

Shortfall penalties – requirements for a “tax position” and a “tax shortfall”

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IS 26/03

This interpretation statement explains the requirements for a “tax position” and “tax shortfall”, common to all the shortfall penalties provided for under ss 141A–141E of the Tax Administration Act 1994.

All legislative references are to the Tax Administration Act 1994.

REPLACES | WHAKAKAPIA

- [IS0053](#): Shortfall penalty for not taking reasonable care (October 2005) *Tax Information Bulletin* Vol 17, No 9 (November 2005)
 - [IS0055](#): Shortfall penalty – Unacceptable interpretation and unacceptable tax position (April 2005) *Tax Information Bulletin* Vol 17, No 9 (November 2005)
 - [IS0060](#): Shortfall penalty for gross carelessness ((August 2004) *Tax Information Bulletin* 168-104 Vol 16, No 8 (September 2004): 10
 - [IS0061](#): Shortfall penalty for abusive tax position (December 2005) *Tax Information Bulletin* Vol 18, No 1 (February 2006)
 - [IS0062](#): Shortfall penalty – evasion (November 2006) *Tax Information Bulletin* Vol 18, No 11 (December 2006)
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Key terms | Kīanga tau tāpua

Tax position	A position or approach regarding tax under a tax law.
Tax shortfall	The difference between the tax effect of the taxpayer’s tax position for the return period and the correct tax position for that period.
Taxpayer’s total tax figure	The amount shown in the taxpayer’s tax return as tax paid or payable (before any group offset election or subvention payment), a net loss (treated as having a positive value multiplied by the basic rate of income tax for companies) or a refund.

Introduction | Whakataki

1. A shortfall penalty may apply where a taxpayer has taken a “tax position” and a “tax shortfall” arises, and the legal test for the relevant penalty is met.¹
2. This item explains the “tax position” and “tax shortfall” requirements.
3. This item should be read alongside the following items, as relevant in the circumstances, which discuss the legal tests for the various types of shortfall penalties:²
 - **IS 26/04: Shortfall penalty for not taking reasonable care**
 - **IS 26/05: Shortfall penalty for unacceptable tax position**
 - **IS 26/06: Shortfall penalty for gross carelessness**
 - **IS 26/07: Shortfall penalty for taking an abusive tax position**
 - **IS 26/08: Shortfall penalty for evasion or a similar act**
4. This item should also be read alongside **IS 26/09: Shortfall penalties – reductions and other matters**, which explains other matters relevant to shortfall penalties. The other matters include when the amount of certain shortfall penalties may be capped at \$50,000, when a shortfall penalty is reduced (or increased), what happens when a taxpayer could be liable for more than one penalty, and the assessment, payment and disputing of shortfall penalties.
5. The flowchart at Figure 1 | Hoahoa 1 shows how the “tax position” and “tax shortfall” requirements apply.

Summary | Whakarāpopoto

6. In summary, this interpretation statement explains the “tax position” and “tax shortfall” requirements for all the shortfall penalties as follows.

The taxpayer has taken a tax position

7. A “tax position” is a position or approach regarding tax under a tax law.³

¹ Sections 3 and 141A-141E.

² Sections 141A-141E.

³ Section 3.

8. Shortfall penalties can be imposed on tax positions taken in respect of the following tax types:
 - Income tax;
 - Except in the case of a shortfall penalty for taking an unacceptable tax position:
 - Withholding-type taxes such as PAYE, FBT, and RWT;
 - GST;⁴
 - Tax credits such as working for families tax credits; and
 - Employer obligations under the Child Support Act 1991 and the Student Loan Scheme Act 2001.
9. **An unacceptable tax position shortfall penalty does not apply to tax positions relating to GST. The unacceptable tax position shortfall penalty applies only to tax positions relating to income tax** (excluding withholding-type taxes such as PAYE, FBT, and RWT) and, beginning 1 January 2027, multinational top-up tax.⁵
10. A tax position can be taken in a tax return. A “tax return” includes the pre-populated account of an individual’s income held by Inland Revenue when finalised.⁶

Tax shortfall

11. A tax shortfall arises when the taxpayer’s tax position is not correct and results in too little tax to pay or overstates a tax benefit, credit or advantage.⁷ Generally, the tax shortfall is the difference between the tax effect of the taxpayer’s tax position for the return period and the correct tax position for the period.
12. **For an unacceptable tax position shortfall penalty to apply, the tax shortfall must be more than both of:**
 - **\$50,000; and**
 - **1% of the total tax figure for the relevant return period.**

⁴ Although a tax position may be taken in relation to GST, an unacceptable tax position shortfall penalty does not apply to tax positions relating to GST (see [9]).

⁵ Section 141B(2) and s 154 of the Taxation (Annual Rates For 2023–24, Multinational Tax, And Remedial Matters) Act 2024.

⁶ Section 3.

⁷ Section 3.

⁸ Section 141B(2).

Legislation

13. Section 3(1) defines “tax position” as follows:

tax position means a position or approach with regard to tax under 1 or more tax laws, including without limitation a position or approach with regard to—

- (a) a liability for an amount of tax, or the payment of an amount of tax:
- (b) an obligation to deduct or withhold an amount of tax, or the deduction or withholding of an amount of tax:
- (c) a right to a tax refund, or to claim or not to claim a tax refund:
- (d) a right to a credit of tax, or to claim or not to claim a credit of tax:
- (e) the provision of a tax return, or the non-provision of a tax return:
- (f) the derivation of an amount of income or exempt income or a capital gain, or the inclusion or non-inclusion of an amount in income:
- (g) the incurring of an amount of expenditure or loss, or the allowing or denying as a deduction of an amount of expenditure or loss:
- (h) the availability of a tax loss component or loss balance, or the use of a tax loss component or loss balance:
- (i) the attaching of a credit of tax, or the receipt of or lack of entitlement to receive a credit of tax:
- (j) the balance of a tax account or memorandum account of any type or description, or a debit or credit to such an account:
- (k) the estimation of the provisional tax payable:
- (kb) the use of the AIM method for provisional tax and the software product of an approved AIM provider:
- (l) whether the taxpayer must provide information to the Commissioner on the income other than reportable income that they derive for a tax year:
- (m) the application of Part 3, subpart 3B:
- (n) a right to a tax credit (1B)

