration is for Inland Revenue to have a strong audit function to verify that taxpayers have paid the correct amount of tax. It is also vital that this function is seen to focus on the areas of greatest risk, such as when taxpayers have decided not to comply or do not want to comply.

Inland Revenue recognises that audit work has a key role in the wider process of compliance management. It has strong links to other business areas to support the collection and analysis of compliance risk intelligence and to initiate a range of responses to identified compliance risk so that compliance is improved over time.

This outcome is central to applying our compliance model approaches to our audit strategy. While the focus of our audit activity is on the taxpayer who has decided not to comply, selective verification is carried out among other taxpayers. This helps to maintain confidence in the tax administration by ensuring that the law is applied equally to those who attempt to comply voluntarily, and to those who do not. Our audit strategy helps us to improve our capability to perform audit work as well as achieving a better understanding of those areas that present the greatest risk to revenue.

## Focus of audit activity

Our investigation and litigation efforts reflected the overall shift in emphasis to the areas seen as posing the greatest risk to revenue. In 2003–04 our focus was on:

- taxpayers covered by our Corporates group
- aggressive tax issues
- cash economy evasion
- fraud and other tax evasion.

(See also *Using the full force of the law*.)

## Corporates

These are mainly large enterprises with a turnover above \$100 million and taxpayers covered by special arrangements. In 2003–04 we assessed \$296.5 million in net discrepancies from this customer group. Our focus for the year was on:

- Closely monitoring the top companies and streamlining our risk evaluation process by introducing targeted risk reviews and a formal approach to risk prioritisation.
- High wealth individuals—we have a separate unit targeting 100 high wealth individuals. Analysis performed to date shows that this group of individuals controls approximately 3,500 entities. Detailed questionnaires have been sent to 69 persons seeking information relating to assets, income, and associated entities, including trusts. To date 57 responses have been received. The questionnaire responses are being matched against a range of information. We anticipate that risk profiles will be completed for the 100 cases in 2005.
- Currently 13 cases are subject to full investigations. They involve complex business structures, including numerous companies and trusts both in New Zealand and offshore. The top four cases involve over 100 entities in each case. Issues identified to date include the treatment of: inter-company transactions, trust structures and transactions, capital gains, tax residence and the treatment of lifestyle assets. By their very nature these cases are complex and will take some time to reach conclusive positions.
- Using questionnaires to evaluate foreign and New Zealand-owned multinationals for their transfer pricing and record keeping requirements. We have now received over 350 responses from companies with a turnover above \$20 million. Where appropriate, more detailed documentation reviews and audits have been completed, and in some cases companies have been put on notice in relation to their ongoing pricing. Special projects have also been conducted in relation to specific industries and our largest

corporates. In addition, advance pricing agreements have been reached with 11 corporates and a further 10 agreements are currently in progress.

- Reviewing structured financial arrangements that have been identified in the banking industry. This review has led to assessments being issued and further investigations being carried out.



**Peter Consedine,**  
Area Manager, South  
Island Investigations

### Property investigations uncover over \$4.7 million in discrepancies

We have been watching transactions involving property development and speculation, particularly at times when the market is expanding. In those areas of rapidly rising prices, we identified an emerging risk to the tax revenue base from a pattern of activity where people, hoping to make quick profits, bought and then on-sold property quickly.

“Many of the people buying up sections in new developments may not be aware of tax implications if they bought properties with the intention of on-selling them, often within a short time, in order to make a profit”, says Peter Consedine, Area Manager, South Island Investigations.

### Aggressive tax issues

These are schemes designed to reduce a taxpayer’s tax liability and are often “marketed” to wealthy investors. For 2003–04 the largest single category of discrepancies was for disallowed depreciation on intangible property relating to aggressive tax avoidance arrangements.

Aggressive tax issues also accounted for a large part of our litigation work in the High Court this year. The test case for New Zealand’s second largest alleged tax

“If people buy property purely to on-sell at a profit, they will be liable for income tax on any profit made.

“We routinely keep our ‘eyes and ears open’ about a wide range of areas where there may be less than full compliance with tax obligations. During 2004, we looked more closely at developments in the property market, including a focus on Queenstown and Wanaka. As part of our routine activities, staff also looked at associated activities, such as building and construction,” says Peter.

“Obviously, Inland Revenue is likely to be initially interested in sales involving properties which have only been held for a very short time. However, the buyer’s intention or purpose at the time when they bought the property is the most important indicator when determining a tax liability.”

The law can be complex and people may need to seek professional advice. People need to talk to their tax agent or contact Inland Revenue if they need to clarify the tax situation before they buy or sell property. As at June 2004, Inland Revenue had undertaken 460 investigations in relation to the Queenstown and Wanaka property market, with another 64 investigations ready to go. So far, this work has revealed more than \$4.795 million in unaccounted tax involving the property market.

avoidance case, concerning investments in the ACTONZ joint venture, was heard in July and August 2003. On 14 November 2003 the High Court delivered a judgment which found in favour of Inland Revenue on all issues. The investors have appealed this decision.

In 2003–04, we assessed \$181.3 million in net discrepancies concerning aggressive tax issues, 39.6% over target reflecting an increased focus in this area.

### Cash economy evasion

Audits were carried out in high-risk areas and have led to prosecutions—for example in the taxi and contract fruit picking industries (see also *Industry Partnership*).

