TAX INFORMATION BULLETIN

Volume Eight, No.7 October 1996

The Taxpayer Compliance, Penalties, and Disputes Resolution Bill was introduced into Parliament in October 1995 and passed in July 1996. The compliance and penalties provisions of the legislation resulted in amendments to these Acts:

- Tax Administration Act 1994
- Income Tax Act 1994
- Goods and Services Tax Act 1985
- Stamp and Cheque Duties Act 1971
- Gaming Duties Act 1971
- Estate and Gift Duties Act 1968
- Student Loan Scheme Act 1992
- Accident Rehabilitation and Compensation Insurance Act 1992
- Child Support Act 1991

This Tax Information Bulletin deals with the legislative changes relating to compliance and penalties. The changes pertaining to the new disputes resolution procedures were addressed in TIB Volume Eight, No.3 (August 1996).

The main features of the new legislation are:

- a clear statement of taxpayer obligations
- new interest rules for overpayments and underpayments of tax
- new penalty and remission rules.

All section references in this document relate to the Tax Administration Act 1994 unless otherwise indicated.

These reforms follow on from the Government discussion documents *Taxpayer compliance, standards and penalties* (August 1994), and *Taxpayer compliance, standards and penalties 2* (April 1995).

See the inside front cover for a full list of this TIB's contents.

This TIB has no appendix

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This is an Inland Revenue service to people with an interest in New Zealand taxation.

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Background - new compliance and penalties rules

The complex job of reviewing and reforming the compliance and penalties rules began four years ago, when in the 1992 budget the Government announced its intention to launch a review and a reform of the compliance and penalties rules in the Inland Revenue Acts.

There was widespread consultation about the changes. The principles of the reforms were outlined in a discussion document issued August 1994. The Government then issued a second document in April 1995, for further consultation, which contained detailed proposals and draft legislation.

In October 1995 the Taxpayer Compliance, Penalties and Disputes Resolution Bill was introduced into Parliament. The Finance and Expenditure Committee considered the bill and submissions from various groups and individuals.

Problems with the existing rules

The current legislative scheme dates back at least to 1916, particularly in respect of income tax. Since then many major changes and new rules have been added to make up the tax system that exists today. At the same time, the nature of tax administration has changed from a system in which each taxpayer's liability was quantified using a manual process to one that is largely based on modern technology. The provisions detailing taxpayer obligations and standards of behaviour, and sanctions which enforce these have not kept pace with the changing nature of tax legislation and administration.

The current rules have a number of weaknesses which broadly relate to gaps in coverage, flaws in design and inconsistencies in application. This has resulted in several problems:

- The rules are unfair to the majority of taxpayers, who comply with the law.
- There are unnecessary costs for taxpayers, their agents and the tax administration.
- The legal processes and requirements are unclear to taxpayers.
- The rules are less effective than desirable in supporting taxpayers' obligations in a self-assessment environment.

The new provisions comprehensively address these problems.

Benefits of the new rules

The last ten years have seen major reforms in taxation and tax administration. They include:

- a significant broadening of the tax base, and associated changes in tax rates
- modernisation of tax administration
- an increasing responsibility placed on taxpayers to assess their own tax liability.

All these changes have taken place in an environment of increasing business and commercial sophistication. However, the rules relating to taxpayers' compliance obligations have never been clearly stated.

Fundamental defects in the area of sanctions have meant that taxpayers who wish to "play the system", could do so, usually without risk of loss. However, under the new rules those found to be engaged in this activity will face interest from the original due date of the tax and the prospect of significant penalties.

There will be considerable benefits from the new rules. Replacing the current ad hoc structure with a comprehensive new structure will encourage all taxpayers to comply with their obligations.

The foundation of the new rules is a clear statement of the appropriate standards that taxpayers must meet in complying with their obligations. These standards are reinforced by a comprehensive structure of penalties.

Many people regard these amendments to taxpayer obligations and tax penalties as the most important change to the tax system in many years.

Application dates of the new provisions

Revenue/provision	Application date
Income tax	1997-98 income year onwards
Withholding taxes	1997-98 income year onwards
Goods and services tax	Taxable periods starting on or after 1 April 1997
Gift duty	Dutiable gifts made on or after 1 April 1997
Stamp and cheque duty	Instruments of conveyance executed on or after 1 April 1997 Liable transactions entered into on or after 1 April 1997
Gaming duty	Races run, lotteries drawn, casino wins arising and dutiable games played on or after 1 April 1997
Accident Rehabilitation and Compensation Insurance	Employers' premium deductions from 1997-98 income year onwards
Student Loans	Employers' deductions from 1997-98 income year onwards
Child Support	Employers' deductions from 1997-98 income year onwards
Court Orders	1 October 1996
Instalment arrangements	Arrangements entered into after 1 April 1997
Penalty remissions	Remissions considered after 1 April 1997

Part 1 - Taxpayers' obligations

Introduction

The new legislation clearly sets out taxpayers' obligations for several reasons:

- to identify those obligations which have interest and/or penalty consequences if taxpayers breach them
- to complement Part II of the Tax Administration Act, which sets out the Commissioner's role and general powers
- to help set the framework for rewriting the Tax Administration Act.

The taxpayer obligations are contained in new sections 15A and 15B.

Background

A recent review of the Inland Revenue Department, chaired by Sir Ivor Richardson, identified New Zealand as operating a system of substantial self-assessment. Under such a system individuals and companies must assess their own tax liability and pay tax according to the requirements of the law.

For taxpayers to be able to satisfy the requirements placed upon them by self-assessment, they must be aware of their primary tax obligations. The new amendments clarify taxpayers' obligation to assess their tax liability and clearly spell out their responsibility to determine the correct amount payable and pay it on time.

The obligations represent the target taxpayers should be aiming for. However, in some circumstances failure to satisfy a tax obligation may not justify imposing a penalty. To reflect this, standards are introduced to define how far taxpayers are expected to go to meet their tax obligations.

Legislation

Section 15A states the purpose of the new part and Section 15B sets out taxpayers' primary obligations as follows:

- correctly determine their amount of tax payable
- deduct or withhold the correct amount of tax from payments or receipts
- pay tax on time
- keep all necessary information and maintain all necessary accounts or balances
- disclose all information that the Commissioner requires in a timely and useful way
- co-operate with the Commissioner to the extent required by the Inland Revenue Acts
- comply with other specific tax obligations.

Discussion

An obligation to comply with the Act remains with the person on whom it is imposed; it cannot be transferred to a third party even if the taxpayer contracts with a third party to meet that obligation. For example, a taxpayer who must file a tax return employs a tax agent. If the return is not filed, it is the taxpayer, and not the agent, who is liable, as the obligation is the taxpayer's.

Part 2 - Interest

Introduction

Use of money interest is not a penalty. Rather, it is intended to reduce any advantage or disadvantage when taxpayers overpay or underpay tax. Interest will be a cost imposed on taxpayers or on the Government to compensate for having the use of the other party's money over a period of time.

The principle behind use of money interest is that all taxpayers' tax payments are due on prescribed dates, and taxpayers have an obligation to pay on those applicable dates. Interest will provide an incentive to taxpayers to pay the right amount of tax at the right time by removing the timing benefit from deferring tax payments.

The interest provisions have adopted a commercial approach, together with safeguards to ensure that Inland Revenue is not used as a financing or investment vehicle.

Adopting a commercial approach to the payment of interest permits the concepts of interest and penalties to be clearly distinguished, and allows them to be applied separately. Interest charges do not imply any culpability on the part of the taxpayer. The primary objective of interest is to provide compensation.

The new interest rules apply to all taxes and duties from the 1997-98 income year onwards, as set out in the table on page 2.

Background

The Tax Simplification Consultative Committee recommended that a full two-way interest system be implemented. It considered that charging interest on underpayments or late payments of tax would give taxpayers an incentive to pay the right amount of tax at the right time by removing any timing benefits from deferrals. Paying interest on overpayments would recognise that taxpayers had lost the use of their funds

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and should be compensated, especially when large refunds are involved and the time delay is significant.

Under the present system interest is not applied consistently across revenues, and does not apply at all in some areas.

Key features

- Split interest rates will apply consistently to all taxes and duties.
- There are comprehensive interest rules for overpayments and underpayments of tax.
- Interest will generally be payable on underpaid and overpaid tax from the original date tax was due until paid or refunded.
- Interest rates will be determined on a market basis to reflect their compensation function and to encourage timely payments.
- Interest will be assessable and subject to resident withholding tax (or NRWT as appropriate).
- Interest will be deductible, subject to the usual business test.

Legislation

Interest is covered in Part VII. Section 120A states that Part VII has three purposes:

- to compensate the Commissioner for the loss of use of money through taxpayers paying too little tax
- to compensate taxpayers for the loss of use of money through their paying too much tax
- to encourage taxpayers to pay the correct amount of tax on time.

Section 120(2) provides that interest is not a penalty.

Discussion

In accordance with section 120D, interest will compensate taxpayers if they overpay tax, and the Commissioner if taxpayers underpay tax. Interest will apply simultaneously with any late payment penalty on any underpaid tax.

Currently, interest applies only to a small number of tax types and duties. The new interest rules will apply consistently to all taxes and duties.

The taxes and duties to which use of money interest will apply are as follows:

- Accident compensation premium deductions by employers (employer and earner premium)
- casino duty
- cheque duty
- Child Support deductions by employers
- credit card transaction duty
- Family Support
- dividend withholding payment accounts
- fringe benefit tax
- gaming machine duty
- gift duty
- goods and services tax
- imputation accounts
- income tax
- lottery duty
- non-resident withholding tax (on interest and dividends)
- PAYE deductions
- qualifying company election tax
- resident withholding tax (on interest and dividends)
- stamp duty
- Student Loan deductions by employers
- specified superannuation contribution withholding tax
- totalisator duty

However, interest will not apply to the following:

- Student Loan borrowers
- custodians and liable parents
- persons who fail to deduct amounts and return them to the Commissioner under section 157, section 43 of the Goods and Services Tax Act 1985, section 154 of the Child Support Act 1991 and section 46 of the Student Loan Scheme Act 1992. (These sections require third parties to make deductions from any payments made to the taxpayer and forward them to Inland Revenue.)

There have been changes to some tax and duty rules to make them consistent with use of money interest. Each is briefly discussed below.

Duties (stamp and cheque duties, gift duty and gaming duties)

Each duty previously contained a provision so that if it wasn't paid by the due date, interest at 5% per month was chargeable. This was effectively a late payment penalty, not interest. These rules have been repealed and duties will be subject to use of money interest.

Dividend withholding payment accounts

The present dividend withholding payment (DWP) interest rules have been incorporated into the new use of money interest rules. Currently, interest applies to underpayments only if late payment penalty is not imposed. From 1 April 1997 interest and late payment penalty can apply at the same time.

Fringe benefit tax

Currently, if a taxpayer elects to pay fringe benefit tax on an annual or income year basis, interest is charged from the due dates which would have applied had the taxpayer not made the election. This was to compensate the Government for the deferral. The regulation which gave effect to this has now been repealed, and section

120S sets out the amount and nature of interest to be added to fringe benefit tax paid on an annual or income year basis. Section 120S gives the same effect as the now-repealed regulation. However, under the new rules interest will be paid on overpayments.

Provisional tax

The new interest rules are effectively an extension of the current provisional tax use of money interest provisions. However, they don't eliminate specific provisions relating to provisional taxpayers, such as dates from which interest applies, and the criteria used to establish who is a provisional taxpayer. Sections 120K to 120N cover the implications of the new rules for provisional taxpayers.

A $100 tax threshold will apply before any use of money interest is imposed or paid. This is provided for in section 183F. The interest rates applying to provisional tax will be consistent with the general interest rates applying to all taxes and duties.

Calculating the interest

Section 120E sets out the formula for calculating interest. It will be calculated on a daily basis on the amount of unpaid or overpaid tax.

Interest will not compound or be included in the calculation of late payment penalties. However, it will be assessable and deductible and subject to resident withholding tax or NRWT. Use of money interest will be calculated on the daily balance of the taxpayer's account, excluding any court costs and solicitors' fees.

Interest on underpayments will be charged on any amount of tax owing to the Commissioner, including any accumulated penalties. This will include any late payment penalty, underestimation penalty, late filing penalty and any shortfall penalty due. The start date for interest will be the day after the date the penalty is due.

Under the previous provisional tax interest rules, payments received after specific due dates were not taken into account when calculating interest. However, under the new rules any payment made at any date will be taken into account for interest calculations. This means taxpayers could incur both debit and credit interest within the same tax period.

Section 120F(4) provides that when debit and credit interest amounts are calculated for the same period, the sum of those amounts will constitute the interest figure that is applied to the taxpayer's account.

Start date

Underpayments

Use of money interest on underpayments will start on the day after the original due date for paying the tax, and end on the date the tax is fully paid.

For example, if a reassessment increases a taxpayer's income tax liability of three years ago, three years' interest will be owing to the Commissioner. Interest will be charged on the difference between the original amount of tax paid and the new amount assessed, even though time will be allowed for payment before a late payment penalty is imposed.

Overpayments

Use of money interest on overpayments will start on the later of:

1. the day after the original payment due date
2. the day after the date the payment was made.

The stop date is the date the tax is fully refunded or transferred to another account.

If a tax return must be filed for the tax to which the interest relates, the start date for credit interest will be the later of either 1 and 2 above, or the day after the tax return is filed. This is because Inland Revenue cannot refund the tax until the return is filed. An exception is made for provisional taxpayers, to ensure they receive interest on overpaid provisional tax.

GST refunds

For a GST refund, use of money interest starts on the latest of the following days:

1. the day after the earlier of:
   - the 15th working day after Inland Revenue receives the GST return
   - the original due date for payment
2. the day after the return is received
3. the day after the date payment is made.

Interest rate

Section 120H states that the interest rate for both underpayments and overpayments will be set by Order in Council. The rate may be reviewed "from time to time".

The interest rates have yet to be determined. They will be determined before 7 February 1997, and based on market interest rates applicable at that time.

Threshold

Under section 183F, a threshold of $100 of underpaid or overpaid tax will apply before interest is charged or paid. This means that only unpaid or overpaid tax greater than $100 on a specific due date will attract interest.

Payment application

Section 120F provides that payments made by taxpayers will first clear any unpaid interest amounts and then be credited against the tax outstanding. This is consistent with the commercial approach to charging and collecting interest.