14. Section 3 defines “tax shortfall” as follows:⁹

⁹ Section 3(1). Paragraph (b) of the “tax shortfall” definition relating to employee share schemes is set out and explained at [37].

tax shortfall, for a return period, means—

- (a) the difference between the tax effect of a taxpayer's tax position for the return period and the correct tax position for that period, when the taxpayer's tax position—
 - (i) results in too little tax paid or payable by the taxpayer or another person:
 - (ii) overstates a tax benefit, credit, or advantage of any type or description whatever by or benefiting the taxpayer or another person; but
- (b) for a person that has taken a tax position for section 23K (the **tax position**) and has not made an election under section RD 7B of the Income Tax Act 2007, the amount of tax that they would have been liable to pay, if they had made an election under section RD 7B of that Act for the period, for the difference between the tax position and the correct tax position

Analysis | Tātari

Taxpayer must have taken a tax position

15. A tax position is widely defined as a position or approach regarding tax under a tax law.¹⁰ "Tax law" includes provisions of "Inland Revenue Acts" and Orders in Council or regulations made under tax laws.¹¹ "Tax" includes, among other things, GST and income tax and tax credits such as a Working for Families tax credit.¹² "Income tax" includes withholding-type taxes such as PAYE, FBT, and RWT.¹³
16. "Tax" also includes certain amounts payable to the Commissioner under the Child Support Act 1991, the KiwiSaver Act 2006, and the Student Loan Scheme Act 2011. Section 3(1) provides:

tax—

- (a) means—
 - (i) a tax, levy, or duty of any type imposed by a tax law, regardless of how the tax, levy, or duty is described:

¹⁰ See [12].

¹¹ Section 3(1). Inland Revenue Acts are listed in sch 1.

¹² Section 3(1). Although a tax position may be taken in relation to GST, an unacceptable tax position shortfall penalty does not apply to tax positions relating to GST (see [9]).

¹³ Section RA 2 of the Income Tax Act 2007.

- (ii) an amount deemed by a tax law to be a tax, levy, or duty:
- (iii) any other amount payable to the Commissioner under a tax law, including:
 - ...
 - (C) an amount payable by a payer (as defined in section 153 of the Child Support Act 1991) under Part 10 of the Child Support Act 1991:
 - (CB) an amount required to be deducted under subpart 1 of Part 3 of the KiwiSaver Act 2006:
 - (CC) KiwiSaver Act 2006 employer contributions:
 - (CD) an amount of compulsory employer contributions unpaid, specified in a notice under section 141(5) of the KiwiSaver Act 2006:
 - (D) a salary or wage deduction (as defined in section 4(1) of the Student Loan Scheme Act 2011), or an amount recovered in accordance with section 193 of that Act:
- (iv) a credit of tax under a tax law:
- (v) a tax of the general character described in any of paragraphs (i) to (iv)—
 - (A) that is imposed on or payable by a taxpayer in a country or territory other than New Zealand; or
 - (B) that is relevant under a tax law for the purposes of determining a tax position:
- ...

17. However, tax does **not** include financial support under the Child Support Act 1991 or repayment obligations under the Student Loan Scheme Act 2011.¹⁴ That is, tax includes only amounts an employer is required to withhold and pay to Inland Revenue under the Child Support Act 1991 and the Student Loan Scheme Act 2011.
18. Accordingly, except for a shortfall penalty for taking an unacceptable tax position, shortfall penalties can be imposed on tax positions relating to the following tax types:
- Income tax, including withholding-type taxes such as PAYE, FBT, and RWT;¹⁵
 - GST;¹⁶

¹⁴ Section 3(1) definition of “tax” at para (a)(ix) and (x).

¹⁵ Section RA 2 of the Income Tax Act 2007.

¹⁶ Although a tax position may be taken in relation to GST, an unacceptable tax position shortfall penalty does not apply to tax positions relating to GST (see [18]).

- Tax credits such as a Working for Families tax credit;¹⁷
 - Child support payments but **not** financial support under the Child Support Act 1991 (that is, only amounts an employer is required to withhold and pay to Inland Revenue);¹⁸
 - Student loan deductions but **not** repayment obligations under the Student Loan Scheme Act 2011 (that is, only amounts an employer is required to withhold and pay to Inland Revenue); and¹⁹
 - KiwiSaver employee deductions.
19. An unacceptable tax position shortfall penalty does not apply to tax positions relating to GST. Shortfall penalties for taking an unacceptable tax position can only be imposed on tax positions relating to income tax (excluding withholding-type taxes such as PAYE, FBT, and RWT) and, beginning 1 January 2027, multinational top-up tax.²⁰
20. A taxpayer can take a tax position knowingly, intentionally or involuntarily by:²¹
- claiming or not claiming, or returning or not returning, a tax position; or
 - being placed in a tax position.
21. A taxpayer may be placed in a tax position when something is done on their behalf by another party. For example:
- a taxpayer may be placed in a tax position by someone acting as their agent;²²
 - a beneficiary may be placed in a tax position by a trustee of a trust;
 - a partner in a partnership may be placed in a tax position by other partners;
 - an employee may be placed in a tax position by their employer in relation to PAYE deductions; and

¹⁷ Section 3(1).

¹⁸ Penalties for non-compliance by liable parents are covered by the Child Support Act 1991.