### Fraud and other tax evasion

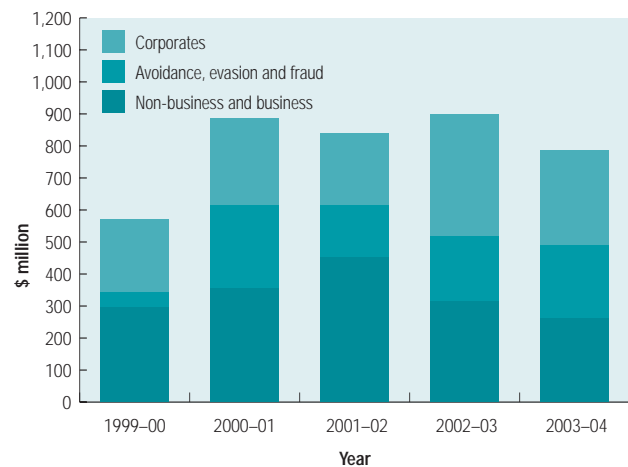
Audit activity led to the prosecution of tax agents who had obtained money intended for their clients, a major case involving rebate fraud, and close attention to speculative property transactions where quick profits were being made. During the year, we assessed \$48.9 million in net discrepancies (64.6% over target) from fraud and evasion activity. The result reflects improved risk assessment and additional resources being applied to detect tax evasion.

### Audit discrepancies

We identified a total of \$787 million in audit discrepancies<sup>17</sup> this year, 4% over our targeted figure. The result of this work is also reflected in the amount of tax in dispute. This is tax generated from current audit activity of businesses, but will generally flow on to future periods as discrepancies when the dispute is resolved. At \$386 million, the level of disputed tax is \$99 million higher than last year.

Discrepancies over the years have also reflected the shift in emphasis to corporate taxpayers and those involved in areas of aggressive tax avoidance, or evasion and fraud.

**Figure 15 –  
Net audit discrepancies**



**Figure 16 –  
Audit discrepancies budget versus actual**

	Annual discrepancy budget \$ million	Net discrepancies \$ million
Non-business audit and business audit	294	260
Aggressive tax issues	130	181
Tax evasion and fraud	30	49
Corporates	301	297
<b>Total</b>	<b>754</b>	<b>787</b>

However, not all these adjustments to a taxpayer's return result in an immediate financial liability or additional tax to be paid in the year that was audited. Adjustments to losses have a potential impact on current or future tax obligations and changes to imputation credits are made in anticipation of a future tax liability. Audits that result in adjustments of this kind are important because they protect the future tax revenue base. In 2003–04:

- discrepancies totalled \$787 million
- less adjustments to losses of \$212 million
- less adjustments to imputation credits of \$69 million
- net result 2003–04 was \$505 million.

<sup>17</sup> A discrepancy is the difference between the tax previously returned or calculated by the taxpayer and that which is ascertained as a result of an audit (plus penalties and interest if applicable).

The 10 most commonly occurring discrepancies (by dollar value) in 2003–04 were:

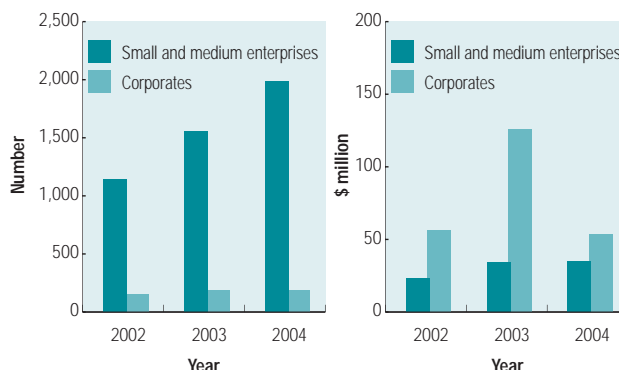
- depreciation, \$134 million—mainly arising in aggressive tax avoidance cases where depreciation on intangible property was disallowed
- losses carried forward, \$82 million—generally because corporate taxpayers have incorrectly applied losses between years or between related companies
- GST on understated sales, \$77 million
- imputation tax adjustments, \$69 million—corrections to the taxpayer’s account so that it agrees with that of the company’s imputation accounts
- treatment of reserves and provisions, \$41 million
- incorrect use of branch equivalent tax account, \$36 million—relates to the tax on controlled foreign companies owned by New Zealand companies
- GST time of supply adjustments, \$28 million
- default assessment, \$18 million—issued when taxpayers have failed to file a return
- sales not accounted for, \$17 million
- GST time of supply adjustment, \$14 million.

Audit-assessed debt is now given higher priority in our debt collection system. This is being done by ensuring that audit-assessed debt is clearly identified in our systems so that we receive a “complete” compliance result.

### Voluntary disclosures and refunds

The discrepancy figures above include cases where taxpayers have made voluntary disclosures about under-reported tax. The disclosures can be made by a taxpayer before, or during the course of an audit. The law provides that these disclosures result in lesser penalties being imposed. The disclosures result from a positive approach by taxpayers to getting their affairs right, together with a desire to avoid or reduce exposure to shortfall penalties and to avoid the consequences of detection in an investigation. This year we have had more disclosures, and the value of the corporates disclosures has returned to normal levels.