Recovery of interest

For recovery purposes, debit interest is treated as being of the same nature as the tax to which it relates. Like-

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wise, overpayments of credit interest can also be recovered in the same manner. Credit interest may be applied towards payment of unpaid tax. This approach also avoids the need to impose late payment penalty on interest.

Assessability and deductibility

Interest paid on overpayments will be assessable, and interest charged on underpayments will be deductible under the normal income tax rules. Interest will be deemed to be interest on money lent for the purposes of determining whether a deduction is available under the Income Tax Act.

Interest will be assessable in the income year in which it is refunded to the taxpayer or transferred to clear tax owing in another revenue account. For reassessments, interest will be assessable in the income year following the year of reassessment.

Interest will be deductible in the income year in which it is assessed. For reassessments, it will be deductible in the income year following the year of reassessment.

Tax in dispute

The tax in dispute provisions were introduced to compensate taxpayers and Inland Revenue for the time value of money over the period of the dispute, and to reduce the taxpayers' incentives to continue litigation simply to defer paying tax.

Under the new disputes resolution rules, the obligation to pay non-deferrable tax in dispute before requesting a case stated or commencing a challenge is unchanged.

If the taxpayer is successful in the dispute, the Commissioner will pay interest on the tax which the taxpayer paid before litigation. Alternatively, if the Commissioner is successful the taxpayer will be liable for interest on the unpaid portion of the tax which is outstanding from the original due date.

Objection to interest

Section 120I provides that a taxpayer may not object to or challenge the imposition of interest payable. However, if the amount of interest imposed has been calculated incorrectly, the taxpayer is still able to require the Commissioner to make the appropriate amendments to ensure that the interest charged is correct.

Special provisions

The following sections contain provisions which relate to particular areas.

Section 120G states that the payment date for interest payable by a taxpayer to the Commissioner is "immediately and without the need for a demand." This means that interest is due from the date that it is charged whether or not a statement of account is sent to the taxpayer.

Section 120O deals with the date interest starts on tax reconciliations. It provides that when tax is overpaid, interest will start on whichever of the following is applicable:

1. If the due date is unchanged, the day after the later of:
   - the due date for payment
   - the date the payment is made
2. If there is a new due date, the later of:
   - the day after the original due date for paying the tax
   - the date the payment is made.

Section 120P applies when taxpayers can elect to spread income back over previous income years. It states that no interest is payable before the terminal tax date for the election income year or apportionment income year.

Example

A taxpayer incurred a tax shortfall in the 1998 year and elected to apportion it back over the 1995, 1996 and 1997 years. Interest would apply only from the 1998 payment due date.

Section 120Q states that for the purposes of Part VII, the due date of underestimation penalty tax is the taxpayer's third instalment date. Currently the due date is the due date for the payment of terminal tax.

Section 120R states that for foreign dividend withholding payments, if a taxpayer elects to reduce losses instead of making foreign dividend withholding payments, payment will be deemed to be made within the required period if the notice of election is given within that time.

Section 120U provides that when a taxpayer pays a bond or other security rather than making a deduction from a payment to a non-resident, and it is later established that a deduction should have been made, the interest start date will be the day after the day on which the amount would have been payable if a bond or other security had not been provided.

Part 3 - Penalties

Introduction

Section 139 sets out the purpose of the penalties provisions of the Act, which are as follows:

- to encourage taxpayers to comply voluntarily with their tax obligations and to co-operate with Inland Revenue
- to ensure that penalties for breaches of tax obligations are imposed impartially and consistently
- to act against non-compliance with tax obligations effectively and at a level that is proportionate to the seriousness of the breach.

The legislation introduces important changes to the penalty provisions of the Inland Revenue Acts. These changes promote fairer and more effective enforcement and improve the consistency in applying penalties overall and between the different tax types.

The foundation of the new rules is a statement of standards which taxpayers must meet in complying with their obligations. These standards are then reinforced by a comprehensive structure of penalties.

At the core of the penalty rules is a positive standard of reasonable care. This means that individual taxpayers' actions in meeting obligations should be at the standard expected of a reasonable person. In addition, for interpretive matters which involve significant amounts of tax, taxpayers must ensure that they have interpreted the law in a reasonable way.

Background

Existing provisions do not comprehensively address the different ways taxpayers may fail to meet the requirements placed on them. They tend to focus on taxpayers' responsibilities to provide factual information, even though today's environment requires more than just the provision of information. The current system generally relies on taxpayers to make a first assessment of their own tax liability, so the standards they are expected to meet in interpreting and applying the law needed to be clarified.

The new penalty rules support self-assessment concepts by encouraging voluntary compliance with the law. They clarify the standards and obligations expected of taxpayers in relation to their tax liability, and reinforce these with a comprehensive structure of penalties.

Key features

- The legislation introduces a late filing penalty of $50, $250 or $500, depending on the taxpayer's net income for the relevant year.
- The late payment penalty has been changed from 10% to 5%, with 2% monthly incremental penalties.
- Shortfall penalties for taxpayers who do not take reasonable care to determine the correct amount of tax have been introduced.
- There is a new penalty of 20% of the resulting tax shortfall if taxpayers have an unacceptable interpretation of how the law applies to their tax affairs. The penalty will apply if the tax at stake exceeds a specified threshold.
- Taxpayers who engage in an abusive tax position will be liable to a shortfall penalty of 100% of the resulting tax shortfall.
- Shortfall penalties will be reduced by 75% for voluntary disclosure before audit and by 40% for voluntary disclosure during an audit. Adequate disclosure at time of filing of an unacceptable interpretation will result in a 75% reduction.
- Shortfall penalties will be increased by 25% if a taxpayer obstructs the Commissioner.
- Shortfall penalties will be reduced by 75% if an incorrect tax position is reversed or corrected in a return period prior to an audit.
- Criminal penalties have been standardised and a maximum five-year term of imprisonment for evasion and related offences introduced. Monetary penalties of up to $50,000 apply to most offences.
- Additional tax and penal tax have been repealed.
- Court orders to obtain information have been introduced.

Civil penalties

Section 3(1) defines civil penalty as:

- an underestimation penalty
- a late filing penalty
- a late payment penalty
- a shortfall penalty

Each category of civil penalty is discussed below.

Non-deductibility of civil penalties

Section DB of the Income Tax Act 1994 prohibits tax deductions for income tax penalties. This has been amended to include civil penalties. Civil penalties are therefore not tax-deductible.

Underestimation penalty

The provisional tax underestimation penalty has been retained. This penalty is still necessary as it has been designed specifically to enforce a particular obligation which cannot be effectively enforced using generic civil penalties like the late payment penalty.

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Late filing penalty

Legislation

Section 139A states that late filing penalties will apply to the following annual returns which are required under the TAA:

- annual income tax returns
- Family Support end of year statements
- partnership returns,
- returns by executors and administrators
- special returns for agents, non-resident traders, taxpayers leaving New Zealand or who have ceased business, returns to date of death, bankruptcy or liquidation
- PAYE and ACC earner premium reconciliation statements
- ACC employer premium calculation returns.

A taxpayer is liable to a late filing penalty if the required return is not filed on time and the taxpayer has been notified that the penalty is payable. For income tax returns the amount of the penalty is as follows:

Amount of net income	Late filing penalty
less than $100,000	$50
$100,000 - $1,000,000	$250
greater than $1,000,000	$500
reconciliation statements	$250

Initially Inland Revenue will restrict the late filing penalty to annual income tax returns for individuals and companies, PAYE reconciliations and ACC reconciliations.

Note that this penalty does not apply to either GST or FBT returns, or other periodic returns that require a payment at the time of filing.

Discussion

The International Monetary Fund recommended introducing a late filing penalty after its review of Inland Revenue in 1989. It proposed that the penalty be a flat fine automatically imposed by Inland Revenue. The Tax Simplification Consultative Committee supported this recommendation in 1990.

The obligation for taxpayers to file income tax returns by the due date is a basic one, but previously there was no effective penalty for those who failed to do so. Because the tax system relies on taxpayers filing their returns on time, it was considered that a failure to meet this obligation should attract a penalty.

Application of penalty

The late filing penalty may apply to a taxpayer who does not file a return "on time", which means on or before the due date. This means the late filing penalty could apply both to late and non-filers of returns.

The late filing penalty will be imposed at the Commissioner's discretion, and only after the taxpayer has been notified that a return is required. The notification would advise taxpayers that they must file a return or notify Inland Revenue if there is some valid reason for not filing the return.

Taxpayers who do not file their return or notify Inland Revenue of the reason for not filing will have the late filing penalty imposed.

The amount of late filing penalty will depend on the amount of the "net income" returned. Net income is the gross income less expenses and before any loss offsets.

The late filing penalty may be remitted if taxpayers were not able to file on time for reasons beyond their control. This is discussed in detail in Part 6, which deals with remissions.

Any taxpayer who files a "nil" or incomplete return by the due date to avoid the late filing penalty may be liable to shortfall penalties. At the very least, a taxpayer who files a return knowing that it may be incorrect would not have shown reasonable care.

Due date for late filing penalty

The late filing penalty for annual income tax returns will be due and payable on the latest of these dates:

- 30 days after the Commissioner notifies the taxpayer that the penalty is payable
- 7 February for IR 5 taxpayers
- the terminal tax due date for all other taxpayers.

The due date for paying the late filing fee for reconciliations will be the latest of these dates:

- 30 days after the Commissioner notifies the taxpayer
- 31 May following the income year to which the reconciliation relates.

A late filing penalty may be imposed even if the return results in no tax to pay or a refund, as the penalty is related to the filing of returns and not the amount of tax payable. The objective of the late filing penalty is to get taxpayers to file their returns on time.

The late filing penalty will be subject to late payment penalty and interest if not paid by the due date.

Extension of time issues

Section 37(3) allows the Commissioner to extend the due date for filing returns if a taxpayer makes a written application on or before the due date for filing. The Commissioner also has a discretion to accept a late request for extension of time.

Written requests for extension of time should state the return period to which the extension application relates, the length of time the extension is required and the reasons for requesting the extension. Acceptable reasons for requesting an extension of time are generally

reasons beyond the taxpayer's control. Some examples of acceptable reasons would be illness or accident.

If a taxpayer becomes a client of an agent who receives an extension of time, and the late filing penalty has already been imposed, the penalty will stand. Also, if an agent's extension of time for a client is withdrawn, the client could become liable for the penalty for the unfiled return. In this situation, Inland Revenue will give the taxpayer notice before we impose the penalty.

Late payment penalty

Legislation

Section 139B states that a taxpayer who does not pay the tax (called 'unpaid tax') by the due date is liable to pay a late payment penalty. The initial penalty is 5% of the unpaid tax, and is imposed on the day after the due date for paying the unpaid tax.

The incremental late payment penalty is 2% of the amount of tax to pay as at each month after the day on which a penalty is imposed. It continues for successive monthly intervals as long as any tax to pay remains unpaid.

The term 'tax to pay' means the unpaid tax together with any accumulated late payment penalty or incremental penalty.

The term 'unpaid tax' includes deductions that must be made and paid to the Commissioner (such as a PAYE deductions made and not returned), but does not include a late payment penalty.

Discussion

Application

The new rules introduce a standardised late payment penalty across all tax types except Student Loan repayments and Child Support.

There are two parts to the late payment penalty: an initial component which penalises taxpayers for not meeting a tax obligation by a due date, and an incremental component which encourages prompt payment of the debt over time.

The initial late payment penalty of 5% will be charged on the amount of tax outstanding after the payment due date.

The existing incremental penalties allow payment to be deferred by almost six months before further penalties apply. The new system shortens this interval, but reduces the rate of penalty. The new incremental penalties of 2% per month will be charged on the amount of tax outstanding as at the date of imposition.

The late payment penalty will apply from the day after the due date for paying the tax.

Threshold

Under section 183F the late payment penalty will not apply to unpaid tax of less than $100. Only unpaid tax greater than $100 will attract a late payment penalty and interest.

Late payment penalties are deemed to be of the same nature as the tax to which they relate, so they are included in the base amount when calculating interest.

Due date for paying tax

For various duties, the payment due dates are as follows:

Totalisator duty	-	20 days from the end of the month in which the race or sporting event was held
Lottery duty	-	14 days after the lottery is drawn
Cheque duty	-	the due dates remain unchanged
Stamp duty	-	for an instrument stamped in New Zealand: six months after the date the instrument was executed
	-	for an instrument stamped outside New Zealand: six months after the date it was first received in New Zealand after execution
Gift duty	-	six months after dutiable gift is made

If a tax liability is increased as a result of a reassessment, a new due date will be set for paying the additional tax assessed. The late payment penalty will apply only if the taxpayer does not pay the tax due by the new due date.

The previous "original due date" provisions for calculating additional tax when a taxpayer has been guilty of neglect or default have been repealed and replaced with the interest rules explained in Part 2 of this bulletin.

Taxpayers in financial difficulties will be able to minimise the impact of the late payment penalties by making an instalment arrangement with the Commissioner. The Commissioner will also be able to remit late payment penalties in limited circumstances. This is discussed in detail in Part 6, which deals with remissions.

Specific provisions

The following sections also relate to the late payment penalties:

Section 139C - Late payment penalty and provisional tax

Section 140 - If another person deducts and pays resident withholding tax

Section 140A - Underestimation penalty when income tax underestimated as at the final instalment date

Section 140B - Imputation penalty tax payable when there is an end of year debit balance

Section 140C - Dividend withholding payment penalty tax payable when there is an end of year debit balance

Section 140D - Application of other provisions of Act to imputation penalty tax and dividend withholding payment penalty tax.

