



## Tax disputes process under review

New Zealand's tax laws can be complex, and it's inevitable that people will interpret provisions differently from time to time. Inland Revenue, NZICA and representatives of the New Zealand Law Society have been working on ways to improve the disputes process when disagreements occur.

**If Inland** Revenue or taxpayers disagree, the provisions of the *disputes resolution and challenge procedures* ("disputes process") in Parts IVA and VIIIA of the Tax Administration Act 1994 must be followed. The disputes process was added to the Act in 1996 to help resolve tax disputes quickly and cost-effectively.

In August 2008, the New Zealand Institute of Chartered Accountants (NZICA) and the New Zealand Law Society (NZLS) sent a joint submission to the Minister of Revenue requesting a review of the disputes process.

The main concerns raised were costs and time-delays. NZICA and NZLS said some taxpayers with a legitimate dispute were walking away part way through the process because they couldn't afford to carry on to the end.

Inland Revenue responded by beginning an internal review of the process, and has been working closely with NZICA and NZLS ever since. NZLS is represented by Casey Plunket from Chapman Tripp, and barristers Joanne Dunne and Geoff Clews, while NZICA's representatives are Geof Nightingale (PwC), Craig Macalister, and Aylton Jamieson.

Regular meetings chaired by Casey Plunket were held last year to analyse the issues. After further discussions internally, Inland Revenue produced a report proposing several administrative and legislative changes.

According to NZICA's Craig Macalister, the consultation process has gone quite well. "The disputes and challenge procedures are simply not working as they should. However, Inland Revenue accepts that changes are needed, and we're pleased offi-

cially have been willing to work with us to resolve the issues identified."

Joanne Dunne says: "It is unprecedented for the Tax Committees of NZICA and NZLS to work together on proposals for change in the way we have with the joint submission. This highlights the level of concern we have that the disputes process is simply not working as it should."

Inland Revenue Assurance Manager Martin Scott acknowledges the time commitment from NZICA and NZLS. "There were about 22 hours spent in meetings. The input we received was invaluable, and much appreciated. Our staff and the two societies have interacted very positively."

All three parties found they agreed on many of the proposals in Inland Revenue's report. Agreed changes include: improvements to Inland Reve-

nue’s notices of proposed adjustment (NOPAs), conferences with a clearer purpose, and guidelines to clarify when Inland Revenue will agree that a dispute can go straight to court after the conference phase.

There are three main areas of difference: the imposition of timeframes for Inland Revenue in certain areas of the disputes process when there are no statutory time limits imposed on Inland Revenue, taxpayer opt-out of the disputes process, and small claims procedures.

**What were the key reasons driving the need for change?**

**NZICA/NZLS:** The disputes process is convoluted, slow, and expensive. Some aspects (like the evidence exclusion rule) can lead to large amounts of duplication. Increasing numbers of taxpayers are withdrawing from the disputes process because they can’t afford to follow all the steps involved. We’re concerned that some incorrect assessments are going unchallenged.

**Inland Revenue:** We acknowledge the current procedures can discourage taxpayers with legitimate disputes. Many of the concerns can best be addressed within the current legislative framework and through better administrative delivery. Key improvements identified include: better prepared NOPAs, conferences with a clearer purpose and better perception of impartiality, and a policy statement to clarify when we’ll agree to the taxpayer opting out of certain steps in the disputes process.

**How can NOPAs be improved?**

**NZICA/NZLS:** We believe Inland Revenue NOPAs should be more focussed. The quality of the legal analysis and arguments needs to improve. NOPAs should be shorter and written clearly, so non-specialists can understand them. When Inland Revenue issues a NOPA, it should be signed off by someone not involved in the investigation. NOPAs should

not be used by Inland Revenue to test the merits of technical arguments with the taxpayer or as an investigation tool. Rather, the NOPA should reflect the assessment Inland Revenue proposes to make.

**Inland Revenue:** We’re currently developing guidelines to set out more precisely the purpose of the Commissioner’s NOPA. NOPAs won’t normally exceed 30 pages in length,



**Proposed changes to small claims procedures will be up for discussion in a policy paper expected to be released this year as part of the government’s tax policy work programme**

– Inland Revenue



and in most cases they’ll be much shorter. Our legal staff will provide input earlier, and we’ll strengthen our quality reviews. We’ll only issue a NOPA once the investigation is substantially complete. That means we may need to make more use of our powers to ensure we have all the relevant information.

**What are the key changes to improve the conference phase?**

**NZICA/NZLS:** The conference is currently a recitation of both sides’ views, or the opportunity for Inland Revenue to progress an investigation. Rarely is there a serious attempt at settlement or a narrowing of the issues in dispute. In some cases, no conference occurs at all. We believe conferences should be mandatory, and have a focus on settlement. The Inland Revenue delegation should include someone with the authority to make decisions.

**Inland Revenue:** The purpose of the conference phase is to exchange information, and narrow or resolve the facts, issues, and propositions of law in dispute. We’ll be offering independent Inland Revenue facilitators at every conference. Conference facilitators will be experienced tax-technical people who have not been previously involved in the case. Their role is to get all the information on the table, help both parties understand the issues, and achieve resolution if possible.