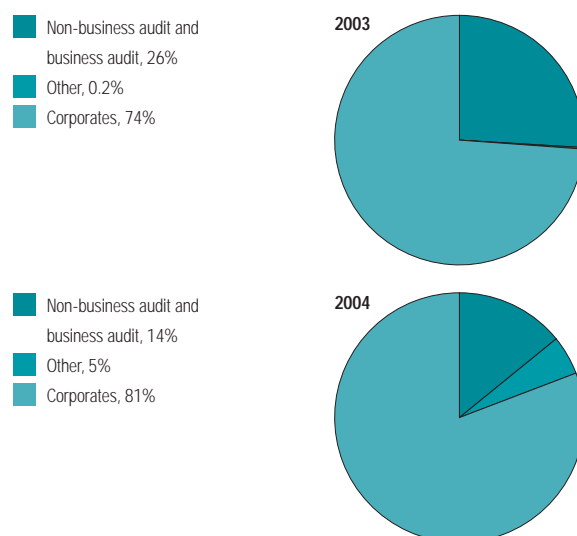
Figure 17 – Voluntary disclosures



Audit work may also find that a taxpayer should actually receive a refund or a credit.

This year we identified \$37.46 million in refunds compared to \$73.46 million in 2002–03. Part of the reason for the difference was that last year two cases accounted for just over \$19 million of the refunds. The differences arise because taxpayers have made mathematical errors, overstated sales or have left out expenses that are actually deductible.

Figure 18 – Audit credits and refunds found in the taxpayer’s favour



## Quality and timeliness of audit work

The quality of our audit work showed significant improvement on last year, with 95.4% of surveyed audits meeting the standards. This compares to a target of 85% and last year's result of 87.9%. The survey involves taking samples of audit work from across New Zealand and the different areas of investigation. The results for 2003–04 reflect an increased focus on quality.

We completed our audits more quickly than targeted:

- business audits completed within an average of 2.4 months (target: 4 months)
- investigations completed within an average of 10.5 months (target: 12 months)
- audits by our Corporates group completed within an average of 10 months (target: 17 months).

## Industry Partnership

Although audit activity has always been carried out in cash economy industries, this year we have continued to strengthen our focus through our industry partnership approach. Our investigators have been concentrating on partnership industries where there is deliberate non-compliance.

In all, ten industries have been covered, with most of the cases completed being in the agricultural contracting, hairdressing, collision repair and painting and decorating industries. The total value of discrepancies identified was \$5.5 million. The most common discrepancies arose from:

- purporting to charge GST
- understating or overstating sales to evade GST payments
- not declaring income
- failing to account for PAYE.

Prosecutions have been taken when appropriate—see section on *Using the full force of the law*, for some examples of action taken.

In 2004–05 we will set up Industry Partnership assurance teams that focus specifically on issues arising from deliberate non-compliance. The teams will undertake investigations and address the return and debt issues associated with Industry Partnership industries, as well as gathering further community intelligence.

## Audit strategy

Work has continued on the implementation of our audit strategy. The strategy is assisting us to change our audit processes to focus on compliance, with an emphasis on the use of gathered intelligence and the range of appropriately targeted responses that can be applied to compliance risk.

The main areas of focus in 2003–04 were:

- **Improvements to the way compliance risk is identified and determining the appropriate response**  
Dedicated compliance risk analyst positions were established to increase the level of effort and expertise devoted to intelligence gathering and analysis. The positions have been designed to carry out research into compliance levels in specific industries. This helps us to target those who are not complying voluntarily as well as supporting our efforts to reduce compliance costs of those taxpayers who do.
- **Strengthening our capability in complex tax areas of high compliance risk corporate taxpayers**  
One of the difficult areas of addressing compliance is the complex nature of arrangements made by corporate taxpayers. It requires a high level of technical tax knowledge and legal expertise, especially about international tax arrangements. Our Corporates group received an extra \$3.7 million in the 2003 Budget to increase its capability, including establishing a new unit to improve risk analysis. Work has also been undertaken to streamline the process for identifying risk issues that may require legislative change.

- **Training our audit workforce to a higher level of competence and capability**

We have recently implemented a comprehensive training framework within our audit units. The framework provides a structured two-year learning programme. It is designed to develop auditing skills and tax technical knowledge to the level required to undertake the most demanding and complex types of case work found within our non-corporate areas.

- **Improving technology to support audit work**

Besides designing and introducing a number of computer tools to assist investigators in the performance of their work, they are being provided with laptops for use in the field. Greater mobility will lead to greater visibility in the community, with more audit work being completed onsite.

- **Developing new ways to measure our audit outcomes**

With the introduction of the compliance-based framework, we recognise the need to change the way we measure our audit performance. We have designed the process to measure the impact of audits on compliance and further work will be carried out in 2004–05.

## Progress on OAG Report recommendations

When the Office of the Auditor-General (OAG) reported on our taxpayer audit activities in August 2003, 11 recommendations were made. These have been implemented or incorporated into our audit strategy. Two of the recommendations will take longer to come into operation—the way we manage audit cases and the full implementation of intelligence systems. They are part of long-term projects and will result in future system changes.

The enhancement of our audit processes is a continuous activity and the time for completing the current initiatives is about five years.