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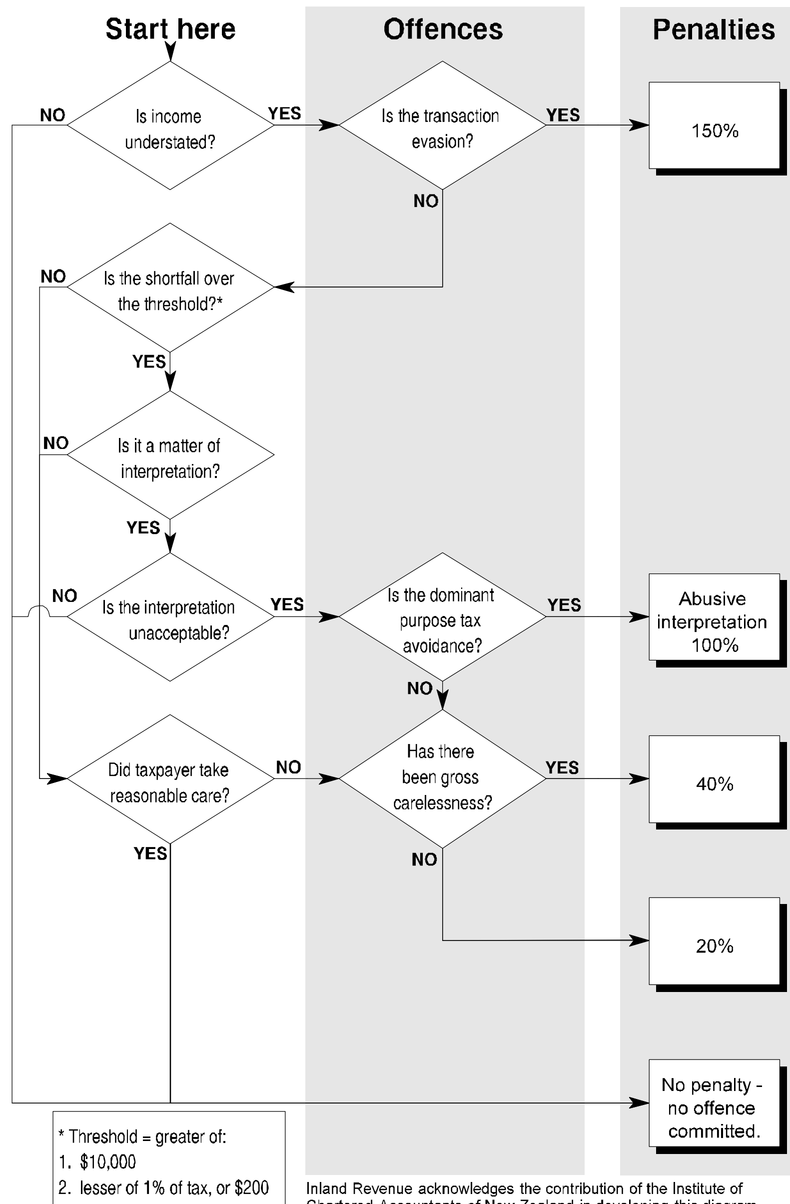
Shortfall penalties

The following table summarises the breaches and shortfall penalty rates applicable and includes the various adjustments that may be made to the base penalty rate.

	Penalty				
Action subject to penalty	Standard rate	If reduced by 75% for disclosure before audit	If reduced by 40% for disclosure during audit	If reduced by 75% for disclosure when filing	If increased by 25% for obstruction
Lack of reasonable care	20%	5%	12%	n/a*	25%
Unacceptable interpretation	20%	5%	12%	5%	25%
Gross carelessness	40%	10%	24%	n/a*	50%
Abusive tax position	100%	25%	60%	25%	125%
Evasion	150%	37.5%	90%	n/a*	187.5%

* This reduction is limited to the unacceptable interpretation and abusive tax position penalties because it specifically relates to the disclosure of the taxpayer's interpretation at time of filing.

The following diagram summarises how to determine whether an action is subject to a penalty, and the penalty rate that will apply.



Inland Revenue acknowledges the contribution of the Institute of Chartered Accountants of New Zealand in developing this diagram.

Reasonable care

Legislation

Section 141A provides that a taxpayer who does not take reasonable care in taking a tax position is liable to pay a shortfall penalty. This penalty will be 20% of the resulting tax shortfall.

If a taxpayer uses an acceptable interpretation of tax law in taking a tax position, he or she has also taken reasonable care in taking that tax position.

Discussion

The penalty for lack of reasonable care applies to any taxpayer who must take a tax position. That means it includes taxpayers who are required to make source deductions and who fail to exercise reasonable care in calculating the amount of tax to deduct or account for. For example, if an employer is away on a planned absence and forgot to make arrangements to pay tax deductions, that employer may incur a penalty for lack of reasonable care.

Whether the taxpayer acted intentionally is not a consideration. The reasonable care test requires a taxpayer to exercise the care that a reasonable person would be likely to exercise in the taxpayer's circumstances to fulfil the tax obligations. It is not a question of whether the taxpayer actually foresaw the probability that the act or failure to act would cause a tax shortfall, but whether a reasonable person in the same circumstances would have foreseen the shortfall as a reasonable probability. It equates with the concept of negligence in the civil law of Torts, and the jurisprudence is well established: "Negligence is to be measured objectively by ascertaining what in the circumstances would be done or omitted by the reasonable man." (*Meulan's Hair Stylists Ltd v CIR*)

In the tax context, reasonable care includes exercising reasonable diligence to determine the correctness of a return position. It also includes keeping adequate books and records to substantiate items properly, and generally making a reasonable attempt to comply with the tax law. The reasonable care test is not intended to be overly onerous to taxpayers. Reasonable care does not mean perfection. The effort required of the taxpayer is commensurate with that of a reasonable person in the taxpayer's circumstances.

Factors to consider

Ordinarily what is expected is the achievement of a standard appropriate to the category of taxpayer, rather than of the individual taxpayer involved.

The category of taxpayer will affect what constitutes reasonable care in each particular case. The standard required of a salary and wage earner will differ from that required of a business taxpayer. For most PAYE taxpayers, an earnest effort to follow the Tax Pack instructions will be sufficient to pass the reasonable care test. For business taxpayers, reasonable care means there must be an appropriate record keeping system and other procedures to ensure that the income and expenditure of the business is properly recorded and classified for tax purposes.

The circumstances that may be taken into account when determining whether a taxpayer has exercised reasonable care include:

- the complexity of the law and the transaction (the difficulty in interpreting complex legislation)
- the materiality of the shortfall (the gravity of the consequence and the size of the risk)
- the difficulty and expense of taking the precaution
- the taxpayer's age, health and background.

Business taxpayers

For a business, reasonable care may also take into account:

- the size and nature of the business
- the internal controls in place
- the business's record keeping practices
- system failures (however, this would be balanced with consideration as to why the system failure occurred).

If a taxpayer's accounting systems are designed to correctly classify entries according to their attributes and the system is monitored to ensure that the likelihood of error is reduced to an acceptable level, reasonable care is exercised.

Arithmetical errors

Arithmetical errors may indicate a failure to take reasonable care, but they are not conclusive. The decision will depend on the procedures the taxpayer had in place to detect such errors, the size, nature and frequency of the error, or the circumstances in which the taxpayer made the error.

Interpretations

On questions of interpretation, reasonable care requires a taxpayer to come to conclusions that a reasonable person would come to in the particular category of taxpayer. If a taxpayer is uncertain about the correct tax treatment of an item, reasonable care requires the taxpayer to make reasonable enquires.

Accordingly, for questions of interpretation, reasonable care will depend on:

- what efforts the taxpayer had taken to resolve the issue
- the types of advice received
- the certainty of the law.

Materiality

Materiality is implicit in the standard of "reasonable care". In considering whether a taxpayer has taken reasonable care, consideration will be given not only to the nature of the shortfall, but also to the size of the shortfall in relation to the taxpayer.

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Example 1

A retired taxpayer receives NZ Superannuation, interest income from three bank accounts and dividend income on several parcels of shares inherited from her late husband. She has not previously prepared a tax return because her husband always dealt with tax matters. Accordingly, she is now completing a tax return for the first time.

When she filled in the first tax return since her husband's death, she overlooked a dividend received from a parcel of shares that had been sold during the year and a small amount of interest. However, she has otherwise carefully returned all other amounts of interest and dividends received as well as the NZ Superannuation.

In this situation, the taxpayer has exercised reasonable care. The oversight was minor and does not detract from her generally careful approach. No penalty would be applied to any resulting tax shortfall.

Defence to reasonable care

In large adjustment cases when the matter turns on a question of interpretation, the acceptable interpretation standard must be satisfied. A taxpayer who can demonstrate that the position taken is an acceptable interpretation is deemed to have satisfied the reasonable care standard.

Tax agents/advisers

A taxpayer who has reasonably relied on the advice of a tax adviser or Inland Revenue will usually be considered to have exercised reasonable care. However, a taxpayer could still be liable for a penalty for lack of reasonable care by taking any of these actions:

- providing inadequate information when seeking advice
- failing to give reasonable instructions to a tax adviser
- relying unreasonably on a tax adviser or on wrong advice.

A taxpayer does not satisfy his or her obligation to take reasonable care simply by using the services of a tax agent or tax adviser. The taxpayer is still responsible for the proper recording of his or her tax affairs during the year, and for drawing all the relevant facts to the attention of the agent or adviser, in order to satisfy the reasonable care test. Taxpayers are expected to answer honestly any questions asked by the agent or adviser to do with preparing the return.

Taxpayers are unlikely to be considered to have breached the standard if Inland Revenue has failed to provide adequate information in our guides, if the taxpayer has relied on misleading information from reputable sources, or if the relevant information is extremely complex or specialised. Errors made for these reasons are understandable.

Case law

In Australia, to date, there has been only one case of "lack of reasonable care" taken to the courts. It is *Case 34/95, 95 ATC 319*, which involved the deduction of a superannuation claim.

The judge referred to the explanatory memorandum which illuminates Parliament's intended meaning of the phrase "reasonable care". It explained that reasonable care "....requires a taxpayer to make a reasonable attempt to comply with the provisions of [the Act] and regulations. The effort required is one commensurate with all the taxpayer's circumstances, including the taxpayer's knowledge, education, experience and skill". The judgment then stated that "...given that the taxpayer's return was prepared by experienced tax agents, who objectively should have known, or at the very least, had the resources to find out, the requirements in respect of the deduction of superannuation contributions, and who furthermore prepared the returns for the particular employer involved, it is difficult to find that reasonable care has been exercised."

A similar case in New Zealand would have a different outcome. This is because New Zealand taxpayers are not vicariously liable for a tax adviser's carelessness. In such a case in New Zealand, if it was established that the taxpayer had reasonably relied on the tax adviser's advice, the taxpayer would be considered to have taken reasonable care.

Burden and standard of proof

The burden of proof rests with the taxpayer to show that he or she has taken reasonable care. The standard of proof is the civil standard of "balance of probabilities". Accordingly, a taxpayer who can show that it is probable that he or she took reasonable care will have satisfied the standard.

Example 2

Facts: A newly-established business was experiencing rapid growth, and its accounting system had not kept pace and had become inadequate. The firm's tax return was prepared from this accounting system

Inland Revenue audited the business and found several omissions of income (from accounts for services rendered by the firm), along with overstated claims for deductions. The tax shortfalls could have been avoided if proper records had been maintained.

Penalty: The taxpayer had been careless in maintaining an inadequate accounting system, which resulted in the tax shortfall. For business taxpayers, reasonable care would require having an appropriate record keeping system to ensure that the business's income and expenditure is properly recorded and classified for tax purposes. A reasonable person conducting the business would have foreseen during the year that unless the accounting system was improved it could have resulted in a tax shortfall.

The taxpayer is subject to a penalty of 20% for lack of reasonable care.

Example 3

Facts: The same as in the previous example, except that the amounts involved were small in relation to total income for the year. The errors occurred early during the period of rapid expansion, and the taxpayer had fixed the problem with the accounting system before the end of the taxable period, by introducing a new system to cope with the expansion of the business. No errors were detected in the later part of the year.

Penalty: The taxpayer had realised that the accounting system had proven inadequate for the expanding needs of the growing business and had taken positive steps to resolve the problem as soon as it became apparent. A reasonable business taxpayer, when establishing the business, may not have foreseen that the accounting system would be inadequate at the outset, but would have foreseen during the year that unless the system was improved it would result in a tax shortfall.

Accordingly, there would be no penalty.

Example 4

Facts: During the stock take an employee transposed the cost price of one category of stock. The entire stock take involved counting 2000 different categories of stock. The error was not found during normal checking procedures used by the company, but came to light during an audit. The shortfall was minimal in relation to the entire stock figure.

Penalty: The taxpayer had taken reasonable care in carrying out the stock take. The procedures in place would have normally picked up any discrepancies. The error was also not sufficiently material to put the taxpayer on notice. Accordingly, there would be no penalty.

Example 5

Facts: The taxpayers, a husband and wife, own a corner dairy. The husband looks after all operations in the shop. His wife helps in the shop and keeps basic accounts which are sent to their accountant at year end for preparation of the final tax return. The business is registered for GST and files two-monthly returns. During previous audits it has been ascertained that good records are kept for each return, comprising a full worksheet substantiated by relevant documentation. One of the taxpayers prepares the GST return and, after completion, the return is checked by the other.

As a result of an audit, a tax shortfall is found in the return for one period. The discrepancy is due to an arithmetical error and is small relative to the GST payable for the period.

Penalty: Inland Revenue considers that the taxpayers have taken reasonable care to complete the GST return. Good records are maintained and the return was carefully prepared and checked as usual. The shortfall is not material and therefore does not detract from the fact that the taxpayers took reasonable care in completing the GST return. Accordingly, no penalty would be imposed in this case.

Example 6

Facts: The taxpayer is a salary and wage earner who regularly gives money to a church group that meets weekly at a member's house to pray. The group is raising funds to build a church.

At year end, she refers to the IR 5 income tax return guide to prepare her income tax return. She notes that the guide states that she may claim a rebate for "donations to churches" provided that she holds a receipt to substantiate her claim. She claims the maximum rebate of $500 as she holds a receipt which she has received from the group which substantiates that she has donated $1,500 for the building of the church.

The return is audited and Inland Revenue notes that the receipt in the return is not from a recognised church in New Zealand that holds approved donee status. The receipt is not eligible for the rebate claimed. Accordingly, the return is reassessed, creating a tax shortfall of the amount of the rebate claimed.

Penalty: The taxpayer has exercised reasonable care as she has followed the instruction as set out in the guide. There was no apparent reason to make further enquires. A reasonable person in the taxpayer's circumstances would not have been aware that the church was required to hold approved donee status. There would be no penalty in this case.

Example 7

Facts: A salary and wage earner started up a lawn mowing business which he operates in the evenings and weekends, to make some additional income.