¹⁹ Penalties for non-compliance by student loan borrowers are covered by the Student Loan Scheme Act 2011. As student loan repayment obligations are calculated based on the borrower's income for tax purposes, where an income tax shortfall exists, it is likely there will also be a repayment obligation shortfall under the Student Loan Scheme Act 2011. If a shortfall penalty is imposed on the income tax shortfall under any of ss 141A-141E, a student loan shortfall penalty may also be imposed on the student loan repayment obligation shortfall under the Student Loan Scheme Act 2011 (ss 158 and 159 of the Student Loan Scheme Act 2011).

²⁰ Section 141B(2) and s 154 of the Taxation (Annual Rates For 2023–24, Multinational Tax, And Remedial Matters) Act 2024.

²¹ Section 4A(1)(b). See also *Chapman v CIR* (2002) 20 NZTC 17,950 (HC) at [35] and [43].

²² *Case Z14* (2009) 24 NZTC 14,165.

- a bank customer may be placed in a tax position by their bank in relation to the rate of withholding tax deducted.

22. A tax position may be taken in a tax return or an individual's final account that is treated as a tax return or in respect of a due date. The definition of "taxpayer's tax position" states:²³

Taxpayer's tax position means—

- (a) a tax position taken by a taxpayer in or in respect of—
 - (i) a tax return; or
 - (ii) an individual's final account that is treated under section 22I(1)(a) as a return of income; or
 - (iii) a due date

23. A "tax return" is a form or document a taxpayer is required to complete and return to the Commissioner. It includes the "pre-populated account" of an individual's income held by Inland Revenue when finalised.²⁴ A "pre-populated account" includes an individual's "reportable income", which is income Inland Revenue receives regular information about such as PAYE income and resident and non-resident passive income, and any other income the Commissioner considers the individual has derived for the income year.²⁵

24. A tax position in a tax return or individual's final account may be taken explicitly or implicitly.²⁶

25. A "due date" is the last day on which a taxpayer can pay tax, provide a tax return or tax form, or do any other thing under a tax law before being liable for a penalty or interest.²⁷

26. A taxpayer who fails to provide a tax return by the due date is treated as having taken a tax position based on the amount of tax they have paid for the return period.²⁸

²³ Section 3(1).

²⁴ Section 22D(5) and (6).

²⁵ Section 22D(3).

²⁶ Section 4A(1)(c) and (ca).

²⁷ Section 3(1).

²⁸ See [27] for the date on which a taxpayer is treated as having taken the tax position. "Return period" is the period covered by a tax return or would be covered by a tax return if one were provided (s 3). For a return that relates to a transaction, "return period" means the time within which the transaction must be returned (s 3).

Where the return period is for an income tax year, the amount of tax paid includes any provisional tax paid for that year.²⁹ A taxpayer who has not paid any tax for the period is treated as having taken a tax position that they had no tax to pay. Section 4A(5) provides:

(5) If a taxpayer does not provide a tax return for a return period, the taxpayer is deemed, in relation to each type of tax, to take, in respect of every due date that would be covered by a tax return for the return period if a return were provided, a tax position that is based on the tax of that type paid by the taxpayer for that return period.

27. Any resulting tax shortfall is calculated by reference to the tax position the taxpayer is treated as having taken.³⁰ The meaning of tax shortfall is discussed from [34].
28. Example | Taura 1 illustrates a tax shortfall calculation where an individual has income but no return is filed and no tax is paid. The example illustrates the calculation where the individual's income is not "reportable income" and, as a variation, where the individual has "reportable income" and other income. Example | Taura 2 illustrates a tax shortfall calculation in a situation where a company has income and pays provisional tax but no return is filed.

²⁹ Sections LA 6(1)(b) and LB 2 of the Income Tax Act 2007.

³⁰ Section 4A(5) and [24].

Example | Taura 1 – Tax shortfall calculation where no return filed and no tax is paid

Facts

A self-employed individual received \$55,000 income for lawnmowing and yard maintenance work during the 2024 income year, and no other income. The individual did not file a tax return for the year or pay any tax on the income. The individual is deemed to take a tax position that they had no income and no income tax to pay.³¹ The individual's tax position is not correct. The Commissioner issued a default assessment showing the correct tax position, that is \$55,000 taxable income.

Tax shortfall calculation

The tax shortfall is the difference between the tax effect of the individual's deemed tax position (that they have no taxable income) and the correct tax position (that the individual has \$55,000 of taxable income). The tax shortfall is calculated using the individual's marginal rates of tax. The marginal rates for the 2024 income year are:

Taxable income	Tax rate
\$0–14,000	10.50%
\$14,001–48,000	17.50%
\$48,001–\$70,000	30.00%
\$70,001–\$180,000	33.00%
\$180,000 upwards	39.00%

The tax shortfall is \$9,520.00, calculated as follows:

Income		Tax rate		
\$14,000	x	10.50%	=	\$1,470.00
\$34,000	x	17.50%	=	\$5,950.00
\$7,000	x	30.00%	=	\$2,100.00
\$55,000				\$9,520.00

³¹ See s 4A(5) and [24].

Variation

In addition to the \$55,000 income from lawnmowing and yard maintenance work, the individual received \$40,000 PAYE income. The individual took a tax position when their pre-populated account was finalised that \$40,000 was their only income. The Commissioner corrects the individual's income tax assessment to include the extra \$55,000 income from lawnmowing and yard maintenance work by way of an agreed adjustment. The tax shortfall is the difference between the tax effect of the individual's tax position (that they had \$40,000 PAYE income) and the correct tax position (that they had \$40,000 PAYE income and \$55,000 from lawnmowing and yard maintenance work).