**Should taxpayers have the right to opt out of the disputes process after the conference?**

**NZICA/NZLS:** Yes, we think so, and a law change is necessary. There is general disillusionment and disengagement with the disputes process and leaving the rules as they are now or relying upon administrative guidelines will not change that. After the NOPA, notice of response (NOR) and mandatory conference phases, both parties should have a good view of each other’s arguments and whether there is a prospect of resolving the matter. If resolution is not possible, then taxpayers should be able to decide how best to apply their resources – either by continuing with the disputes process or proceeding directly to the courts. We propose new laws for opt-out situations that would limit taxpayers to legal arguments in the statement of claim, and Inland Revenue to the legal basis for the assessment.

The courts should have the discretion to enlarge those grounds of assessment/legal arguments in special cases.

**Inland Revenue:** A law change is unnecessary. There are currently legislative provisions providing for opt-out that have seldom been used. We plan to develop and publish administrative guidelines which can be refined as required. The guidelines will allow opt-out in cases when the tax is less than \$75,000 (excluding

use of money interest [UOMI] and penalties), and in over \$75,000 cases when the case turns on facts/expert opinion, or it has substantially similar facts/issues to a case that has already been considered by the courts or Adjudication Unit. A significant number of disputes fall into these categories.

**How could Inland Revenue improve timeliness?**

**NZICA/NZLS:** Currently, there are no statutory time limits on Inland Revenue after the NOPA/NOR stage. Taxpayers have a higher UOMI burden, and if there are delays on Inland Revenue's part, the taxpayer is unable to progress the dispute further. Inland Revenue has administrative guidelines, but staff don't always keep to the timeframes. We propose a set of statutory timeframes for Inland Revenue to work to (in the same way as those imposed on taxpayers). There would be sanctions if timeframes are not met: either acceptance of the taxpayer's position or suspension of UOMI.

**Inland Revenue:** We accept our disputes documents could sometimes be issued in a timelier manner. However, a legislative approach may not provide the flexibility we need in more complex cases. This could result in frontloading work to meet timeframes, which may not enhance resolution. We plan to improve timeliness with tighter internal administrative timeframes and monitoring. After the conference phase, we'll advise the taxpayer how long it will take to issue a statement of position (SOP). Internal approval will be required for complex or precedential cases that may take longer than three months.

**Should the evidence exclusion rule be relaxed?**

**NZICA/NZLS:** The evidence exclusion rule was introduced to reduce the possibility that disputants would be taken by surprise when

the case gets to court. It states that a party can't raise arguments and facts in court, unless these arguments and facts have previously been raised at the SOP phase. The evidence exclusion rule is now redundant, as the general court processes have been reformed to ensure that this sort of ambushing can't occur. Fear of ambush has led to a "kitchen sink" approach where both parties tend to include every possible argument in their disputes documents. Relaxing the evidence exclusion rule – with the knowledge that the courts will intervene in cases of ambush – would help streamline the disputes process.

**Inland Revenue:** Inland Revenue is supportive of changing the evidence exclusion rule to a legal grounds/issues exclusion rule. We agree there's a natural incentive for both parties to provide the best evidence as early as possible. However, given the evidence exclusion rule is seen as central to the "all cards on the table" approach, further consideration and consultation will be needed.

**What changes should be made to the small claims procedures?**

**NZICA/NZLS:** The current process doesn't work. There have only been six cases taken through the small claims jurisdiction of the Taxation Review Authority (TRA) in the past 13 years. We believe this is because the current process still requires taxpayers to go through the disputes process and incur all the antecedent costs before going to the small claims jurisdiction of the TRA. In many cases, it becomes uneconomic to pursue a case, even if the taxpayer is in the right. A new small claims forum is required.

**Inland Revenue:** We believe the changes allowing Inland Revenue and taxpayers in certain circumstances to agree to go straight to court after the conference is a significant step forward in reducing costs for disputes. Further thinking is required on how the process for small sum disputes (say less than \$5,000 tax)

can be addressed. Proposed changes to small claims procedures will be up for discussion in a policy paper expected to be released this year as part of the government's tax policy work programme.

**What else could Inland Revenue do to make the disputes process go more smoothly? What could taxpayers do?**

**NZICA/NZLS:** Both parties need to have a greater focus on the settlement or resolution of disputes. Currently there's a perception that Inland Revenue staff can't settle a dispute unless the terms agree with Inland Revenue's view of the law. A statement guiding officials and taxpayers in this area is urgently needed. We also believe the test case process needs to be more flexible, to potentially reduce costs for taxpayers from duplicate or similar disputes.

**Inland Revenue:** At the moment, we're revising our standard practice statements to update them for the administrative changes to the disputes process. This will be done in close consultation with NZICA and NZLS. From our point of view, taxpayers can help the process by providing the right information before we issue a NOPA and during the conference phase. Inland Revenue can help the process with regular contact and updates with taxpayers and their agents.

**NEXT STEPS**

Martin Scott advises Inland Revenue is currently working on the agreed administrative changes. These will be implemented by 1 April this year.

"Legislative proposals will be included in a policy paper planned for release in the middle of this year as part of the government's tax policy work programme. It is hoped that legislation will be introduced towards the end of the year following the public consultation process." ■

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