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## **Tips for handling an IRD audit**

### **Introduction**

In recent years, Inland Revenue has received significant extra funding for carrying out tax investigations and audits. A few years ago property transactions were targeted, and in return IRD collected tax and penalties of many times the amount spent.

Recently IRD has been focusing on the so-called "black" economy - largely owner operated businesses without strong accounting controls, and especially where a high proportion of transactions are carried out in cash, with the opportunity for the owners or employees to take some cash away and not declare for tax.

It is difficult to disagree with the principles of this project, but we do believe that sometimes IRD staff can be overly aggressive, and not very efficient.

This article aims to provide some guidance on how to handle an IRD audit

### **IRD information gathering**

Sometimes IRD will give a clue that they may be starting an audit. This can be phrased as "information gathering", an investigation, a risk review, but whatever the contact, you should assume that an audit is likely to follow.

This is very important, as to the extent that you disclose underpaid tax, any potential penalties can be reduced by as much as 75 or 100%. However you need to take care that you are not admitting to things that are not actually true.

Any contact from IRD should be an immediate alert that you need to get professional assistance.

### **Tax years under review**

If IRD conducted such reviews in the early stage of the business, then it might help identify any problems early, and ensure any errors are fixed for the future. Unfortunately, IRD has let businesses operate for many many years without any sort of review, and is then going back into ancient history and charging huge penalties and interest.

### **Visit from IRD**

IRD will sometimes come to your premises, and this may be without any warning. You should insist that IRD staff produce their business cards and appropriate warrants.

IRD may seem very friendly, or alternatively they can be quite aggressive – seizing records, examining your cash register, separating your staff and asking them questions without your knowledge.

Either way, you should explain to IRD that you are not prepared to answer any questions unless you have professional assistance, and this needs to be at a minimum your accountant, along with someone who is an expert in handling IRD audits.

Get full contact details from each IRD person and advise that you will make a more convenient time to meet with them, and also your professional advisors.

### **IRD interviews**

Never respond to IRD questions without having your advisors present. Ask IRD to provide the questions in advance so that you have time to prepare necessary information. If they refuse to do so, your professional advisors should be able to provide you with a schedule of IRD's likely questions.

### **Providing records to IRD**

IRD may require you to provide tax and other financial records in order to help them verify your taxable income. Unfortunately IRD from time to time lose taxpayers' records. Explain to IRD that you need to retain the originals, and if IRD wants copies they should bring their own copy machine. Insist on two copies, one for IRD, and one to keep in a separate file so that you know exactly what IRD has taken.

### **Writing to IRD**

As far as possible, all your communications should be in writing. When you write to IRD, keep a record of when you wrote, and ask IRD to acknowledge receipt of your letter and provide an estimate of when they will be responding. It is quite inappropriate that currently the Commissioner of Inland Revenue will not undertake that staff will acknowledge receipt of your correspondence. However if IRD fails to acknowledge receipt within a few days, you should complain to someone further up the chain until you do get acknowledgement.

When IRD writes to you, they will generally require a reply within three or four weeks. There is no statutory basis for this timeframe, but in general I recommend that you do respond promptly. IRD is supposed to invite you to request further time if necessary, but either way you are perfectly entitled to do so.

### **Getting a response from IRD**

Given IRD imposes timeframes on you, it is reasonable to expect that they will reply within a comparable time. Indeed the Commissioner of Inland Revenue tells the Minister and the public that they reply to 95% of correspondence within three weeks and the balance within four weeks.

Unfortunately the truth is significantly different. As well as sometimes failing to even acknowledge receipt of correspondence, IRD will often take months to get around to responding. You should maintain pressure on IRD to respond within a reasonable time, and elevate matters if they fail to do so.

### **Written agreements with IRD**

At such time as IRD has managed to reach an agreement with a taxpayer, they may document it in a form called an "agreed adjustment". You need to ensure that this is only signed when there is genuine agreement.

It is also important that the form disclose all tax liabilities, including different tax types, interest that is almost always charged by IRD, and potential penalties.

For many years, IRD has tried to trick taxpayers into signing such a form without disclosing interest, and even when there is no actual agreement in place. We have been recently successful in getting the IRD to change this form so that it is clear whether it is in agreement or simply an IRD proposal. It is good to see this change, although it has taken over 15 years.

### **Professional assistance**

This can't be repeated too many times. Dealing with IRD audits is a specialist area, and often your accountant will not have the right expertise to handle this on their own. This is no criticism of accountants in general – it is no different from your doctor seeing you to a specialist when you have a brain tumour or a heart problem. The fees you pay to a professional expert will benefit you many many times over in savings in time and stress and often significant savings in tax and penalties.