Tax shortfall calculation

The tax shortfall would be \$16,250, calculated as follows:

Income		Tax rate		
\$8,000	x	17.50%	=	\$1,400.00
\$22,000	x	30.00%	=	\$6,600.00
\$25,000	x	33.00%	=	\$8,250.00
\$55,000				\$16,250.00

Example | Taura 2 – Tax shortfall calculation where provisional tax paid but no return filed

Facts

A company received net income of \$75,000 from its equipment hire business during the 2024 income year. The company paid provisional tax of \$21,000 income tax ($\$75,000 \times 28\%$) in three instalments for the 2024 income year but failed to file a tax return by the due date. The company is deemed to have taken a tax position based on the income tax paid by way of provisional tax payments, that is, \$21,000.³² This is the correct tax position. In the absence of a return, the Commissioner issues a default assessment showing \$75,000 income and \$21,000 tax to pay.

Tax shortfall calculation

As there is no difference between the tax effect of the company's deemed tax position (\$21,000 tax on \$75,000) and the correct tax position (\$21,000 tax on \$75,000), there is no tax shortfall.

29. A taxpayer who files a tax return takes a tax position on the date they file the return.³³ If the taxpayer's tax position is incorrect, any tax shortfall arises on that date. This is the outcome even if the tax position is later corrected and the correct amount of tax paid before the due date.³⁴ The tax shortfall is calculated based on the taxpayer's original tax position. In some cases, the amount of any shortfall penalty may be reduced if the tax shortfall is voluntarily disclosed.³⁵
30. A taxpayer who fails to provide a tax return is treated as having taken a tax position on the due date for payment of the tax covered by the return.³⁶

³² Section 4A(5), see [24]. The company would also be liable to a late filing penalty under s 139A for not completing and filing a tax return.

³³ See ss 33 and 92 for income tax and ss 16 and 92B of the Goods and Services Tax Act 1985 for GST. See also *Ben Nevis Forestry Ventures Ltd v CIR*; *Accent Management Ltd v CIR* [2008] NZSC 115, (2009) 24 NZTC 23,188, at [176].

³⁴ Example | Taura 3 illustrates a tax shortfall calculation in a situation where a tax position is corrected before the due date for payment of the tax. Some taxpayers attempt to correct an incorrect tax position by filing what are often referred to as "amended returns". However, the Act does not make any provision for amended returns (*CIR v FB Duvall Ltd* (2005) 22 NZTC 19,142 (HC)). For example, a taxpayer assesses their income tax on the date they file their income tax return (ss 33 and 92). If a taxpayer subsequently considers their income tax return is incorrect, they may propose an adjustment to their assessment by issuing a Notice of Proposed Adjustment or request the Commissioner to amend their assessment (ss 89DA and 113 and see SPS 20/03: Requests to amend assessments *Tax Information Bulletin* Vol 32, No 6 (July 2020): 11). The Act also makes provision for the correcting of minor errors in income tax, GST, and FBT in the next return that is due (s 113A).

31. Individuals who have derived reportable income **and** other income are treated as having taken a tax position when their pre-populated account is finalised.³⁷ Generally, a pre-populated account is finalised when the individual confirms the information in the account is correct and complete or when Inland Revenue is satisfied the information is correct and complete.³⁸ Before an account is finalised, an individual can amend the information in it without taking a tax position.
32. The position is different for individuals who have derived **only** reportable income.³⁹ Such individuals may amend the information in their finalised account at any time before their terminal tax date for the year. In that case, the amended information becomes the individual's tax position. The earlier tax position taken when the individual's account was first finalised is regarded as not having been made.⁴⁰
33. A default assessment may be issued if the Commissioner is not satisfied the information in an individual's pre-populated account is complete and correct.⁴¹ In that case, the individual takes a tax position based on the information in their account after the date by which they must have adjusted or corrected their account. For individuals deriving only reportable income, this is their terminal tax date for the year.⁴² For other individuals, this is 7 July of the year following the tax year or later if the individual has an extension of time to file a return.⁴³ The tax shortfall will be calculated based on the difference between the tax position the individual takes based on the information in their pre-populated account and the tax position in the Commissioner's default assessment.

³⁵ The voluntary disclosure of tax shortfalls is considered in IS 26/09: Shortfall penalties – other matters.

³⁶ Section 4A(5) and see [24].

³⁷ An individual makes a return of income and assesses their income tax liability on that date (ss 22H, 22I(1)(c) and (2), and 92(2B)). "Reportable income" is explained in [21].

³⁸ Section 22H.

³⁹ An individual who derives only reportable income is a "qualifying individual", see s 22D(2) and (3).

⁴⁰ Sections 22D and 22G(3).

⁴¹ Sections 22G(4) and 106.

⁴² Section 22G(3).

⁴³ Section 22H(4) and the s 3(1) definition of "tax position", para (l).

Tax position results in a tax shortfall

34. A tax shortfall arises when the taxpayer's tax position is not correct and results in too little tax to pay or overstates a tax benefit, credit or advantage.⁴⁴
35. A "tax shortfall" is the difference between the tax effect of the taxpayer's tax position for the return period and the correct tax position for the period, when the tax position results in too little tax paid or overstates a tax benefit, credit, or advantage.⁴⁵
36. The tax effect of a tax position is calculated using:⁴⁶
 - the taxpayer's marginal tax rate or tax rates during the return period; or
 - where the taxpayer has no tax to pay, the tax rate or lowest marginal tax rate that would apply to the taxpayer during the return period if they had tax to pay.
37. The "correct tax position" for a period is the "correct tax position established under 1 or more tax laws".⁴⁷
38. The difference between the tax effect of the taxpayer's tax position and the tax effect of the correct tax position is the "tax difference, in monetary terms, for the taxpayer between the two positions".⁴⁸
39. Specific provision is made for the calculation of a tax shortfall where an employer has understated the value of a benefit provided to an employee under an employee share scheme and has not elected to withhold and pay tax for the benefit. In that case, the tax shortfall is the tax the employer would have been liable to pay for the difference in value if they had made the election.⁴⁹ The following examples illustrate tax shortfall calculations in situations where a tax position is corrected before the due date for payment of the tax, where a taxpayer's taxable income is increased, where a claimed loss is reduced, and where a claimed loss is extinguished.