The taxpayer knows that this additional income is taxable and has set up a cash book system for recording his lawn mowing income. However, occasionally when he is busy he forgets to record some of this income.

He prepares his income tax return using the information in his records. As a result of an audit, he incurs a tax shortfall resulting from lawn mowing income being understated.

Penalty: The taxpayer has displayed a lack of reasonable care. Although he has set up a system and kept records, he has not maintained them sufficiently to return the correct amount of income for tax purposes. The result of not keeping accurate records would have been foreseen by a reasonable person in this taxpayer's circumstances. Therefore there is a 20% penalty for lack of reasonable care.

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Example 8

Facts: The taxpayer inherited two rental properties in 1996. The properties had been rented out before he inherited them, and each was being managed by a separate real estate firm.

The taxpayer noted that the property values in the area where one of the houses was situated had increased substantially. He undertook renovations in this house which involved redecorating the interior and replacing carpet in the living room. He also had a carport built at this property as there had previously been no off-street parking.

In the tax return for the year ended 31 March 1998 he understated his gross income by omitting to return the March rental from one of the properties, because he had not received the rental income statement from the real estate agent. He also claimed a deduction for the expenditure incurred in erecting the carport, along with the cost of redecorating and recarpeting one of the properties.

As a result of an audit, a tax shortfall was ascertained for the understated income, and the expenditure claimed for building the carport was disallowed.

Penalty: The taxpayer had been careless in not returning the rental income for March as he should have been aware that not all of the income for the year had been accounted for.

Before claiming the carport as a revenue expense, a reasonable person would have contacted Inland Revenue or an adviser to find out if this expenditure was deductible for tax purposes. Accordingly, there will be a 20% penalty for lack of reasonable care .

Unacceptable interpretation

Legislation

Section 141B provides a penalty for unacceptable interpretations.

A taxpayer who has a tax shortfall for a return period will be liable to pay a shortfall penalty if all of the following apply:

- The shortfall was caused by a tax position involving an interpretation or application of a tax law.
- The tax shortfall exceeded both $10,000 and the lesser of $200,000 or 1% of the taxpayer's total tax figure for the relevant return period.
- The tax position taken, when viewed objectively, fails to meet the standard of being about as likely as not to be correct.

The penalty payable is 20% of the resulting tax shortfall.

Discussion

The unacceptable interpretation standard signals that taxpayers who take a position which has significant tax consequences should take extra care. The standard is designed to encourage taxpayers to ensure that the conclusions they reach are sound.

Interpretation or application of a tax law

The unacceptable interpretation standard only applies to tax shortfalls caused by a taxpayer treating a tax law as applying in a particular way.

A taxpayer treats the tax law as applying in a particular way by concluding that, on the basis of the facts and the way the law applies to those facts, a particular consequence follows. An example would be concluding that an amount of expenditure is deductible. In some cases a taxpayer's tax position may not represent the taxpayer's conclusions, but instead reflect errors in calculation or transposition. As a broad rule, if a tax shortfall was caused by an error in calculation or transposition error, section 141B will not apply because the taxpayer will not have treated a tax law as applying in relation to a matter in a particular way. An example would be a transposition error in a depreciation schedule. However, in such a case the reasonable care standard would need to be considered.

Threshold

The unacceptable interpretation standard applies only if the tax shortfall exceeds a specified threshold.

Section 141B(2) states:

A taxpayer is liable to pay a shortfall penalty if -

(b) The tax shortfall arising from the taxpayer's tax position exceeds both -

(i) $10,000; and

(ii) The lesser of $200,000 and one percent of the taxpayer's total tax figure for the relevant return period.

Tax cap

There is a $200,000 tax cap attached to the one percent threshold. The reason for this is that any tax shortfall over $200,000 is considered significant to the revenue, even if it isn't considered significant to the taxpayer. For example, if a taxpayer's total tax position was $30 million the cap of $200,000 tax would apply, as one percent of $30 million is $300,000.

The taxpayer's total tax figure

The taxpayer's total tax figure is defined in section 141B(3) as:

(a) The amount of tax paid or payable by the taxpayer in respect of the return period for which the taxpayer takes the taxpayer's tax position before any group offset election or subvention payment; or

(b) Where the taxpayer has no tax to pay in respect of the return period, -

(i) Except in the case of GST, an amount equal to the product of -

(A) The net losses of the taxpayer in respect of the return period, ascertained in accordance with the provisions of the Income Tax Act 1994; and

(B) The basic rate of income tax for companies in the relevant return; or

(ii) In the case of GST, the refund of tax to which the taxpayer is entitled for the return period, -

that is shown as tax paid or payable, or losses incurred, or as a refund to which the taxpayer is entitled, in a tax return provided on time by the taxpayer for the return period.

Accordingly, a taxpayer who is in a loss situation for the relevant period may convert the tax losses into a tax figure for the purposes of establishing the total tax position. This is done by using the company tax rate applicable for that period. This applies both for individuals and companies, for the purposes of converting the losses in the relevant period.

Note that the losses to be converted are only those incurred for that relevant period - they do not include losses carried forward. For example, if a company made a profit of $50,000 in 1999 and had losses carried forward from 1998 of $100,000, the taxpayer's total tax position for 1999 would be $50,000, as this is the taxpayer's tax position before any losses carried forward or offsetting occurs.

The relevant return period

"Return period" is defined as "..the period covered by a tax return, or which would be covered by a tax return if one were provided". Therefore if a discrepancy spanned several periods, a separate tax shortfall would be calculated for each return period.

Other entities

Partnerships

Section 141B(8)(a) provides that in establishing whether a partnership is over the threshold it is necessary to consider the shortfall incurred by the partnership against the partnership income. This means that for the purposes of calculating whether a partnership is over the threshold, it is treated as a separate entity, as it currently would be for GST.

Section 141B(8)(b) provides that the company tax rate applies when calculating the tax shortfall to determine whether a partnership is over the threshold.

Example

In one return period, a partnership takes various tax positions which result in $1,200,000 tax to pay.

During an audit Inland Revenue disallows a claim for a non-allowable deduction, resulting in a tax shortfall of $14,000 for the partnership. The two partners in the partnership share equally in the profits, so each partner would be assessed with an additional $7,000 tax.

For the purposes of establishing whether an unacceptable interpretation standard applies, the shortfall of the partnership ($14,000) is considered, not that of the individual partners. As the partnership tax shortfall exceeds both $10,000 and $12,000 (being 1% of $1,200,000), the partnership must have an acceptable interpretation.

If it is determined that the partnership has an unacceptable interpretation, a shortfall penalty would be imposed. The penalty would be $2,800, being 20% of the tax shortfall. Accordingly, each partner would be assessed with $7,000 tax and a shortfall penalty of $1,400.

Trusts

When a shortfall arises from a trust the tax shortfall will be assessed as trustee income and any shortfall penalties will be imposed on the trustee. This is because the trust is a separate legal entity, with the trustee liable for tax on any income which is not beneficiary income.

Accordingly, when establishing whether the trust is over the threshold it is necessary to consider the shortfall incurred by the trust.

Joint ventures

Joint venturers will be separately liable for any shortfall penalty as they are independent parties for tax purposes.

Generally, a share of gross income is returned by each venturer and the individual expenses of each venturer deducted. In these situations it is appropriate that the threshold for the penalty be determined on each individual venturer.

Similar or identical items

Section 141(10) states:

If

(a) In a return period, a taxpayer takes a taxpayer's tax position -

(i) In respect of, or as a consequence of entering into, an arrangement; or

(ii) In respect of an article, item, or matter; and

(b) In the same return period, the taxpayer takes a similar or identical taxpayer's tax position -

(i) In respect of, or as a consequence of entering into, a similar or identical arrangement; or

(ii) In respect of a similar or identical article, item, or matter, -

the tax shortfalls arising from the taxpayer's tax positions are to be aggregated and deemed to be one tax shortfall.

"Identical" and "similar" items are to be treated as one tax shortfall. As no guidance is given in the Act on what "similar" means, it takes its ordinary meaning.

The New Shorter Oxford English Dictionary definition of similar is:

Of the same substance or structure throughout; homogeneous. Having a resemblance or likeness; of the same nature or kind.

The second of the Government's discussion documents on this subject provided the following example:

Separate lease payments for two cars leased on the same terms will be added together for the purposes of testing whether the threshold has been reached.

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Accordingly, identical and similar items must be treated as one for the purposes of determining whether the tax position is over the threshold.

What is an "unacceptable interpretation"

Section 141B of the Act provides that

..an unacceptable interpretation of a tax law is, in relation to a tax position taken by a taxpayer that ....(b) Fails to meet the standard of being, viewed objectively, about as likely as not to be the correct tax position.

Level of standard

The unacceptable interpretation standard does not require that the treatment a taxpayer gives to a particular matter must be the better view, or must be more likely than not the correct treatment. The test is "about as likely as not to be correct".

The commentary to the Bill states

...the words 'about as likely as not correct' are intended to confirm that it need not be a 50% or more expectation that the taxpayer's position is the better view. A slightly lower expectation will be accepted...

Significant emphasis should be given to the word "about". It is not intended to remove the right of a taxpayer to take up issues with the Commissioner, rather, it must be a position to which a court would give serious consideration, but not necessarily agree with. This means that the prospect of the taxpayer's interpretation being upheld by the court must be substantial, although not necessarily 50 percent. The taxpayer's argument should be sufficient to support a reasonable expectation that the taxpayer could succeed in court.

If a taxpayer adopts one of several equally likely interpretations this will generally satisfy the standard, as each position is about as likely as any other position to be the correct tax position.

Taxpayer effort

The unacceptable interpretation standard is an objective test involving an analysis of the law to the relevant facts. This means that it is not relevant that a taxpayer believes that the position taken was an acceptable interpretation.

The unacceptable interpretation standard does not take into account taxpayers' efforts in resolving unclear issues. The standard is intended to focus on the merits of an argument in support of a particular position, rather than the taxpayer's effort in resolving issues. The strength of the argument is weighed by considering the existence and reasoning of relevant authorities. Relevant authorities have not been defined in the legislation, but the following matters must be considered.

Matters which must be considered

Section 141B(7) states:

The matters that must be considered in determining whether the tax position taken by a taxpayer involves an unacceptable interpretation of a tax law include -

(a) The actual or potential application to the tax position of all the tax laws that are relevant (including specific or general anti-avoidance provisions); and

(b) Decisions of a court or a Taxation Review Authority on the interpretation of tax laws that are relevant (unless the decision was issued up to one month before the taxpayer takes the taxpayer's tax position).

Relevant tax laws

Tax law is defined in section 3(1), which states:

Tax law means -

(a) A provision of the Inland Revenue Acts or an Act that an Inland Revenue Act replaces:

(b) An Order in Council or a regulation made under another tax law:

(c) A non-disputable decision:

(d) In relation to an obligation to provide a tax return or a tax form, also includes a provision of the Accident Rehabilitation and Compensation Insurance Act 1992 or a regulation made under that Act:"

Section 141B(7)(a) specifically refers to the anti-avoidance provisions. This ensures that it cannot be argued that a tax position or interpretation is an acceptable interpretation in terms of a particular legislative provision irrespective of the operation of other provisions such as general anti-avoidance provisions. This is a scheme and purpose view of tax legislation.

Relevant court decisions

Factors that affect the weight of an authority:

- Source - This refers to the court or tribunal which made the decision upon which the taxpayer places reliance. The higher the source of a decision in the judicial hierarchy, the greater the weight. For example, a Court of Appeal decision will be accorded greater weight than a TRA decision.
- Relevance - Authorities that have similar factual circumstances to the case asserted by a taxpayer are more relevant than those authorities which can be materially distinguished on the facts.
- Persuasiveness - An authority that merely states a conclusion is ordinarily less persuasive than one that reaches its conclusions by cogently relating the applicable law to pertinent facts.

However, if a taxpayer has no authorities to support a case there may still exist an acceptable interpretation. In such cases, a taxpayer needs a well-reasoned construction of the statutory provision which is about as likely as not to be correct.

Opinions expressed by tax professionals

The commentary to the bill states

...In the absence of relevant case law, information which supports a reasonable argument may include such items as......the contents of tax opinions, legal articles and related material. However, the mere existence of an opinion from an adviser would not on its own indicate that an acceptable interpretation exists. It is the contents of the opinion, not the fact of seeking advice, which will be relevant.

Accordingly, the existence of a tax professional's opinion does not of itself indicate an acceptable interpretation, but the contents of that opinion may support an acceptable interpretation.

Other matters

Other matters which may be considered in particular circumstances include the commentary to the bill, enacting the relevant law, binding public rulings on similar issues, articles written by tax professionals with expertise in the particular field, and related material, and references made to statutes other than the Inland Revenue Acts.

Timing

Under section 141B(5), whether an interpretation of a tax law is acceptable is to be determined at the time the taxpayer takes a tax position in which the interpretation is involved.

To determine whether an unacceptable interpretation exists, one must consider the authorities available at the time the taxpayer took the tax position - generally when the taxpayer files the tax return. In addition, subsequent clarification or development of case law or public rulings in a particular area may confirm that a position taken is acceptable. However, subsequent developments will not be used to argue that a taxpayer's position was an unacceptable interpretation.

For example, a taxpayer may have relied on a court case which was later overturned. The taxpayer would not be penalised because at the time of taking the tax position the law supported the interpretation.

An unacceptable interpretation standard applies whether or not the taxpayer has articulated that position. Taxpayers will be able to substantiate their arguments if a dispute arises after filing their returns. However, in most cases taxpayers will need to consider the validity of an interpretation relating to a sizeable transaction when they take the position in their returns or earlier.

Binding rulings and the unacceptable interpretation standard

The fact that a taxpayer adopts an interpretation that differs from that of a ruling will not necessarily mean that the taxpayer has an unacceptable interpretation. However, the existence of an applicable binding ruling supporting the taxpayer's position will be an absolute defence against the imposition of a penalty as there will be no tax shortfall.

Relationship to the reasonable care standard

The aim of the unacceptable interpretation standard is to ensure that taxpayers take care in considering their position. This is also required by the reasonable care standard, but the unacceptable interpretation standard takes away some of the so called "subjective elements" (for example, taxpayer effort) when there is a significant amount of tax at stake.

A taxpayer who satisfies the unacceptable interpretation standard is also deemed to have satisfied the reasonable care standard.