## Working with the OECD

Inland Revenue has been working to develop relationships with other tax administrations through the Organisation for Economic Cooperation and Development (OECD). In April 2004, we hosted a meeting of more than 50 specialists who came to Auckland to discuss international tax evasion and avoidance schemes. This is the first time this gathering has been held outside of Paris.

The increasing use of cross-border tax evasion and avoidance schemes is a major challenge for all tax administrations and the meeting looked at legal ways to facilitate cooperation and the effective exchange of information between tax administrations.

In addition, this year Robin Oliver, Deputy Commissioner (Policy), was appointed Vice-Chairman of the Bureau of the OECD's Committee on Fiscal Affairs.

# Managing debt and outstanding returns

Our overdue debt and return collection activities allow us to influence and maintain community confidence, through tailoring our enforcement activities to reflect the severity of non-compliance. By doing so, we can show people that deliberate non-compliance will be dealt with firmly, while minor transgressions are dealt with in a more appropriate manner.

Much of the work mentioned earlier in this report helps prevent debt, but when debt does occur we have worked hard to assist those who have genuinely tried to comply but, for whatever reason, have failed to do so.

We have also taken firm action against deliberate non-compliers, including those identified through our audit activities. For example, during the year there has been an increase in our use of our statutory powers to gain payment where companies have been deliberately stripped of their assets to avoid paying their tax liabilities. Several sums over \$1 million have been recovered using these statutory powers.

We are also identifying taxpayers who are using the insolvency laws to avoid paying tax. These non-compliers voluntarily liquidate their companies and choose the liquidator. A new company is then incorporated to continue the same business but without the liabilities.

We are now highly active in the insolvency area and have replaced questionable liquidators, followed up assets that have been transferred out of the company for no consideration or under their value and pursued directors for the personal use of company funds.

Our efforts in one liquidation resulted in the director of the company entering into an arrangement with the liquidator to pay \$850,000 of tax. This was to avoid legal action against the director for the personal use of company money. In addition, our actions in the insolvency area have been effective in having four people banned as directors for their repeated involvement with insolvent companies.

## Improving our performance

We have also been looking at how we can maximise the level of taxpayers filing and paying on time by

ensuring we work with taxpayers to make it easy to comply. To achieve this result in 2004–05 we will complete an on-time filing and paying strategy. This will guide us in the further development of our processes, our people capability and our relationships with customers, so that we achieve and maintain higher levels of compliance. This year we have carried out research on the issue. We are combining the findings of our analysis and the research so we can develop services tailored to respond to different behaviours.

Even though considerable efforts are being placed into improving and maintaining on-time filing and paying, maintaining our current performance will be a challenge in 2004–05, as we continue to deal with the increasing level of complexity in debt.

The performance highlights for our outstanding return and overdue debt management activities are outlined as follows.

## Outstanding returns

During the year, we identify all returns that were expected to be filed, but were not, and take appropriate follow-up action to obtain these returns. Of those not filed, 82.1% were collected within 12 months of their due date. The prompt collection of returns ensures that we are able to assess a taxpayer's correct liability in a timely manner.

At times, it is necessary to prosecute non-complying taxpayers who have taken a stand against filing their returns (see section *Using the full force of the law*).

Given the compliance nature of outstanding return collection work it is hard to achieve high levels of customer satisfaction. This year, our survey of customers with outstanding returns showed that 61% were satisfied with our return collection activities, compared to 57% in 2002–03.

### Overdue debt

During 2003–04, we collected a total of \$1.099 billion of overdue debt in cash.

Improvements in the management of overdue debt included:

- clearing 39,500 more debt cases than in 2003, thereby removing 9,500 debtors from our books
- reducing by 3.1% the average age of open debt cases
- \$184 million decrease in net collectable debt and a \$120 million increase in debt under instalment.

These results mean our collectable debt position improved by \$64 million, the first time that debt has declined in five years.

These improvements can be linked to:

- focusing on collecting high value debts
- legislative change through the debt and hardship provisions, and
- the investment made in upskilling our staff working in this area.

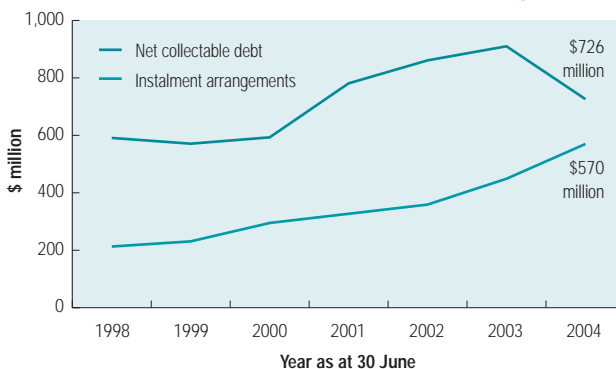
Figure 19 – Debt summary<sup>18</sup>

	2003 \$ million	2004 \$ million
Total outstanding debt	2,324	2,343
Less debt deferred due to tax in dispute, debt assessed in the absence of a return, and debt to be written off	964	1,047
Collectable debt	1,360	1,296
Less debt under instalment	450	570
<b>Net collectable debt</b>	<b>910</b>	<b>726</b>
Cash collected during year from debt activities	1,042	1,099
Penalty and interest component of total outstanding debt	1,049	1,013

<sup>18</sup> These debt figures include all debt types with the exception of child support debt.