⁴⁴ An incorrect tax position overstating the amount of a loss a taxpayer is entitled to may not result in too little tax to pay. However, the incorrect tax position overstates a tax benefit or advantage, *Case 4/2017* [2017] NZTRA 04, (2017) 28 NZTC 4-003, at [69] and example 5.

⁴⁵ Section 3(1), "tax shortfall" (see [13]).

⁴⁶ Section 141(12).

⁴⁷ Section 3(1).

⁴⁸ *Accent Management Ltd v CIR* (2007) 23 NZTC 21,323 (CA).

⁴⁹ Paragraph (b) of the definition of "tax shortfall" in s 3 (see [13]).

Example | Tauria 3 – Tax shortfall where tax position later corrected

Facts

A company filed a GST return for the period ended 31 January 2024 on 15 February 2024 showing \$106,500 output tax, \$87,700 input tax and \$18,800 GST to pay. The company paid the \$18,800 GST the same day.

The senior employee responsible for the preparation and filing of the company's GST returns had delegated the task of preparing and filing the GST return to a new inexperienced employee and did not check the correctness of the return before it was filed.

On 20 February 2024, the senior employee discovered an error in the GST return. Due to their inexperience, the new employee had overlooked including \$12,000 of sales and income on which GST output tax of \$1,565.21 was payable. Also on 20 February 2024, the company made a request in myIR for the Commissioner to amend its return and paid the extra GST.

Tax shortfall calculation

There was a tax shortfall despite the company making a request for the Commissioner to amend its return and paying the extra GST before the due date for returning and paying the tax (28 February 2024).

The tax shortfall is the difference between the tax effect of the tax position the company took on 15 February 2024 when it filed its GST return (GST payable of \$18,800, which excluded the GST output tax of \$1,565.12) and the correct tax position (\$20,365.21). The tax shortfall is \$1,565.21.

Example | Tauria 4 – Tax shortfall calculation where taxable income is increased

Facts

A company filed its 2024 income tax return showing \$150,000 taxable income. In its tax return, the company took a tax position that \$100,000 it received on the sale of a property was a capital receipt and not income. When reviewing the company's income tax return, Inland Revenue discovered the \$100,000 receipt was income and the taxpayer's tax position was not correct.

Tax shortfall calculation

The tax shortfall is the difference between the tax effect of the company's tax position (that the \$100,000 is not income) and the correct tax position (that the \$100,000 is income).

The tax shortfall is \$28,000, calculated using the company tax rate of 28% ($\$100,000 \times 28\%$).

Example | Taura 5 – Tax shortfall calculation where claimed loss is reduced

Facts

An individual filed their 2024 income tax return showing a \$65,000 loss for the year. In their tax return, the individual took a tax position that a \$50,000 distribution from a trust they received during the year was not income. When reviewing the individual's income tax return, Inland Revenue discovered the \$50,000 receipt was income and corrected the individual's tax position by way of agreed adjustment. After adjustment, the claimed loss is reduced to \$15,000.

Tax shortfall calculation

The tax shortfall is the difference between the tax effect of the individual's tax position (that the \$50,000 is not income) and the correct tax position (that the \$50,000 is income). As the individual has no tax to pay (their loss is reduced but not extinguished), the tax effect of the individual's tax position is calculated using the lowest marginal tax rate that would apply if the individual had tax to pay, that is, 10.5% for the 2024 income year.⁵⁰

The tax shortfall is \$5,250 ($\$50,000 \times 10.5\%$).

Example | Taura 6 – Tax shortfall calculation where claimed loss is extinguished

Facts

An individual filed their 2025 income tax return showing a \$10,000 loss for year. In their tax return, the individual took a tax position that they were entitled to a \$30,000 deduction for a revenue expense. When reviewing the individual's income tax return,

⁵⁰ Section 141(12) and Part A of sch 1 of the Income Tax Act 2007.

Inland Revenue discovered the \$30,000 expense was not deductible. The correct tax position is that the expense is capital in nature and not deductible. Consequently, the individual had understated their income by \$30,000. After adjustment, the claimed loss of \$10,000 is extinguished, and the individual has \$20,000 taxable income.

Tax shortfall calculation

The tax shortfall is calculated based on the \$30,000 difference between the individual's tax position and the correct tax position using the individuals marginal rates of tax.

The relevant marginal rates for the 2025 income year are:

Taxable income	Tax rate
\$0–14,000	10.50%
\$14,001–15,600	12.82%
\$15,601–48,000	17.50%

The tax shortfall is \$4,195.12, calculated as follows:

Income	Tax rate			
\$14,000	x	10.50%	=	\$1,470.00
\$1,600	x	12.82%	=	\$205.12
\$14,400	x	17.50%	=	\$2,520.00
\$30,000				\$4,195.12

40. A taxpayer's tax return for a return period may include multiple tax positions. If more than one of the tax positions is incorrect, a separate tax shortfall calculation is required for each incorrect tax position. If a taxpayer takes the same incorrect tax position in more than one return period, a separate tax shortfall calculation is required for each return period and for each tax position.⁵¹
41. If, in the same return period, a taxpayer is liable to pay one or more shortfall penalties in respect of the same tax type and the taxpayer's liability to the tax is overstated in one or more respects, the tax shortfall is calculated by setting off the tax effects of the overstatements:⁵²
 - against the understatement, in the case of one tax shortfall; or

⁵¹ Section 141(3).

⁵² Section 141(5).