Example 1

Facts: When preparing its tax return, a corporate taxpayer claims a $500,000 deduction for the purchase of a particular item. This deduction exceeds the threshold for requiring an acceptable interpretation.

In taking this tax position, the corporate taxpayer adopted an old TRA decision in which it had been held that items of that nature were revenue expenditure. However, over subsequent years case law in this area has evolved, and a recent Privy Council decision clearly established that this type of expenditure is of a capital nature and should be capitalised and depreciated, rather than deducted. That decision was given 12 months before the taxpayer took the tax position.

Penalty: The taxpayer's tax position was based on a TRA authority which had similar factual circumstances, so it would not be considered unreasonable. However, the recent Privy Council decision also had similar factual circumstances which could not be materially distinguished from those of the taxpayer, so its authority outweighs the TRA decision. Accordingly, the corporate taxpayer's tax position fails to satisfy the standard of "about as likely as not to be correct".

The corporate taxpayer did not have an acceptable interpretation, so a penalty of 20% would be imposed on the tax shortfall resulting from the tax position taken.

Example 2

Facts: The taxpayer is a corporate entity involved in property development. Its in-house accountant prepares the year end tax return.

During the year the taxpayer purchased land which cost $1,000,000, for the purpose of a large residential housing development project. However, at year end development of the land had not started.

The taxpayer sought advice from an outside tax adviser on the appropriate tax treatment of the development of the project. The tax adviser considered that the taxpayer could claim the cost of the land as a deductible expense. However, the adviser overlooked the fact that as development had not yet started the cost of the land had to be added back to income.

The corporate taxpayer's tax return showed that the total tax payable for the year was $210,000.

Inland Revenue audited the taxpayer's income tax return. Even though the cost of the land was a deductible expense, no development had started by year end. The purchase price of the land was considered to be trading stock, and accordingly added back to assessable income. The result was that the taxpayer incurred a tax shortfall in excess of the threshold for requiring an acceptable interpretation.

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Penalty: The taxpayer had taken reasonable care with its tax affairs as it had sought advice regarding the correct tax treatment of the land purchased. The taxpayer had no reason to doubt the tax advice received about the development project.

As the unacceptable interpretation standard is objective, the taxpayer's efforts and intention are irrelevant. The unacceptable interpretation standard focuses on the merits of an argument in support of a particular position, rather than the taxpayer's effort in resolving the issues.

It is clear in statute law that any trading stock must be added back to income at year end, and case law supports this interpretation.

The purchase of the land is considered to be trading stock, so the taxpayer's position does not meet the test of being "about as likely as not correct". Consequently, the taxpayer is liable to a 20% shortfall penalty for an unacceptable interpretation.

Example 3

Facts: A large corporate taxpayer values its closing trading stock at cost price for the year ended 31 March 1998. In accordance with the group's policy on trading stock it then adjusts the closing stock values, based on a formula which writes down all trading stock by a fixed percentage. The adjustment is made to allow for obsolescence.

In compiling its tax return for the year ended 31 March 1998, the taxpayer did not add back the adjustment made to the closing stock. The adjustment for the return period ended 31 March 1998 was for $730,000 which exceeded the threshold for requiring an acceptable interpretation.

Tax law clearly provides that taxpayers must value their closing stock at either cost price, market selling price or replacement price. The taxpayer has valued the closing stock at cost price, and then made an adjustment to this value, resulting in an overall lower value of trading stock.

The taxpayer considers that tax law allows for adjustments to trading stock for obsolescence and, accordingly, contends that the adjustment should not be added back for taxation purposes.

It is accepted that adjustments can be made to trading stock for obsolescence. However, using a fixed percentage writedown across all closing stock does not fairly reflect the obsolescence of the individual lines of stock. Statute law requires that the basis used must be fair and reasonable and gives guidance in this area on the factors to be considered.

Penalty: Even though the taxpayer used what it considered to be the most appropriate method of valuation, it is well established in tax law that such global adjustments to trading stock, resulting in a stock reserve, are not allowable for tax purposes. To reasonably reflect the obsolescence of stock, the taxpayer should have considered the stock items held on a line by line basis. Accordingly, the taxpayer's tax position does not meet the test of being "about as likely as not correct". A 20% penalty for an unacceptable interpretation would be imposed on the tax shortfall.

Gross carelessness

Legislation

Section 141C deals with gross carelessness. It states:

(1) A taxpayer is liable to pay a shortfall penalty if the taxpayer is grossly careless in taking the taxpayer's tax position (referred to as "gross carelessness").

(2) The penalty payable for gross carelessness is 40% of the resulting tax shortfall.

(3) For the purposes of this Part, gross carelessness means doing or not doing something in a way that, in all the circumstances, suggests or implies complete or a high level of disregard for the consequences."

Discussion

Gross carelessness is a more serious breach than lack of reasonable care. Gross carelessness will occur if a taxpayer's behaviour displays a high degree of carelessness and disregard of consequences. Typically, a high level of carelessness will be characterised by conduct which creates a high risk of a tax shortfall occurring when this risk and its consequences would have been foreseen by a reasonable person in the circumstances.

Gross carelessness does not require taxpayers to intend to pay less than is owed, but will require more than mere inadvertence or carelessness.

Gross carelessness is a new objective standard. It is something more than a lack of reasonable care but less than evasion in that it does not require the necessary intention to evade.

Gross carelessness is similar to recklessness. However, the standard does not consider the knowledge or intent of the taxpayer concerned, but rather whether a reasonable person would have known that there was a high chance that the action or inaction would have resulted in a tax shortfall.

Gross carelessness is not tax evasion because the taxpayer may not have the requisite criminal intent (mens rea) to evade. However, such action is more than negligence. Gross carelessness is "the doing of something which in fact involves a risk, whether the doer realises it or not, and the risk being such having regard to all the circumstances, that the taking of that risk would be described as 'gross carelessness'.

Example 1

Facts: A taxpayer started up a window cleaning business. She knows that her income from this venture is taxable and, after taking the advice of a tax agent, has set up a cash book system for recording the income and expenditure. However, over the year she has neglected on numerous occasions to record her income in the cash book. She could find the time to update her cash book if she was better organised, but felt that personal matters were more important.

At year end, before giving her records to the tax agent to prepare her income tax return, she makes a guess as to how much income she has earned and notes the cash book accordingly. As a result of an audit by Inland Revenue, it is ascertained that her income has been substantially understated.

Penalty: Although the taxpayer is aware that her business income is taxable, she has not kept sufficient records to accurately record the income. The result of not keeping complete records would have been foreseen by a reasonable person in this taxpayer's circumstances.

The taxpayer has demonstrated such a level of carelessness that it resulted in a high risk of her income being understated. This is a higher breach then failure to take reasonable care as there is clearly a complete disregard for the consequences. She would therefore be charged a 40% penalty for gross carelessness.

Note that the taxpayer has not intended to evade paying tax. She has consistently, over the year, neglected to take the necessary steps to ensure that the correct amount of income is returned.

Example 2

Facts: During the year a large company spent a substantial amount of money on renovations to part of its premises. At year end, the company's in-house tax accountant claimed all of the expenditure as deductible repairs and maintenance. The accountant was unsure whether all of the items were deductible for tax purposes, but did not bother to review the account to ascertain which items of expenditure were of a capital nature and therefore not deductible. As a result of an IRD audit, a substantial tax shortfall was revealed.

Penalty: Any reasonable person in this same situation would have analysed the repairs and expenditure account to ensure that capital items had not been claimed. In neglecting to do so, the company has shown complete disregard for the consequences. Therefore the penalty of 40% for gross carelessness is imposed.

The company had not intended to evade paying tax. However, the accountant neglected to take the necessary steps to ensure that the correct amount of income was returned. This is a more serious breach than not taking reasonable care.

Example 3

Facts: A company rents some space in a neighbouring warehouse as its existing premises are no longer adequate owing to the increase in business.

The owner of the company oversees the year end stock take, as he has done for many years. He forgets to include the stock held off premises. Before completing his records to give to his accountant, the manager recalls that his stock take figure is not correct. He is aware that he should have accurate figures available for the accountant but considers that he is too busy to take the time to check the stock held off-site. He makes a guess at the value of the stock in the other building and includes this in the total stock take figure. As a result of an IRD audit, a substantial tax shortfall which is caused by the inaccurate stock figures is ascertained.

Penalty: The taxpayer did not intentionally set out to underestimate his tax liability. However, he was grossly careless in not ensuring that the stock take figures were accurate. A reasonable person would have foreseen the results of inadequate attention to ensuring the accuracy of the stock take figures. He has displayed a high level of disregard for the consequences. Accordingly, a 40% penalty for gross carelessness is imposed.

Abusive tax position

Legislation

Section 141D introduces a penalty for abusive tax positions. A taxpayer who has a shortfall for a return period will be liable to pay a shortfall penalty for abusive tax position if all of the following apply:

- The tax shortfall exceeded $10,000.
- The tax position taken is an unacceptable interpretation.
- It has a dominant purpose of avoiding of tax.

The penalty payable is 100% of the resulting tax shortfall.

Purpose statement

The purpose statement is relatively new to tax law. It is intended to give the judiciary, taxpayers, tax advisers and Inland Revenue officers further guidance on what Parliament intended to achieve.

Section 141D(1) introduces the purpose statement for 'abusive tax positions'. It states:

> The purpose of this section is to penalise those taxpayers who, having applied an unacceptable interpretation to a tax law, have entered into or acted in respect of arrangements or interpreted or applied tax laws with a dominant purpose of taking, or of supporting the taking of, tax positions, that reduce or remove tax liabilities or give tax benefits.

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Discussion

The objective of an avoidance penalty is to deter taxpayers from entering into arrangements which have a dominant purpose of avoiding tax. Such arrangements are a risk to the revenue base. They may rely on literal interpretations of the law but abuse the law's intent.

It is intended that the penalty for abusive tax positions may apply not only when an anti-avoidance provision is invoked, but also when other provisions have been applied. This is important to ensure that identical conduct is not penalised differently solely because taxpayers are of different levels of sophistication or because Inland Revenue is not required to resort to an anti-avoidance provision.

Before a penalty for an abusive tax position can be imposed, three criteria must be met:

- The position taken must be an unacceptable interpretation.
- It must involve over $10,000 tax.
- There must be a dominant purpose of avoiding tax.

Unacceptable interpretation

The unacceptable interpretation standard will be applied to determine if a penalty is warranted. The standard recognises that there are many uncertainties in law and that more than one valid interpretation of that law is possible.

In determining whether an interpretation is unacceptable, all provisions of the relevant legislation, including the potential application of any general or specific anti-avoidance provisions, will be considered. Therefore, it can not be argued that a tax position or interpretation is acceptable in terms of a particular legislative provision irrespective of the operation of other provisions such as general anti-avoidance provisions. This is a scheme and purpose view of the tax legislation. (This is discussed under the section on Unacceptable Interpretation.)

Threshold

Section 141D(4) states:

> This section applies to a taxpayer only if - ...
> (b) The tax shortfall arising from the taxpayer's tax position exceeds $10,000.

Accordingly, this threshold differs from the threshold for an unacceptable interpretation. The 1% materiality threshold which applies to the "unacceptable interpretation" penalty does not apply to the "abusive tax position" penalty.

Dominant purpose of avoiding tax

Section 141D(7) states:

> For the purposes of this Part, an 'abusive tax position' means a tax position that, -...
> (b) Viewed objectively, the taxpayer takes -
> (i) In respect, or as a consequence, of an arrangement that is entered into with a dominant purpose of avoiding tax, whether directly or indirectly; or
> (ii) Where the tax position does not relate to an arrangement described in subparagraph (i), with a dominant purpose of avoiding tax, whether directly or indirectly."

Dominant purpose

The Act refers to a dominant "purpose". This differs from section BB 9 of the Income Tax Act 1994, which refers to "its purpose or effect is tax avoidance".

Inland Revenue considers that nothing turns on the distinction between "purpose or effect" and "purpose". In the context of section BB 9, case law certainly supports this view (*Tayles v Commissioner of Inland Revenue* [1982] 2 NZLR 726 ,734).

It could be considered that the term "purpose" is more of a "subjective" term than that of "effect", which is an objective term. However, the new legislation is explicit that the test of whether an arrangement has the dominant purpose of avoiding tax is an objective one[1]. It is also firmly established in case law that the purpose of an arrangement is to be argued objectively for section BB 9:

> Purpose is something to be decided not subjectively in terms of motive but objectively by reference to the arrangement itself[2].

> It is well established that the approach is objective not subjective; the taxpayer's motives are irrelevant, purpose and effect being gathered from the arrangement itself[3]:

Avoiding tax

The concept of "avoiding tax" encompasses the deferral of tax and the claiming of tax credits. Inland Revenue considers that "avoiding tax" would incorporate "tax avoidance" as defined in section OB 1 of the Income Tax Act 1994.

Facts to consider

The commentary to the bill states that:

> indicators of a dominant purpose of avoiding tax may include artificiality, contrivance, circularity of funding, concealment of information and non-availability of evidence, and spurious interpretations of tax laws.

Situations which do not involve anti-avoidance provisions

A taxpayer may be reassessed under a substantive provision of the Inland Revenue Acts rather than an anti-avoidance provision. This does not mean that the penalty for an abusive tax position cannot apply.

Section 141D(6) states:

> A taxpayer's tax position may be an abusive tax position if the tax position is an incorrect tax position under, or as a result of either or both of -

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1. "Abusive tax position" means a tax position that, viewed objectively, the taxpayer takes ... with a dominant purpose of avoiding tax, whether directly or indirectly.
2. Challenge v Commissioner of Inland Revenue [1986] 2 NZLR 513,533 (CA)
3. Hadlee v Commissioner of Inland Revenue [1989] 2 NZLR 447,466 (HC)

(a) A general tax law, or
(b) A specific or general anti-avoidance tax law.

The commentary to the bill stated

> The penalty for abusive tax positions will apply not only in situations where a general or specific anti-avoidance provision is invoked but also where other provisions have been applied. The need for the Commissioner to rely explicitly on an anti-avoidance provision does not necessarily indicate that the tax position is more deserving of a high penalty than an aggressive interpretation intended to avoid tax but which fails under another provision.

Accordingly, the penalty can apply even when an anti-avoidance provision has not been used.