Included in the total outstanding debt figure are monies that can be collected and those that are categorised as being non-collectable at the time.

Figure 20 – Net collectable debt and instalment arrangements



The level of collectable debt decreased by 4.7% to \$1.296 billion—the target was less than \$1.35 billion. Collectable debt includes debt that is under an instalment arrangement. These arrangements allow taxpayers to successfully reduce their tax debts over an agreed period of time. Currently, \$570 million (51,314 taxpayers) of debt is under an arrangement representing 44% of collectable debt, compared to 33% in 2003.

Figure 21 – Level of debt under instalment arrangement

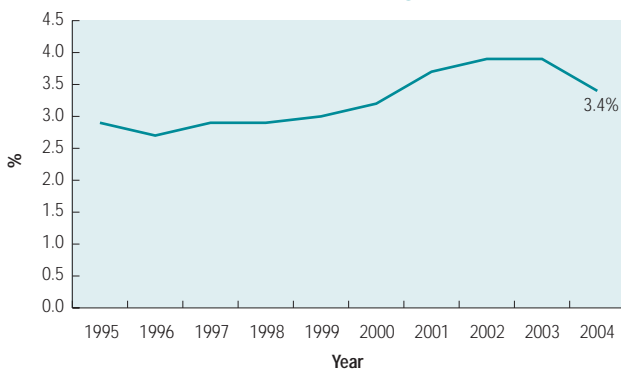
Year ended 30 June	Value of debt under instalment \$ million	Annual change %
1998–99	231	28%
1999–00	295	11%
2000–01	327	10%
2001–02	359	25%
2002–03	450	27%
2003–04	570	

Over 100,000 new instalment arrangements were entered into in the last 12 months, up 40% on last year. Of the new arrangements over 40,000 had paid their debt by 30 June.

The other component of collectable debt is net collectable debt which is at its lowest level since February 2001. We are currently undertaking collection action on 71% of the net collectable debt.

A key measure of debt performance is collectable debt as a percentage of revenue.

**Figure 22 –  
Collectable debt as a percentage of revenue**



The increase in revenue has contributed to this improvement, along with significant improvements in our debt collection activity.

The balance of Inland Revenue debt is categorised as non-collectable debt and includes:

- debt deferred or under dispute in the courts. Much of this debt relates to litigation following tax audits. There is currently \$435 million in the deferred debt category, up \$99 million on June 2003.
- assessments raised by the department in the absence of a filed return by a taxpayer, and
- debt that is with the Official Assignee or Liquidator and awaiting declaration of a final dividend.

We strive to collect debt while it is young and therefore easier to collect, while continuing to clear older debt.

This can be seen with the improvement in debt paid within 24 months.

**Figure 23 –  
Timeliness of debt payment**

	2003	2004
Paid within 6 months	78.9%	78.8%
Paid within 12 months	86.1%	86.6%
Paid within 24 months	89.9%	92.5%

Our approach to debt is reflected in our customers' satisfaction with our service. The nature of overdue debt collection means it is hard to achieve high levels of customer satisfaction. This year, of overdue debt customers surveyed, 66% were satisfied with our overdue debt collection activities, compared to 57% in 2002–03.

### Debt and hardship provisions

The debt and hardship provisions (implemented in December 2002) provide us with greater flexibility when dealing with taxpayers who are in debt or financial hardship. These provisions are influential when considering a taxpayer's financial capacity to meet their debt repayments, particularly as they give us the flexibility to write debt off if repayment of the debt would place the taxpayer in "serious hardship". Being able to use these provisions has also resulted in the large increase in the amount of debt under instalment arrangement (as discussed earlier).

**Figure 24 – Debt cases written off using hardship provisions<sup>19</sup>**

Year	Cases	Value	Average per case	Annual increase/decrease	
		\$ million		Cases	Value \$ million
1999–00	5,736	10.7	1,857	–	–
2000–01	17,579	38.4	2,183	11,843	27.7
2001–02	27,949	58.3	2,087	10,370	20.0
2002–03	55,803	116.4	2,086	27,854	58.1
2003–04	43,827	90.9	2,075	-11,976	-25.5

### Improving debt profile from industry partnership approach

Looking at the longest-standing relationships (painters and decorators, electricians), the partnership approach has had some pleasing results relating to debt profiles. The following table compares the current profile to that before Industry Partnership's establishment just over two years ago.

**Figure 25 – Industry partnership debt and returns**

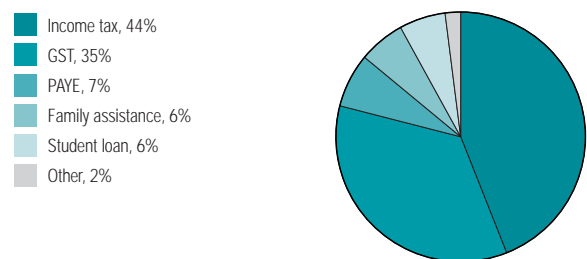
	As at 30 June 04
Number of debt cases	23% decrease
Average age of debt	16% decrease
Percentage of debt under arrangement	258% increase
Number of outstanding returns	27% decrease
Average age of outstanding returns	20% decrease

### Provision for doubtful debt

There will always be a need to make a provision to cover doubtful debts (see Note 9 in Part 7 of this report). For the 2003–04 year, the total provision was \$554.6 million, which is \$41.2 million over the 2003 provision.