- prorated against the understatements, in the case of more than one tax shortfall.
42. The Commissioner may offset credit adjustments against debit adjustments for the purpose of calculating shortfall penalties. This includes offsetting between different tax types, periods, and associated taxpayers.⁵³
 43. If, in the same return period, a taxpayer has a tax shortfall in respect of one tax type and refund in respect of different tax type, the Commissioner may reduce the tax shortfall by the amount of the refund.⁵⁴ The tax shortfall must have arisen as a result of an adjustment made by the Commissioner. The tax refund must have resulted from an adjustment made by the Commissioner as a consequence of the adjustment giving rise to the tax shortfall. If the 2 tax types have different return periods, the Commissioner may, for the purpose of determining a tax shortfall, treat the return periods as the same return period.⁵⁵
 44. The Commissioner may also reduce a taxpayer's tax shortfall by the amount of a tax refund an associated person is entitled to or reduction in the tax they must pay. The tax shortfall and refund or reduction must relate to the same tax type and return period, must have resulted from adjustments made by the Commissioner, and the adjustments resulting in the refund or reduction must be linked to the adjustment resulting in the tax shortfall.⁵⁶
 45. The Commissioner may make the offset if the taxpayer and associated person have different return period. This is if the taxpayer's return period overlaps the associated person's return period and the taxpayer's tax position is not an abusive tax position and does not involve evasion or similar act.⁵⁷
 46. Generally, in calculating tax shortfalls, the Commissioner will make these offsets unless there is good reason not to, such as where taxpayers have deliberately sought to avoid meeting their tax obligations.
 47. Tax shortfalls arising from tax positions taken in the same return period can be aggregated if the tax positions are similar or identical and relate to similar or identical arrangements, articles, items or matters.⁵⁸

⁵³ Section 141(6)-141(9).

⁵⁴ Section 141(6).

⁵⁵ Section 141(9).

⁵⁶ Section 141(7).

⁵⁷ Section 141(7B).

⁵⁸ Section 141(10).

48. The following examples illustrate when overstatements of tax are offset against understatements when calculating tax shortfalls.

Example | Taura 7 – Same taxpayer, same tax types and same return periods

Facts

A company is liable for a shortfall penalty for gross carelessness for an incorrect tax position it took in its income tax return for the 2025 income year. The incorrect tax position resulted in the company's sales income being understated by \$100,000. The company's income for the 2025 income year was also overstated by \$10,000 as the company mistakenly returned a non-taxable capital amount as income. The company returned \$160,000 income for the 2025 income year. The correct tax position is that the company had \$250,000 income for the 2025 income year.

Tax shortfall calculation

The tax shortfall is calculated by offsetting the tax effect the understated income against the tax effect of the overstated income:⁵⁹

$$\begin{aligned} & \text{tax effect of understated income} - \text{tax effect of overstated} \\ & \text{income} \\ & = \$28,000 (\$100,000 \times 28\%) - \$2,800 (\$10,000 \times 28\%) \\ & = \$25,200 \end{aligned}$$

Example | Taura 8 – Same taxpayer, different tax types and different return periods

Facts

During an audit, Inland Revenue discovers that a GST registered company has incorrectly claimed a \$1,304.35 input tax deduction for \$10,000 salary and wages paid to employees in its GST return for the period ended 31 March 2025. The error occurred due to a genuine misunderstanding about what should be included in a GST return. There is no evidence the company claimed the input tax deduction knowing it was not entitled to it.

⁵⁹ Section 141(5).

Due to the same misunderstanding, the company included the salary and wages expense in its income tax return for the year ended 31 March 2025 using an amount adjusted for GST (that is, \$8,695.65). Consequently, the company's income for the 2025 income year was overstated by the amount of GST not included in the salary and wage expense (that is, \$1,304.35).

Inland Revenue proposes adjustments to the company's GST assessment for the period ended 31 March 2025 to reverse the incorrect input tax deduction and to the company's 31 March 2025 income tax assessment to increase the amount of the salary and wage expense. The company agrees. After the adjustments, there is a GST tax shortfall of \$1,304.35 and the company is entitled to an income tax refund of \$365.22 (28% of \$1,304.35).

Tax shortfall calculation

Inland Revenue decides to treat the \$365.22 income tax refund as GST paid by the company for the period ended 31 March 2025. This is because the GST tax shortfall arose due to a genuine error made the taxpayer, not deliberate non-compliance. Also, although the income tax and GST return periods are different, Inland Revenue decides to treat the return periods as being the same.⁶⁰ Consequently, the company's GST tax shortfall is reduced to \$939.13.⁶¹

⁶⁰ Section 141(9).

⁶¹ Sections 141(6) and (9).

Example | Taura 9 – Associated persons, same tax type and return periods, and Commissioner adjustments

Facts

Company A and company B are associated.⁶² They have identical shareholders, directors, and GST registrations and share offices. In June 2025, company A purchased a fishing vessel from a non-resident, non-GST registered, vendor for \$1.8 million and imported it into New Zealand. Due to confusion in their shared offices, company B claimed a \$234,782.60 input tax deduction in its GST return for the 2-month period ended 31 July 2025 for the GST collected by New Zealand Customs at the border when the vessel was imported. Inland Revenue reviewed company B's GST assessment for the period and discovered the error. The Commissioner corrected each company's GST assessment for the 2-month period ended 31 July 2025 by way of agreed adjustments. After the adjustments, company B has a \$234,782.60 GST tax shortfall for the 2-month period ended 31 July 2025 and company A is entitled to a \$234,782.60 GST refund.

Tax shortfall calculation

The Commissioner exercises discretion to treat the GST refund owing to company A in the 2-month period ended 31 July 2025 as GST paid by company B in that period. This is because the companies share the same GST return period and there was a genuine error and no evidence of any deliberate non-compliance on the part of either company. Consequently, company B has no GST tax shortfall in the 2-month period ended 31 July 2025.⁶³

Example | Taura 10 –Associated persons, same tax type and return period, but no Commissioner adjustment

Facts

A married couple are the trustees of a family trust and the partners of a partnership through which they operate an orchard business. The partnership and the trust are associated for GST purposes.⁶⁴

⁶² Section 3(2) and s YB 2 of the Income Tax Act 2007.