Evasion or similar act

Legislation

Section 141E of the TAA imposes a penalty for evasion if a taxpayer takes any of the following actions:

- evades the assessment or payment of tax on his or her own behalf or on behalf of any another person
- knowingly applies or permits someone else to apply a deduction or withholding of tax which had to be paid to the Commissioner
- knowingly does not make a deduction or withholding of tax which had to be made;
- obtains a refund or payment of tax knowing that he or she is not lawfully entitled to the refund or payment
- enables another person to obtain a refund or payment of tax, knowing that the other person is not entitled to the refund or payment.

The penalty payable for evasion or similar act is 150% of the resulting tax shortfall.

Discussion

Wilful or knowing breach of an obligation is the most serious form of non-compliance. The civil penalty for tax evasion has been rewritten to apply generically to all revenue tax types.

Tax evasion involves a deliberate attempt to cheat the revenue. This may include a taxpayer obtaining refunds (tax credits, rebates) knowing that he or she is not lawfully entitled to them and knowingly not accounting for tax deductions to the Commissioner.

The category for "evasion or similar act" is not significantly different from the previous penal tax provision for evasion. The main difference lies in the standard of proof. The difference between the standard of "on balance of probabilities" and "beyond reasonable doubt", is explained under "Onus and standard of proof" on page 34 of this TIB.

Under section 149(5), if a shortfall penalty has been imposed on a taxpayer for taking an incorrect tax position, the Commissioner may not subsequently prosecute the taxpayer for taking the incorrect tax position. However, prosecution does not preclude the Commissioner from imposing the civil penalty for evasion.

Example 1

Facts: A salary and wage earner who enjoys working with cars has trained as a mechanic. In the evenings and on weekends he undertakes mechanical repairs for customers that he has gained through advertising in the local paper.

The taxpayer knows that the money he earns from his private business is taxable but he has no intention of returning the income. To this end, he asks his customers to pay him in cash. He puts this cash into a separate bank account under a false name. At year end, he prepares his income tax return omitting all mention of his income earned from his mechanical repair business.

Penalty: This taxpayer deliberately attempted to cheat the revenue. He is fully aware that this income is taxable and has taken steps to conceal the income from Inland Revenue. Penalty of 150% for tax evasion is imposed. In addition, he is liable to prosecution for knowingly making a false return with the intention to evade tax. However, prosecution must be taken before a shortfall penalty is imposed.

Example 2

Facts: A taxpayer owns a business which mainly has cash sales. During the year he took $100 per week from the till for personal use. He banked the remainder in the business bank account.

The taxpayer's accountant prepares his income tax returns. At year end the taxpayer told his accountant that all the money earned from the business was deposited into the business bank account and none was taken for private use. The taxpayer knew that his income would be understated in his tax return.

Penalty: The taxpayer deliberately lied to his accountant to get his income understated and his tax liability reduced. He is liable for a penalty of 150% for tax evasion. In addition, he is liable to prosecution for knowingly filing a false return with the intention of evading tax. However, prosecution must be taken before a shortfall penalty is imposed.

Example 3

Facts: The taxpayer operates a small business. During the year he has materials and goods delivered to his home. He falsifies details on the invoices to show the delivery details to be his business premises and claims the expenditure as deductible for tax purposes.

Inland Revenue undertakes an investigation and the auditor confirms that the expenditure claimed using the altered invoices was private expenditure.

Penalty: The taxpayer has deliberately altered invoices to make them appear to be for business expenditure. He is liable to the 150% penalty for

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evasion. He is also liable to prosecution for knowingly making a false return with the intention to evade tax. However, prosecution must be taken before a shortfall penalty is imposed.

Officers liable to pay amounts equal to shortfall penalties

Legislation

Section 141F of the TAA deals with cases involving tax deductions and withholding payments. It provides that officers may be liable to pay a shortfall penalty equal to that which could be incurred by their employer if:

- the law requires the employer to deduct or withhold tax and pay it to the Commissioner,
- an officer of the employer fails to deduct or withhold the tax, or applies or permits the tax to be used for anything other than payment to the Commissioner.

Discussion

Section 194 previously imposed penal tax upon an employer *or any other person* who knowingly permitted a deduction to be applied in any way other than to the Commissioner. This section is now repealed.

Section 141F replaces the previous provision and allows a shortfall penalty to be imposed upon the officer responsible. The shortfall penalty imposed would be equal to that which could have been imposed on the taxpayer.

Accordingly, the Commissioner has not changed the policy on this offence. It is clear that the person who failed to make and/or account for the deductions would have had to do so knowing that the deductions were to be made or accounted for to the Commissioner.

This would usually be a person in a responsible position within the company, such as a director or secretary. It would be very unlikely that a person in a clerical position, merely following instructions from a senior officer, would be accountable for the penalty.

Factors affecting level of penalty imposed

The amount of shortfall penalty may be adjusted for the following reasons:

- voluntary disclosure before or during an audit
- disclosure of an unacceptable interpretation at time of filing the return
- self-amended returns
- obstruction of an Inland Revenue officer during an investigation
- temporary shortfall

Voluntary disclosure

There are two areas of voluntary disclosure:

- voluntary disclosure before notification of an audit
- voluntary disclosure after notification of an audit.

Legislation

Section 141G provides that a shortfall penalty imposed on a taxpayer under sections 141A to 141E may be reduced if the taxpayer makes a full voluntary disclosure of all details relating to the tax shortfall. The disclosure must be made either before the taxpayer receives the first notice that an audit or investigation is to be undertaken, or after the first notification but before the audit or investigation starts. The Commissioner may at any time specify the information required for a full voluntary disclosure and advise the form in which it must be provided

The level by which the shortfall penalty is reduced is:

- for pre-notification disclosure - 75%
- for post-notification disclosure - 40%

Discussion

Disclosure before notification of an audit

The fixed rate for shortfall penalties will be reduced by 75% (reflecting a minimum penalty of 5% for breaches) for full voluntary disclosure before notification of an audit. The reduced penalty for voluntary disclosure before an audit will apply if the disclosure is made before the taxpayer is first notified of a pending tax audit or investigation. This follows similar procedures already in practice.

Notification of a pending audit or investigation will be the date of the written confirmation advising the start of the audit or investigation.

In the case of registration checks and other unannounced visits, the date of first contact with the taxpayer will be the date of notification.

If an investigator is carrying out an audit of one revenue and the taxpayer discloses a discrepancy in another revenue, and the taxpayer has not been notified that the other revenue was going to be audited, then the taxpayer will qualify for the voluntary disclosure before notification of an audit.

Disclosure after notification of an audit

A 40 percent shortfall penalty reduction is available for disclosure made after notification of an audit. This reduction will apply if the disclosure is made after the taxpayer is notified of a pending tax audit or investigation, but before the start of the audit or investigation.

Subsection (4) provides that a taxpayer has been notified of a pending audit or investigation if any of the following persons have received notification:

- the taxpayer
- an officer of the taxpayer
- a shareholder of the taxpayer (for close companies)
- a tax adviser acting for the taxpayer
- a partner in a partnership
- a person acting for, or on behalf of, or as a fiduciary of the taxpayer.

Subsection (5) states that a tax audit or investigation starts at the earlier of:

1. the end of the first interview an Inland Revenue officer has with either the taxpayer or the taxpayer's representative, after the taxpayer receives the notice.
2. the time when:
   - an Inland Revenue officer inspects the taxpayer's information (including books or records) after the taxpayer receives notice; and
   - the taxpayer is notified of the inspection.

Any disclosure made by a taxpayer during an unannounced visit would be a disclosure made after notification of an audit and a 40% reduction in the shortfall penalty will be allowed.

Disclosure by a subsidiary of a company

An audit of a parent company, or a subsidiary of that company, may necessitate the audit of other subsidiaries in the group. In such cases, disclosure would depend upon which entity had been notified. If the parent company had received notification that the audit was restricted to that entity, then any disclosure made by the subsidiary is voluntary disclosure before notification of an audit. However, if another company in the group has been notified that the audit is being extended, any disclosure made by that other company would be considered a disclosure after notification of an audit.

When a company has a branch or branches, they are considered to have been notified at the same time as the company, as they are part of the company, not separate entities.

Methods of making a voluntary disclosure

A voluntary disclosure can be made by either visiting, telephoning or writing to Inland Revenue. In addition, specified forms for voluntary disclosure are available from Inland Revenue.

Adequate disclosure

Disclosure must be full and complete. This does not mean disclosing the discrepancies to the last dollar, but does require providing enough information to enable the Commissioner to make an assessment.

It is not up to the Commissioner to elicit the required information from the taxpayer. It is the taxpayer's responsibility to have the necessary accounts and returns prepared.

If a taxpayer is not able to make a full disclosure at the first point of contact with Inland Revenue, he or she may still make the disclosure and advise the Commissioner when the remaining information will be provided. A time limit will be imposed for providing the remaining information.

To satisfy full and complete disclosure, the following minimum details must be provided:

- taxpayer's details (name, trade name, IRD number, address, date of birth, contact telephone and contact times)
- an explanation as to why the errors or omissions occurred
- enough information to enable an assessment to be made
- a declaration and signature by taxpayer.

Section 146(2) states that the Commissioner must not publish the names of taxpayers who make a voluntary disclosure before notification of an audit, if they give *complete information and full particulars* of:

- the relevant offence; or
- their tax position giving rise to the relevant shortfall penalty.

In addition, a taxpayer who makes a voluntary disclosure will not be prosecuted.

Self-amended returns

Self-amended returns will be treated as a form of voluntary disclosure if they are made before notification of an audit. Accordingly, if the tax shortfall being amended is due to a culpable act, the taxpayer will receive a reduced penalty in accordance with a voluntary disclosure made before notification of an audit.

If a self-amended return is made after notification of an audit but before the start of the audit the taxpayer must provide sufficient details, as is required for voluntary disclosure after notification of an audit, before the amended return will be treated as a voluntary disclosure and any reduction made to the shortfall penalty.

If a taxpayer files an amended return after the audit has already started, it will not be treated as a form of voluntary disclosure.

For income tax purposes, if an amended return is made before the earlier of the issuing of an assessment for the tax or the due date for payment of the tax, no penalty will be imposed as there will be no tax shortfall.

In addition, if a tax shortfall is corrected in a later return period from that in which the original tax position was taken and before notification of an audit, it will be treated as a temporary tax shortfall. Temporary tax shortfalls are discussed later.

Disclosure at time of filing

Legislation

Section 141H provides that:

- A shortfall penalty payable by a taxpayer for having an unacceptable interpretation or having taken an abusive tax position may be reduced if adequate disclosure of the tax position is made at the time of filing the tax return.
- The level by which a shortfall penalty is to be reduced for adequate disclosure is 75%.
- The Commissioner may at any time specify the type of information required for adequate disclosure and the form in which the information must be provided.

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Discussion

A taxpayer can disclose the tax position taken in his or her tax return at the time of filing. Provided the disclosure is adequate and the position taken is not frivolous, the taxpayer would be eligible for a reduced penalty if the position is later found to be an unacceptable interpretation.

For disclosure to be effective, the taxpayer must provide full and relevant arguments for the tax position taken. The level by which a shortfall penalty is to be reduced for adequate disclosure at the time of filing is 75%.

Adequate disclosure at time of filing

Section 141H(3) states that the Commissioner may from time to time specify the type of information required for adequate disclosure.

Disclosure must be made on a specified form. The following information will be required in order to satisfy the requirement of adequate disclosure:

- taxpayer's details (name, trade name, IRD number, address, date of birth, contact telephone and contact times)
- overview of the position taken
- interpretation of case law on the subject, contents of any tax opinions, legal articles and related material
- any relevant Inland Revenue public ruling
- a calculation, if necessary, to show the position and how it was arrived at
- a declaration and signature by taxpayer.

The disclosure form must be filed with the return in which the particular tax position has been taken.

E-File

If the tax return is filed electronically, the specified form will need to be sent to Inland Revenue separately.

Obstruction

Legislation

The new penalty provisions contain both a civil penalty and criminal penalty for obstruction. Section 141K provides for the civil penalty for obstruction as follows:

(1) A shortfall penalty payable by the taxpayer under any of sections 141A to 141E may be increased by the Commissioner if the taxpayer obstructs the Commissioner in determining the correct tax position in respect of the taxpayer's tax liabilities.

(2) The level by which a shortfall penalty may be increased for obstruction is 25%.

Section 143H provides for the criminal penalty for obstruction as follows:

(1) A person who obstructs the Commissioner or an officer of the Department acting in the lawful discharge of the duties or in the exercise of the Commissioner's or officer's powers under a tax law commits an offence against this Act.

(2) A person who is convicted of an offence under subsection (1) is liable—

(a) The first time the person is convicted of that type of offence, to a fine not exceeding $25,000; and

(b) on every other occasion the person is convicted of the same type of offence, to a fine not exceeding $50,000.

Discussion

Taxpayers must co-operate with Inland Revenue, to the extent required by the tax laws, in providing information and facilitating investigations. Obstruction is a term used to describe situations in which a taxpayer takes steps to prevent the Commissioner from discovering part or all of the deficient tax in an audit.

Differences between civil obstruction and criminal obstruction

For both civil and criminal obstruction the onus of proof rests with the Commissioner. However, the standard of proof varies.

The standard of proof for civil obstruction is the civil standard of "on balance of probabilities". This requires the Commissioner to show that it was more than probable that the event occurred. The standard of proof for criminal obstruction is "beyond reasonable doubt".

In addition, the civil penalty for obstruction can be applied only if there is a tax shortfall, but a tax shortfall is not necessary for the criminal sanction.

Meaning of obstruction

The New Shorter Oxford English Dictionary definition of obstruction is:

The action or an act of obstructing something or someone; the condition of being obstructed; the action of impeding the movement of traffic on a highway. A thing impeding or preventing passage or progress; an obstacle, a blockage

Case law

In *Urlich v Police* (1989) 4 CRNZ 144: "the ordinary meaning of "obstruct" is to impede or to make more difficult....."

Accordingly, obstruction occurs when the action or actions make it more difficult for the Commissioner or officer to carry out their lawful duties.

Obstruction does not require physical use. In *Urlich* v *Police* it was found that "there is no reason why words alone, provided they are uttered in circumstances under which they can be believed, cannot amount to obstruction."