### Debt by tax type

**Figure 26 – Total outstanding debt by tax type**



The tax types comprising debt have remained relatively steady between 2003 and 2004. Minor reductions in family assistance and income tax debt have been offset by 2% increases in GST and student loans.

### Family assistance debt

Family assistance debt, totalling \$141.2 million, was \$22.6 million lower than the 30 June 2003 total. Because people receiving family assistance can easily receive an over or underpayment when their circumstances change, we take proactive steps (such as checking actual income against predicted earnings) to avoid debt being incurred, or to minimise any debt that does occur. Although the percentage of family assistance customers with an overpayment debt remained at the same level as last year (28%), the value of those overpayments is steadily falling.

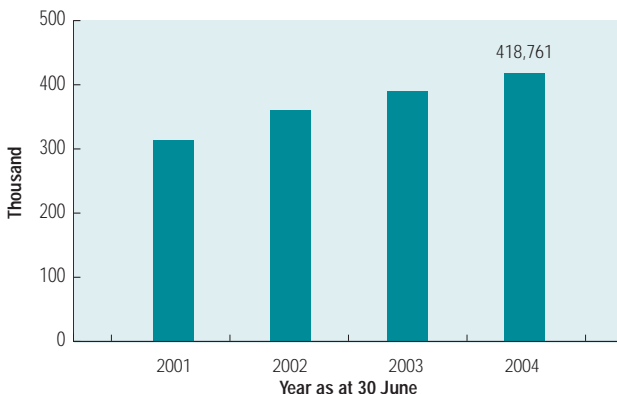
<sup>19</sup> The higher figure for 2002–03 reflects the expected higher levels of write-offs following the changes introduced on 1 December 2002.

We have also used the debt and hardship provisions to consider whether family assistance debt can be collected, taking into account the current financial position of the debtor.

### Overdue student loan repayments

In 2003–04 there were 393,382 student loan borrowers living in New Zealand and 25,379 overseas.

**Figure 27 –  
Total student loan borrowers**



As at 30 June 2004, there were 53,075 borrowers who had overdue repayments totalling \$139 million. While the value is \$37.8 million above last year it is \$12 million below predicted levels. Overdue debt had been predicted to grow due to a combination of factors, including both increased borrower numbers and non-resident borrowers. Overdue repayments represent 2.3% of the total student loan balance.

**Figure 28 –  
Overdue repayments – student loans**

	2003 \$ million	2004 \$ million
Resident borrowers	43.1	57.9
Non-resident borrowers	58.1	81.1
<b>Total</b>	<b>101.2</b>	<b>139.0</b>

Non-resident student loan borrowers continue to have a major impact on the level of repayments owing, as they account for a large number of debt cases that are relatively difficult to clear. To address this issue, we

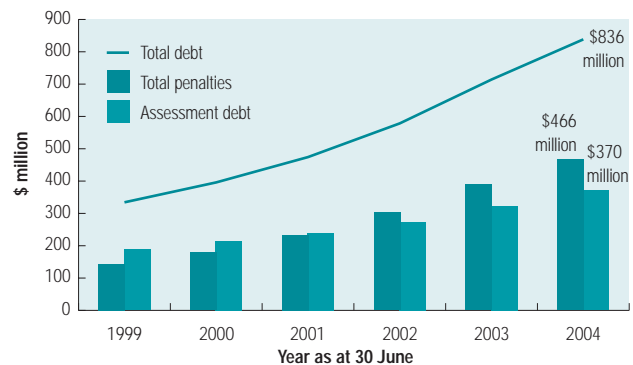
introduced measures to make it easier to repay, including a credit card payment option and the ability to securely look at account information online (see section *e-government services*).

The provision for doubtful debt for student loan borrowers is now \$718.775 million.

### Child support debt

This year we have seen the growth rate of child support assessment debt (the amount people have been assessed to pay, but have not paid) slowing from 18% to 14.5%.

**Figure 29 –  
Child support debt**



Currently, our penalty debt is increasing with limited options available for debtors, other than paying off the full value of the assessment and penalty debt. Although sanctions for non-compliance are important they can also, over time, create a perceived barrier to people fully meeting their obligations. Proposed legislative change focuses on improvements to the way child support is administered, with a bill scheduled for introduction in the second half of 2004. The main proposal is to tackle the problem of child support debt by forgoing the collection of some penalties to provide an incentive for non-payers to re-enter the payment system.

Of total debt, 66,340 customers have an arrangement with Inland Revenue to make regular payments; a similar number to last year. The value of debt under instalment has grown by 6% this year to \$261 million, although the percentage of debt under instalment has declined by 3% to 31%.



**Child Support Christchurch debt team**

*Seated, left to right: Gareth Sanders, Jason Grose, Louise Davidson, Ken Pope. Standing, left to right: Beverley Tobin, Kaye McLean, Larissa Batchelor. Absent: Jon Kingsbury.*

## **Child Support—making a real difference**

“One of the best things about working for Child Support is seeing the real difference we make to the lives of families,” says David Udy, National Manager, Child Support.