⁶³ Section 141(7).

⁶⁴ Section 3(2) and ss YB 4, YB 12, and YB 14 of the Income Tax Act 2007.

The trust is not GST registered, but the partnership is, with a 2-month GST period. In February 2025, the trust purchases an item of plant for the packing shed for \$1 million (including GST). Through a misunderstanding about the transaction, the partnership claims a \$130,434.78 input tax deduction for the purchase in its GST return ending 31 March 2025.

When reviewing the partnership's GST return, Inland Revenue discovers the partnership is not entitled to the input tax deduction for the plant purchased by the trust. Inland Revenue proposes an adjustment reversing the deduction. The partners agree to the adjustment. After the adjustment, the partnership has a \$130,434.78 GST tax shortfall.

The trust then applies for GST registration. The Commissioner accepts the trust's application and registers the trust for GST from 1 February 2025 with a 2-month GST period. The trust claims an input tax deduction relating to the purchase of the plant in the GST period ended 31 March 2025 and is entitled to a \$130,434.78 GST refund.

Tax shortfall calculation

In calculating the partnership's tax shortfall, the trust's GST refund cannot be offset against the partnership's GST tax shortfall. To be offset, the trust's GST refund must have resulted from an adjustment made by the Commissioner and no such adjustment was made when the trust filed its GST return.⁶⁵ For shortfall penalty purposes, the partnership's GST tax shortfall is \$130,434.78.

⁶⁵ Section 141(7).

Example | Taura 11 –Associated persons, same tax type and return period, and non-compliance

Facts

Company C and company D are associated.⁶⁶ They have identical shareholders, directors, and GST registrations. Company C purchased a supply chain software platform in the GST period ended 31 July 2025 for \$2.3 million (including GST). Company C is entitled to claim a \$300,000 input tax deduction relating to the purchase in its GST return for the period ended 31 July 2025. If company C claimed the input tax deduction, its return for the period would show a \$200,000 refund. Company C needs the refund to be able to pay its suppliers and other creditors to ease a temporary cashflow problem. However, company C has a significant amount of unpaid GST relating to previous GST periods. Company C is concerned that if it claims the input tax deduction the Commissioner will offset the refund against company C's GST arrears. Consequently, company C and company D decide that the input tax deduction should be claimed by company D in its GST return for the period ended 31 July 2025 because it does not have any outstanding GST. The Commissioner reviews company D's GST assessment for the period and discovers the error. The Commissioner corrects each company's GST assessment for the period by way of an agreed adjustment. After the adjustments, company D has a \$300,000 GST tax shortfall and company C has a \$200,000 GST refund.

Tax shortfall calculation

In calculating company D's tax shortfall, the Commissioner exercises discretion not to treat the company C's \$200,000 GST refund as GST paid by company D in the GST period ended 31 July 2025. This is because the companies deliberately claimed an input tax deduction in the wrong entity to prevent the Commissioner from using the GST refund company C would otherwise be entitled to pay its tax debt.⁶⁷ For the purpose of imposing a shortfall penalty, company D's GST tax shortfall is \$300,000.

Tax shortfall threshold for unacceptable tax position shortfall penalty

49. For a taxpayer to be liable for an unacceptable tax position shortfall penalty, the tax shortfall must exceed:⁶⁸

⁶⁶ Section 3(2) and s YB 2 of the Income Tax Act 2007.

⁶⁷ Section 141(7).

⁶⁸ Sections 141B(2) and (3).

- \$50,000; and
 - 1% of the “taxpayer’s total tax figure” for the relevant return period.
50. The taxpayer’s total tax figure is the amount shown in the taxpayer’s tax return (as filed by the taxpayer) as tax paid or payable, a net loss or a refund.⁶⁹ Where a taxpayer has paid tax or has tax to pay, the amount is the tax paid or payable before any group offset election or subvention payment.⁷⁰ Where a taxpayer has no tax to pay, the amount is equal to the net loss of the taxpayer, treated as having a positive value multiplied by the basic rate of income tax for companies.⁷¹
51. For the purpose of determining whether a tax shortfall exceeds the threshold amounts:⁷²
- a tax return provided by a partnership, look-through company or group of persons is treated as if it were a tax return of every partner in the partnership, effective look-through interest holder for the look-through company, or person in such group; and
 - the tax rate applying to a partnership or look-through company is the same as the basic rate for income tax for companies.⁷³
52. Where there is more than one tax shortfall in a return period, the threshold amounts in s 141B(2) are applied to each tax shortfall. This is except for tax shortfalls arising from similar or identical tax positions that are aggregated and deemed to be 1 tax shortfall.⁷⁴
53. Example | Taurira 12 shows how to determine whether a tax shortfall exceeds the threshold amounts where there is more than one tax shortfall in a return period.

⁶⁹ Section 141B(3).

⁷⁰ Section 141B(3)(a).

⁷¹ Section 141B(3)(b). On and after 1 January 2027, s 141B(3)(b) will not apply to multinational top-up tax (Taxation (Annual Rates for 2023–2024, Multinational Tax, and Remedial Matters) Act 2024). This is because, when multinational top-up tax applies, there will always be tax to pay. See IS 26/05 Shortfall penalty for taking an unacceptable tax position, example 4, on how to calculate 1% of the “taxpayer’s total tax figure” for the relevant return period.

⁷² Section 141B(8).

⁷³ Section 141B(8). This is except in the case of a multinational top-up tax (Taxation (Annual Rates for 2023–24, Multinational Tax, and Remedial Matters) Act 2024).

⁷⁴ Section 141(10).