Before obstruction can constitute an offence, the conduct must be without justification and lawful excuse. This was discussed in the following cases:

- *Goldsmith* v *Police* (1993) 10 CRNZ 106: "The conduct must be obstructive and without justification or lawful excuse."
- *Police* v *Hardaker* [1959]: "Once a prima facie case of obstruction is made out against a defendant, the onus lies on him to satisfy the Court that his conduct was with lawful justification or excuse."

- *Stewart* v *Police* [1961] NZLR 680: "The appellant in evidence gave no reason for his decision to do what he, in fact, did. He might, for example, have given evidence of some reasonable excuse such as sudden illness or the like."

Accordingly, it is clear from case law that two factors must be present before a penalty can be imposed for obstruction. First, the conduct must be obstructive and second, it must be without justification or lawful excuse.

Actions that are not obstruction

A taxpayer is entitled to:

- exercise legal rights (Accordingly, obstruction does not include asserting the right to legal privilege.)
- contest an assessment (The obstruction offences are not intended to discourage taxpayers from using legal processes in the course of any disagreement with Inland Revenue.)
- maintain an opinion contrary to that of Inland Revenue.

Examples of obstruction

Examples may include:

- refusing reasonable access to business premises
- destroying relevant records
- successful prosecution of a taxpayer for a section 17 offence of failing to provide records or information requested
- lying at an interview
- falsifying details in a statement of assets and liabilities (IR 110)
- deliberate delay by the taxpayer to frustrate Inland Revenue enquiries.

Agents and other third parties

The civil penalty for obstruction will not apply to agents and third parties. For example, when an agent obstructs an Inland Revenue officer, the civil penalty for obstruction cannot be applied, as it must be the taxpayer who obstructs and there must be a resulting tax shortfall.

If agents and third parties obstruct, the criminal offence of obstruction may be used, resulting in prosecution and possible fines.

Temporary shortfalls

Legislation

Section 141I deals with temporary shortfalls. A tax shortfall is a temporary tax shortfall if all of these conditions are met:

- It has been permanently reversed or corrected in an earlier or later return period, so that the taxpayer pays the correct amount of tax or calculates and returns the correct tax liability.
- No tax shortfall will arise in a later return period for a similar item or matter.
- No arrangement exists in any return period which has the purpose or effect of creating a further related tax deferral or advantage.
- The tax shortfall was permanently reversed or corrected before the taxpayer was first notified of a pending tax audit or investigation.

If a shortfall is temporary the shortfall penalty must be reduced; it will be 75% of the penalty that would otherwise apply.

Discussion

This section is restricted to tax shortfalls which have been permanently reversed or corrected in a return period before notification of an audit or investigation.

The definition applies provided that no arrangement exists in any return period which has the purpose or effect of creating a further related tax deferral or advantage.

Example

A property developer enters into an unconditional sale and purchase contract to sell a townhouse. The purchaser pays a deposit to the property developer on 1 June 1997, with the balance being due when the purchaser takes actual possession of the townhouse three months later.

The property developer is registered for GST on an invoice basis and files two-monthly GST returns.

She returns the amount of the deposit received in the GST return for the period ended 30 June and the balance of the sale price in the GST return for the period ended 31 October.

However, the time of supply took place when the contract became unconditional and the deposit was received, so she must return the entire amount of the sale price in the GST period ended 30 June. This results in a tax shortfall of $15,000.

As the matter relates to an issue of interpretation and the amount is over the specified threshold, she must have an acceptable interpretation for the position taken. Assuming that she doesn't have an acceptable interpretation, she would be liable to a shortfall penalty of 20% of the tax shortfall.

However, the tax shortfall qualifies as a temporary shortfall because it has been corrected in a later return period before an audit and there is no arrangement to reverse the correction out in a later period. Accordingly, the shortfall penalty imposed would be 5%.

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Limit to reduction

Legislation

Section 141J sets out the limit on reducing a shortfall penalty. When a taxpayer who is liable to a shortfall penalty makes a voluntary disclosure, and the penalty is for a temporary tax shortfall, the shortfall penalty will be reduced only once. This means the total reduction will be 75%.

Discussion

Taxpayers may make a voluntary disclosure of a temporary shortfall.

The fixed rate for shortfall penalties will be reduced by 75% for voluntary disclosures made before notification of any pending tax audit or investigation. This reduction is consistent with the reduction offered when the tax shortfall is temporary.

However, a taxpayer will not receive a reduction for both a temporary shortfall and voluntary disclosure before an audit. In such a case the total penalty reduction will still be 75%.

Disputes resolution

A taxpayer has the right to disagree with the Commissioner's decision to impose shortfall penalties.

The Commissioner will raise the issue of shortfall penalties as soon as practicable, which in most cases will be at the time the substantive issues are being discussed. A Notice of Proposed Adjustment (NOPA) will be issued before any assessment or adjustment of shortfall penalties unless there is full agreement with the taxpayer before the issue of the NOPA or a court has directed the adjustment.

If the taxpayer cannot resolve the issues in the NOPA with the Inland Revenue officer who initially dealt with the case, the matter will be referred to Inland Revenue's Adjudication Unit for further consideration before any assessments are issued.

A taxpayer who still disagrees with the assessment has the normal rights of review through the courts.

Calculating shortfall penalties

Legislation

Section 141 deals with calculating tax shortfalls. Here is a summary of its provisions:

- A tax shortfall is calculated each time a taxpayer is liable to pay a shortfall penalty.
- A separate tax shortfall calculation is required for each return period and for each tax type.
- Each tax deemed to be another tax is a separate tax type.
- The tax shortfalls in the return will be calculated taking any overstatement into account on a pro rata basis.
- If a debit adjustment in a tax type (return) results in a corresponding credit adjustment in another tax type (return) for the same return period, the credit will be offset against the debit for the purposes of calculating the tax shortfall.
- If a debit adjustment is made to a taxpayer's return and that adjustment causes a corresponding credit adjustment in an associated person's return for the same return period, the resulting refund or increased refund will be offset against the debit.
- The Commissioner may treat companies in a wholly-owned group as a single taxpayer when determining a tax shortfall.
- If two tax types have different return periods (for example, income tax and GST), the Commissioner may treat one of the tax types as having the same return period as the other.
- Similar or identical tax shortfalls will be aggregated and deemed to be one tax shortfall.
- If an adjustment to a return increases the taxpayer's assessable income under section EC 1 of the Income Tax Act 1994, and the taxpayer elects to allocate that increased income to the year of adjustment and any other income year, the total tax shortfall will be computed for the year of adjustment when calculating the penalty.
- The tax effect of a tax position taken by a taxpayer in a return period is to be calculated using the taxpayer's marginal tax rates for that return period.
- If a taxpayer has no tax to pay in the return period, the rate of tax that would apply is the lowest marginal rate that would apply to the return period if the taxpayer did have tax to pay.
- For the purposes of this section, "tax" does not include a civil penalty.

Discussion

Before a shortfall penalty can be imposed, there must be a tax shortfall. In calculating this shortfall, adjustments will be offset between wholly-owned group companies and associated persons, and within the same tax type on a return basis.

This section also provides that offsets will be allowed across different tax types if these two conditions are met:

- An adjustment to one tax type has a direct effect on another tax type.
- The effect on the other tax type results in a credit available to be refunded.

The amount of the offset will be the lesser of the amount of the refund and the credit available as a direct result of the adjustment.

Taxpayers in a loss situation will still be subject to shortfall penalties, but they may elect to pay those penalties by offsetting an equivalent amount of tax losses in accordance with section IG 9A of the Income Tax Act 1994. To calculate the equivalent amount of tax losses, the lowest marginal tax rates are used.

Example

An individual taxpayer files a tax return which shows tax losses of $20,000. An audit of the taxpayer establishes that a deduction of $10,000 was not deductible for tax purposes, so there is a tax shortfall of $2,400. A penalty of $480 for lack of reasonable care is imposed, being 20% of the tax shortfall.

The taxpayer still has $10,000 losses available, so he may elect to use some of these losses to pay the shortfall penalty of $480. The taxpayer would need to forfeit $2,000 of losses. ($480 ÷ 0.24 = $2,000). 0.24 is the lowest marginal tax rate that applies - 24 cents in the dollar.

A taxpayer who has no losses carried forward from prior years, but who expects to have losses in the current year, can elect to use those losses, even though the final determination of the losses for that current year has not been established.

Section IG 9A(2) provides that if the taxpayer does incur sufficient losses for that current income tax year, then the shortfall penalties will be deemed to have been paid by the due date. However, if at the end of the income year the taxpayer does not incur sufficient losses, late payment penalties and interest will be imposed on the tax shortfall penalty that should have been absorbed by the losses.

A tax shortfall may result in adjustments across varying tax types, which are likely to have different return periods. In such cases, the Commissioner may deem one tax type to have the same return period as another. An example would be when a taxpayer's income tax return period ends on 31 March, and the GST period spanning that date is 1 March to 30 April. In this case, the Commissioner may decide to treat both tax types as having the 31 March return period.

The two examples that follow demonstrate how the penalty offset applies. The shortfall penalty categories used in these examples have been applied for calculation purposes only.

Example 1

This example includes calculations for shortfall penalties, late payment penalties and interest.

A taxpayer is audited as follows:

- Income tax - year ended 31 March 1998
- GST - 6 two-monthly periods from the period ended 31 May 1997
- FBT - four quarters from the quarter ended 30 June 1997

Several shortfalls were found in all three revenues.

Because of the interrelationship between GST and income tax, and between FBT and income tax, a credit adjustment occurred in the income tax calculation.

In the following calculations, the shortfalls have been converted into tax shortfalls.

Shortfall penalties

Income tax

The following income tax shortfalls attract shortfall penalties:

Gross carelessness	$12,339.36	4%	40%	$4,834.73
Lack of reasonable care	$36,442.79	12%	20%	$7,252.10
Lack of reasonable care - temporary shortfall[4]	$259,247.34	84%	5%	$12,691.17
Total	$308,029.49			$24,778.00
Less adjustments for GST and FBT assessed	($5,858.64)			
Tax shortfall	$302,170.85			

[1] Calculating tax shortfall: any credits that became available to the taxpayer as a result of the audit must be taken into account. Therefore the tax shortfall equals the total tax discrepancy less the tax value of any credits ascertained.

[2] Calculating percentage of total: percentage of total is calculated on the total tax discrepancy before the credit adjustments are deducted as follows:

12,339.36 ÷ 308,029.49 = 4%
36,442.79 ÷ 308,029.49 = 12%
259,247.34 ÷ 308,029.49 = 84%

[3] Calculating the penalty: to calculate the total, the adjusted tax shortfall is used [as the denominator] to obtain the amount of penalty attributed to each tax shortfall:

302,170.85 x 4% = 12,086.83 x 40%	=	4,834.73
302,170.85 x 12% = 36,260.50 x 20%	=	7,252.10
302,170.85 x 84% = 253,823.51 x 5%	=	12,691.17
Total shortfall penalty	=	24,778.00

[4] Calculating temporary shortfall: Penalty rate for temporary shortfall is 75% of the standard rate for a culpable act. In this example there is a penalty for lack of reasonable care, but the tax shortfall was temporary. The lack of reasonable care penalty (20%) is therefore reduced to 5%.

Goods and services tax

The taxpayer did not take reasonable care in calculating the GST liability, so there is a 20% shortfall penalty. The following tax shortfalls were established:

31 May 1997	$3,379.57	20%	$675.91
31 Jul 1997	$3,379.57	20%	$675.91
30 Sept 1997	$3,379.57	20%	$675.91
31 Oct 1997	$3,379.57	20%	$675.91
31 Jan 1998	$3,379.57	20%	$675.91
31 Mar 1998	$3,379.57	20%	$675.91
Total	$20,277.42		$4,055.46

Fringe benefit tax

The taxpayer did not take reasonable care in calculating the FBT liability, so there is a 20% shortfall penalty. The following tax shortfalls were established:

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30 Jun 1997	$12,722.06	20%	$2,544.41
30 Sept 1997	$12,722.06	20%	$2,544.41
31 Dec 1997	$12,722.06	20%	$2,544.41
31 Mar 1998	$12,722.06	20%	$2,544.41
Total	$50,888.24		$10,177.64

Summary of shortfall penalties

Total shortfall penalties incurred by the taxpayer are as follows:

Income tax	$24,788.00
Goods and services tax	$4,055.48
Fringe benefit tax	$10,177.64
Total	$39,011.12

Late payment penalties

Income tax

Amount of tax shortfall	$302,170.85
Amount of shortfall penalty	$24,778.00

The original due date for the 1998 income tax period is 7 February 1999. The amended notice of assessment is dated 30 November 1999, and it sets a new due date of 30 January 2000.

Assuming that, as at 15 April 2000, the taxpayer has not paid the tax shortfall or the shortfall penalties, the late payment penalty would be calculated as follows:

30/11/99	Shortfall	$302,170.85	$302,170.85
30/11/99	Shortfall penalty	$24,778.00	$326,948.85
31/1/2000	5% LPP	$16,347.44	$343,296.29
28/2/2000	2% LPP	$6,865.92	$350,162.21
31/3/2000	2% LPP	$7,003.24	$357,165.45

Goods and services tax

For this example, late payment penalty has been calculated for the period ended 31 May 1997 only. The calculations for other periods are similar.

Tax shortfall attributed to each period	$3,379.57
Shortfall penalty attributed to each period	$675.91

The amended notice of assessment is dated 30 November 1999, and it sets a new due date of 30 January 2000.

Assuming that, as at 15 April 2000, the taxpayer has not paid the tax shortfall or the shortfall penalties, the late payment penalty is calculated as follows:

30/11/99	Shortfall	$3,379.57	$3,379.57
30/11/99	Shortfall penalty	$675.91	$4,055.48
31/1/2000	5% LPP	$202.77	$4,258.25
28/2/2000	2% LPP	$85.16	$4,343.41
31/3/2000	2% LPP	$86.86	$4,430.27

Fringe benefit tax

In this example the FBT shortfall and associated shortfall penalties were paid by the new due date of 30 January 2000. Accordingly, no late payment penalties would be imposed.

Interest

Income tax

Interest will be calculated from the time the tax shortfall was originally due (7 February 1999) until the date of the amended Notice of Assessment (30 November 1999) - a total of 296 days.