Our focus has been on reducing the debt of people who owed more than \$5,000; they represent 27% of total debt and 9% of our customer database<sup>20</sup>. At the start of the year this group comprised 11,336 cases who owed \$116.2 million in assessment debt (\$224.6 million total debt). Our focus has resulted in a significant improvement in the profile of this group including:

- in 2003–04, 43% of current year assessments were paid in full and on time, compared to 27% in 2002–03
- a 4% reduction in their assessment debt to \$111.5 million, while total assessment debt slowed from 18% growth last year to 14.5%
- 447 customers who owed \$7 million in debt with an average value of \$15,660 are now debt-free.

We are now expanding our current focus to include:

- actively case managing new customers for a longer period to ensure early compliance habits are formed and maintained

- increasing the number of debtors being actively case managed and focusing on paying parents who are self-employed and have a high assessment debt
- improving the collection of debt from salary and wage earners
- developing relationships with employers to ensure paying parent deductions occur
- increasing our focus on the debt of overseas customers.

We have already improved our ability to collect debt from people based in Australia. Under the enhanced reciprocal agreement with our equivalent Australia-based agency it does not matter whether a person is based in Australia or New Zealand, their debts will be followed up for payment.

“It’s very rewarding to be able to collect payment from a parent where there has been continued non-compliance for some time because of the difference it can make to the custodian and children.

“The actual work of negotiating a payment takes some effort to ensure the interests of all parties are taken into account. This possibly includes the new family of the paying parent, as well as the custodian and children who have been missing out on the payments. If we can’t negotiate an arrangement to pay off a debt over time and maintain any current payments, then we take enforcement actions.

“We’ve all got stories of where we have telephoned custodians to tell them that they will be getting some extra money because a child support debt has been paid or enforcement action has resulted in collection from the paying parent. Sometimes the money has been outstanding for a number of years and the custodian gets quite emotional in telling us how the payment will improve their child’s quality of life. Sometimes

this is for basics like healthcare, such as new glasses.

“We’ve also found that getting debt under control can be a real relief for the paying parent. This year Child Support got some extra funding to deal with customers with long-term and high-level debts of over \$5,000. These parents were often difficult for us to reach—for instance, if we knew their contact details, they may not have responded to our mail or telephone contact. And sometimes it was the worry of the level of the debt that stopped them communicating with us. Some paying parents have told us what a relief it is to be doing something about the debt, rather than just have it hanging there.

“Having the extra funding has allowed us to individually case manage these customers. We’ve been able to put extra effort into making contact and either negotiate payment of the debt over time, arrange the payment of a lump sum, or take enforcement action. The results of our actions have seen some positive outcomes for families.”

<sup>20</sup> As at 30 June 2004.

While this means payment is collected from parents based in Australia, our debt figures also increase from the New Zealand-based Australians who we are now following up for payment of debt. Under the reciprocal agreement:

- \$22 million (2,400 debtors) of our total debt concerns Australians now living in New Zealand
- \$77 million (5,200 debtors) of our total debt concerns New Zealanders now living in Australia, up from \$29 million in 2002–03
- approximately \$3.2 million has been collected on both sides of the Tasman.

The provision for doubtful debt (penalty and interest only) has increased by \$60.6 million from 2002–03, reflecting the growth in penalty debt. The increase in the provision is \$21.5 million less than the increase last year.



# Adjudicating and ruling on the law

The role of our Adjudication and Rulings group is to identify and apply the correct interpretation of the Inland Revenue Acts and other relevant laws while considering case law.

This year we focused on further building our people capability in this complex and highly technical area. Although our staff numbers have been slightly below full complement during the year, we have recruited to both entry-level and senior positions over the past few months. These senior positions include a new group manager, three senior tax counsel and a principal advisor. In addition, we have continued our professional training for both graduates and more experienced staff.

Our Rulings units produce binding rulings that provide clarity on the Commissioner's view of the law as administered by Inland Revenue. Although we did not receive our forecast number of rulings for the year, we completed 139 more than in 2003. Like last year we met all of our quality targets, and this year we also achieved all our timeliness targets.

Our Corporates group has also begun carrying out some rulings with their role forecast to increase in 2004–05. This will free up the Rulings Units to focus on the more difficult and contentious rulings, as well as the production of public rulings and statements.

Our Adjudication unit plays an integral part in resolving a number of the disputes that arise between taxpayers and Inland Revenue during the course of administering the tax laws. The function of the unit is to consider disputes independently of the audit function, to ensure consistency and impartiality in the application of the tax law.

During 2003–04, there were 67 adjudication cases, compared to 63 cases in 2002–03. Although all cases met the quality standards and were allocated within the required timeframes, we did not meet the targeted average time for completion of 16 weeks. This was due to a particularly complex project that involved 14 separate statements of position and referrals, which took 51 weeks to complete. The average of all other cases was just under 16 weeks.



The Tauranga investigations team who worked on the Sharma case

Front, left to right: Peter Cooke, Todd Blythe, Kane Hetherington. Middle: Mike Williams, Peter Hastings. Back: Paul Hamilton

## Fruit picking contractor given 21-month prison sentence

Yoginder Sharma was sentenced in Tauranga to 21 months in prison after pleading guilty to one charge of tax evasion.

# Using the full force of the law

We use the full force of the law when circumstances warrant it, for example, when people:

- do not file tax returns
- operate in the “cash economy”, or
- engage in schemes designed to avoid paying tax.