Example | Taura 12 –More than one tax shortfall in a return period

Facts

The following unacceptable tax positions and tax shortfalls are identified during an audit of a company’s income tax returns for the 2021, 2022, and 2023 income years:

Unacceptable tax position	2021 tax shortfall	2022 tax shortfall	2023 tax shortfall	Total tax shortfall
Deduction claimed for a non-deductible capital expense	\$30,000	\$25,000		\$55,000
Income under-reported due to incorrect accounting procedures	\$10,000	\$30,000	\$51,000	\$91,000
Total	\$40,000	\$55,000	\$51,000	

None of the tax shortfalls are more than 1% of the company’s “total tax figure”.⁷⁵

Result

The only return period in which the s 141B(2) threshold is met is the 2023 income year. In this year, the tax shortfall relating to the under-reported income exceeds the \$50,000 threshold amount or 1% of the company’s “total tax figure”.

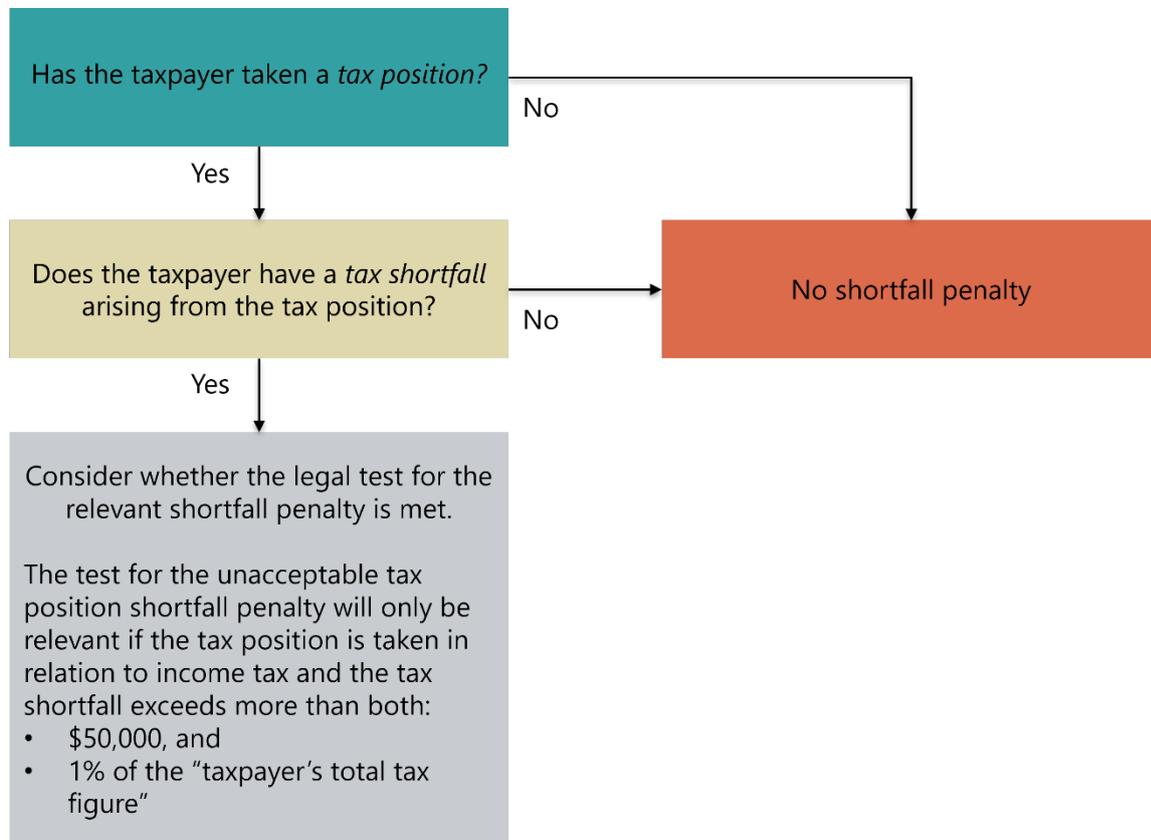
The tax shortfalls in the 2021 and 2022 income years do not exceed the s 141B(2) threshold amounts because:

- each tax shortfall is less than \$50,000 and 1% of the company’s “total tax figure”, and
- the tax shortfalls do not arise from similar or identical tax positions and cannot be aggregated and deemed to be 1 tax shortfall.

54. The following flowchart shows how the “tax position” and “tax shortfall” requirements apply.

⁷⁵ See [49].

Figure 1 | Hoahoa 1 showing how the “tax position” and “tax shortfall” requirements apply



References | Tohutoro

Legislative references | Tohutoro whakatureture

Child Support Act 1991

Goods and Services Tax Act 1985, ss 16, 92B

Income Tax Act 2007, s RA 2, sch 1 part A

Student Loan Scheme Act 2011, ss 158, 159

Tax Administration Act 1994, ss 3(1) (“tax”, “tax law”, “tax position”, “tax shortfall”, “taxpayer’s tax position”), 4A(1) and (5), 22D, 22G, 22H, 22I, 33, 89DA, 92, 113, 113A, 141, 141A to 141E, sch 1

Taxation (Annual Rates for 2023–24, Multinational Tax, and Remedial Matters) Act 2024

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Accent Management Ltd v CIR (2007) 23 NZTC 21,323 (CA)

Ben Nevis Forestry Ventures Ltd v CIR; Accent Management Ltd v CIR [2008] NZSC 115, (2009) 24 NZTC 23,188

Chapman v CIR (2002) 20 NZTC 17,950 (HC)

CIR v FB Duvall Ltd (2005) 22 NZTC 19,142 (HC)

Case 4/2017 [2017] NZTRA 04, (2017) 28 NZTC 4-003

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Other references | Tohutoro anō

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IS 26/05: Shortfall penalty for taking an unacceptable tax position

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IS 26/06: Shortfall penalty for gross carelessness

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IS 26/07: Shortfall penalty for taking an abusive tax position

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