We have also actively investigated and carried out prosecutions in cases of deliberate fraud involving false documents and tax agents who have taken their clients’ funds.

By exercising these powers we also ensure that people maintain their confidence in the tax administration. This especially applies to taxpayers who operate their business alongside others who do not fully report their income or pay GST. They will be assured that their businesses will not be undermined by unethical operators.

## Use of our powers

Sections 16 through to 19 of the Tax Administration Act 1994, gives us a wide range of powers to encourage compliance. These powers allow us to:

- access private premises
- request the books and documents
- institute enquiries under oath in a district court or before a suitably delegated officer of the department.

The Court heard that Inland Revenue estimated that a total of \$168,472 had not been accounted for, however the full extent of the offending wasn’t known.

This year we have been focusing on tax evasion in the fruit picking and contracting sectors, particularly in the Bay of Plenty, Hawke’s Bay, Otago and Marlborough. Legitimate orchardists, contractors and pickers working in the industry are welcoming Inland Revenue’s efforts to stamp out tax fraud.

Tony Morris, Hamilton Service Centre’s Area Manager Investigations, says “We’re heartened

by the response we get when we’re out talking to people in the orchards. Those people who don’t pay their taxes are able to undercut the legitimate players, and that’s not fair to all those people who do pay their fair share of taxes.

“We think people realise that tax evasion is stealing from the whole community. We want the people involved in these types of tax evasion schemes—and the people who turn a blind eye to it—to understand that sooner or later they’re going to get caught,” says Tony.

These powers are used sparingly in a formal way to assist gathering relevant information from, or about, taxpayers who may not be fully complying with their tax obligations. During 2003–04, we used our powers 486 times, as shown in Figure 30.

**Figure 30 –  
Use of powers**

		Total formal usage
s16	Judicial warrants for access to private premises	9
s16	Where it is proposed to demand access to premises	6
s16	Where it is proposed to demand a person to provide assistance	1
s17	Notice to provide books or documents	434
s17A	Court order for production of records	6
s18	Enquiries before a district court judge	1
s19	Enquiries before the Commissioner of Inland Revenue	29

### Prosecution action

In 2003–04, we took action in a number of ways. Prosecutions were taken where people had not met their obligation to file returns, resulting in:

- 553 cases for failure to file income tax returns
- 380 cases for failure to file GST returns
- 42 cases for failing to deduct or account for PAYE deductions.

Prosecutions have been taken for deliberate non-compliance within Industry Partnership industries. The most notable among these have been in the contract fruit picking industry where operators have been evading tax. The extensive media coverage of these cases sent strong messages to the public about Inland Revenue's attitude to tax evasion, and has lent support to initiatives aimed at gaining overall compliance in an industry that does not have a good compliance record.

### Fraud

Our audit work has also revealed major cases of fraud. In these cases, people have used false documents to systematically defraud Inland Revenue. Two cases have also led to the prosecution of tax agents who had taken funds from their clients or refunds that had been paid by Inland Revenue. In some cases the magnitude of the fraud has meant that we have involved the Serious Fraud Office in the investigation and prosecution of the offenders.

In 2003–04 Inland Revenue completed 47 prosecutions, (both under revenue Acts and the Crimes Act) as a result of audit activity. These cases were mainly concerning evasion of income tax, GST and PAYE. A further 23 cases are pending.



**David Welsh, Team Leader, Audit, who worked on the Hirawani investigation, with Loraine Elliott, Auckland South Service Centre Manager**

### Five years jail for making fraudulent rebate claims

Peter Charles Hirawani was convicted in the Manukau District Court in November 2003 on 369 charges of fraudulently claiming tax rebates. He was sentenced to five years on each charge, to be served concurrently.

The tax agent had claimed fraudulent rebates on behalf of clients for donations made to charity, childcare costs and fees paid to him. He then took a 15% fee. This activity took place during 1999–2000, but he filed back year returns for the tax periods 1991–99. Auckland South Service Centre staff spent two and a half years investigating the \$1.8 million fraud and had the defendant extradited from Sydney.

Loraine Elliott, Auckland South Service Centre Manager, says the fraud came to light when sharp-eyed investigators in Tauranga noticed large numbers of people were filing returns for previous years, claiming rebates for childcare and donations.

As it became clear that the fraud had caught up people across the North Island, the investigation team grew. A dozen investigators, working in three teams, completed the case, which culminated in 376 tax charges being laid.

Ms Elliott said the case was significant for Inland Revenue. “It’s the biggest rebate fraud case we’ve had. It involved many individual taxpayers, and there were 100 witnesses called. It was a major step for us to extradite someone, and our computer forensic unit helped to produce crucial evidence.

“The professionalism, commitment, persistence and hard work of our staff played a vital role,” said Ms Elliott. “They were superb.”

A number of measures have been put into place to mitigate the risk of this kind of fraud happening in the future. These include:

- ensuring that rebate claim forms are not processed without receipts for the expenditure
- educating targeted groups about what expenditure is claimable—this is resulting in voluntary disclosures.

### Tax litigation

The principal focus of our tax litigation activity in 2003–04 has been on alleged tax avoidance with action taken against two of the largest alleged tax avoidance schemes. These are currently before the courts, therefore we are unable to provide further comment.