The amount of interest shown on the amended notice of assessment would be as follows:

$$\$302{,}170.85 \times \frac{296}{365} \times 12\% = \$29{,}405.77$$

In this example the taxpayer was allowed two months in which to pay the tax shortfall, interest and penalties. The taxpayer did not pay within this time so interest continues to accrue from the date the amended Notice of Assessment is issued (30 November 1999) to the date payment is made. Calculations for the various periods are as follows:

- 1 December 1999 to 30 January 2000 (61 days):

  $$\$302{,}170.85 \times \frac{61}{365} \times 12\% = \$6{,}059.97$$

- 1 January 2000 to 27 February 2000 (28 days):

  $$\$334{,}296.29 \times \frac{28}{365} \times 12\% = \$3{,}160.21$$

- 28 February 2000 to 30 March 2000 (31 days):

  $$\$350{,}162.21 \times \frac{31}{365} \times 12\% = \$3{,}568.78$$

- 31 March 2000 to 15 April 2000 (16 days):

  $$\$357{,}165.45 \times \frac{16}{365} \times 12\% = \$1{,}878.79$$

Therefore total interest calculated would be as follows:

7 February 1999 to 30 November 1999	$29,405.77
1 December 1999 to 30 January 2000	$6,059.97
31 January 2000 to 27 February 2000	$3,160.21
28 February 2000 to 30 March 2000	$3,568.78
31 March 2000 to 15 April 2000	$1,878.79
Total	$44,073.52

The taxpayer's statement of account issued on 15 April 2000 would look like this:

30/11/99	Shortfall	$302,170.85	$302,170.85
30/11/99	Shortfall penalty	$24,778.00	$326,948.85
31/1/2000	5% LPP	$16,347.44	$343,296.29
28/2/2000	2% LPP	$6,865.92	$350,162.21
31/3/2000	2% LPP	$7,003.24	$357,165.45
15/4/2000	Interest	$44,073.52	$401,238.97

Goods and services tax

Interest is calculated on each period up to the date of the amended notice of assessment as follows:

- For the period ended 31 May 1997 the original due date was 30 June 1997. From 1 July 1997 to 30 November 1999 is 883 days.

  $$\$3{,}379.57 \times \frac{883}{365} \times 12\% = \$\ 981.09$$

– For the period ended 31 July 1997 the original due date was 31 August 1997. From 1 September 1997 to 30 November 1999 is 821 days.

$\$3,379.57 \times \frac{821}{365} \times 12\% = \$\,912.20$

– For the period ended 30 September 1997 the original due date was 31 October 1997. From 1 November 1997 to 30 November 1999 is 760 days.

$\$3,379.57 \times \frac{760}{365} \times 12\% = \$\,844.42$

– For the period ended 30 November 1997 the original due date was 15 January 1998. From 16 January 1998 to 30 November 1999 is 684 days.

$\$3,379.57 \times \frac{684}{365} \times 12\% = \$\,759.98$

– For the period ended 31 January 1998 the original due date was 28 February 1998. From 1 March 1998 to 30 November 1999 is 640 days.

$\$3,379.57 \times \frac{640}{365} \times 12\% = \$\,711.09$

– For the period ended 31 March 1998 the original due date was 30 April 1998. From 1 May 1998 to 30 November 1999 is 579 days.

$\$3,379.57 \times \frac{579}{365} \times 12\% = \$643.32$

Total interest = $4,852.10

For this example, further interest has been calculated on the period ended 31 May 1997 only. The calculations for other periods are similar.

The taxpayer's Notice of Assessment was issued on 30 November 1997, and allowed the taxpayer until 30 January 1998 to pay the tax shortfall, interest and penalties. However, the taxpayer did not pay until 15 April 2000, so interest continued to accrue from the date of the amended notice of assessment (30 November 1999) until the date payment is made. The calculations are as follows:

– 1 December 1999 - 30 January 2000 (61 days):

$\$3,379.57 \times \frac{61}{365} \times 12\% = \$67.77$

– 31 January 2000 - 27 February 2000 (28 days):

$\$4,258.25 \times \frac{28}{365} \times 12\% = \$39.20$

– 28 February 2000 - 30 March 2000 (31 days):

$\$4,343.25 \times \frac{31}{365} \times 12\% = \$44.26$

– 31 March 2000 - 15 April 2000 (16 days):

$\$4,430.27 \times \frac{16}{365} \times 12\% = \$23.30$

Therefore total interest calculated for the period ended 31 May 1997 would be as follows:

30 June 1997 to 30 November 1999	$ 981.09
1 December 1999 to 30 January 2000	$67.77
31 January 2000 to 27 February 2000	$39.20
28 February 2000 to 30 March 2000	$44.26
31 March 2000 to 15 April 2000	$23.30
Total	$1,155.62

The taxpayer's statement of account for the May 1997 period will look like this:

15/4/2000	Interest	$44,073.52	$401,238.97
30/11/99	Shortfall	$3,379.57	$3,379.57
30/11/99	Shortfall penalty	$675.91	$4,055.48
31/1/2000	5 % LPP	$202.77	$4,258.25
28/2/2000	2 % LPP	$85.16	$4,343.41
31/3/2000	2 % LPP	$86.86	$4,430.27
15/4/2000	Interest	$1,155.62	$5,585.89

Fringe benefit tax

The calculation that applied for GST will also apply to each FBT quarter. Interest will be calculated on each quarterly shortfall from the date the tax was originally due to the date of the amended notice of assessment, and then on the account balance including shortfall penalty and late payment penalty (but not on any previous interest charged) through to the date of payment.

Only interest has been calculated in this case.

Shortfall attributed to each quarter = $12,722.06

Interest calculated on each period up to the date of the amended notice assessment is as follows:

– Period ended 30 June 1997 (original due date 20 July 1997). From 21 July 1997 to 30 November 1999 = 863 days.

$\$12,722.06 \times \frac{863}{365} \times 12\% = \$3,609.57$

– Period ended 30 September 1997 (original due date 20 October 1997). From 21 October 1997 to 30 November 1999 = 771 days.

$\$12,722.06 \times \frac{771}{365} \times 12\% = \$3,224.78$

– Period ended 31 December 1997 (original due date 20 January 1998). From 21 January 1998 to 30 November 1999 = 679 days.

$\$12,722.06 \times \frac{679}{365} \times 12\% = \$2,839.98$

– Period ended 31 March 1998 (original due date 20 April 1998). From 21 April 1998 to 30 November 1999 = 589 days.

$\$12,722.06 \times \frac{589}{365} \times 12\% = \$2,463.54$

Total interest = 12,137.87

In this example the FBT shortfall and related shortfall penalties were paid by the new due date of 30 January 2000. Accordingly, no further interest is accrued.

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Example 2

This example involves a partnership consisting of two 50/50 partners who also run a company. The partners are the company shareholders, and they do all of their own day to day accounting. At the end of the year they give their paperwork to their accountant.

During the year end meeting with the accountant, the partners neglected to advise the accountant that they sometimes pay personal accounts through the company. The accountant assumed that all accounts paid were company expenses.

Inland Revenue audited both the company and the partnership.

Company

The audit covered the income tax return periods ended 31 March 1998, 31 March 1999 and 31 March 2000. A number of discrepancies were ascertained and culpability has been considered.

In the years ended 31 March 1999 and 2000, the taxpayer incurred shortfalls for which Inland Revenue considered shortfall penalties were warranted. However, as a result of the audit, credits were ascertained in those years which reduced the tax shortfall to a negative amount. As a result no penalty was imposed for those years.

In the following example, the shortfall has been converted into a tax shortfall.

31.3.98			
Lack of reasonable care	$6,814	20%	$1,362.80
31.3.99			
Lack of reasonable care	$5,608		Nil
Less cr. adjustments	($20,428)		
Tax shortfall	($14,820)		
31.3.2000			
Lack of reasonable care	$4,000		Nil
Unacceptable interpretation	11,367		Nil
Less cr.adjustments	($17,615)		
Tax shortfall	($2,248)		

Partnership

During the audit of the partnership for the return periods ended 31 March 1999 and 2000, shortfalls were ascertained and penalties imposed. The partnership return for the year ended 31 March 1998 did not require reassessment, but the partners incurred a 1998 shortfall each as a result of the audit of their company.

As the partnership is not assessed with tax, the shortfall is allocated to the partners in their respective percentages and at their respective tax rates.

Therefore, after considering the culpability resulting from the partnership shortfall, the amount of shortfall is then allocated to the partners and the tax shortfall ascertained. Shortfall penalties are then imposed on the individual partners based on each individual partner's tax shortfall.

As a result of the audit of the partnership the following shortfalls have been ascertained and are liable to penalty:

Year ended 31 March 1999

Lack of reasonable care:
The partnership shortfall ascertained is $2,955, so the share of shortfall allocated to each partner is $1,477.50 (50% of total shortfall).

Year ended 31 March 2000

Lack of reasonable care:
The partnership shortfall ascertained is $23,140, so the share of shortfall allocated to each partner is $11,570 (50% of total shortfall).

Unacceptable interpretation[5]:
The partnership shortfall ascertained is $33,634, so the share of shortfall allocated to each partner is $16,817.

Individual partners

As a direct result of the audit of the company and partnership the partners have incurred tax shortfalls. The shortfalls arose due to the assessing of deemed dividends to the partners in their respective returns. The partners are liable to penalty as follows:

Note: for the purpose of the exercise, tax shortfall is calculated at a rate of 33%.

Year ended 31 March 1998

Lack of reasonable care:
The total deemed dividend allocated to each partner as a result of company audit is $3,407 (50% of deemed dividends disallowed). The tax shortfall allocated to each partner is therefore $1,124.31

Year ended 31 March 1999

Lack of reasonable care:
The total deemed dividend allocated to each partner as a result of company audit is $2,804 (50% of deemed dividends disallowed). The tax shortfall allocated to each partner is therefore $925.32.

Lack of reasonable care:
The partnership shortfall ascertained is $2,954. The share of shortfall allocated to each partner is therefore $1,477 (50% of total shortfall). This means each partner's tax shortfall is $487.41.

[5] When determining whether the shortfall breaches the threshold for requiring an acceptable interpretation, the figure used is the shortfall in the partnership return, not the amount allocated to the original partners.

Year ended 31 March 2000

Lack of reasonable care:
The total deemed dividend allocated to each partner as a result of company audit is $2,000 (50% of deemed dividend disallowed). Tax shortfall allocated to each partner is therefore $660.

Lack of reasonable care:
The partnership shortfall ascertained is $23,140. The share of shortfall allocated to each partner is therefore $11,570 (50% of total shortfall), and each partner's tax shortfall is $3,818.10

Unacceptable interpretation:
The partnership shortfall ascertained is $33,634. The share of shortfall allocated to each partner is therefore $16,817. Each partner's tax shortfall is $5,549.61.

Penalties will be calculated for each partner as follows:

31 March 1998			
Lack of reasonable care	$1,124.31	20%	$224.86
31 March 1999			
Lack of reasonable care	$925.32	20%	$185.06
Lack of reasonable care	$487.41	20%	$97.48
Total penalty			**$282.54**
31 March 2000			
Lack of reasonable care	$660.00	20%	$132.00
Lack of reasonable care	$3,818.10	20%	$763.62
Unacceptable interpretation	$5,549.61	20%	$1,123.10
Total penalty			**$2,005.54**

Summary

Total penalty imposed for each partner:

Year ended	31.3.98	$224.86
	31.3.99	$282.54
	31.3.2000	$2,005.54
Total penalty		$2,512.94

Due dates for paying penalties

Legislation

These sections set the due dates for paying penalties:

142	Late filing penalty	later of 30 days after notification and various dates as set out in legislation
142A	Tax that is not a penalty (if amount due on a due date is increased)	at least 30 days after notice of assessment or reassessment issued
142B	Shortfall penalties	at least 30 days after notice of assessment or reassessment issued
142C	Payments by officers	at least 30 days after notice of assessment or reassessment issued
142D	Repayment of excess refund or credit of tax	later of 30 days after the date of notification requiring payment or the date specified in the notice
142E	Imputation penalty tax and dividend withholding penalty tax	20 June following the end of the imputation year
142E	underestimation penalty tax	Terminal tax date for income year to which unpaid provisional tax relates
142F	deferrable tax	30th day after the last day of the relevant period of deferral

Discussion

A taxpayer who is charged a shortfall penalty will generally receive a new due date for paying both the penalty and the tax shortfall to which the penalty relates. The exception is if the taxpayer has failed to file a return.

However, interest on the unpaid tax will still be charged from the original due date until the date the assessment identifying the shortfall is issued.

Criminal penalties

Legislation

The legislation provides for criminal penalties under the following sections:

- 143 - Absolute liability offences
- 143A - Knowledge offences
- 143B - Evasion or similar offences
- 143C - Offence for failure of officers of Department to maintain secrecy
- 143D - Offence for failure of other persons to maintain secrecy
- 143E - Secrecy requirements where information given by Department
- 143F - Offence in relation to inquiries
- 143G - Offence in relation to court orders
- 143H - Obstruction
- 145 - Penalties for offences for which no specific penalty imposed
- 147 - Employees and officers
- 148 - Aiding or abetting

Discussion

In current legislation criminal offences and penalties are contained in a number of the Inland Revenue Acts. They duplicate each other and treat similar breaches in an inconsistent manner. In many cases the penalties are ineffective.

The new legislation consolidates the criminal offences and standardises the resulting penalties across all revenues.

The sanctions for some offences have been increased so they act as a more effective deterrent. A maximum jail

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term of five years may be imposed for evasion, and for most offences a maximum monetary fine of $50,000 may be imposed.

While higher sanctions have been introduced, the nature and scope of the offences have not changed significantly.

Tax offences relating to negligence have been repealed as the new shortfall penalties will punish negligent conduct.

Criminal offences fall into three broad categories:

- absolute liability offences
- offences for knowingly failing to comply with an obligation
- evasion or similar offences

Absolute liability offences

Section 143(1) provides that it is offence if a person –

- does not keep the books and documents required to be kept by a tax law
- does not provide information (including tax returns and tax forms) when required to do so by a tax law
- does not apply for registration as required under section 51 of the Goods and Services Tax Act 1985.

It is fundamental to the operation of the tax system that taxpayers provide and maintain information. Accordingly, failure to keep the books and documents required by a tax law and provide information to the Commissioner when required to do so by a tax law are to remain absolute liability offences.

The only defence against conviction under the absolute liability offences would be if the person required to provide information, other than tax returns and tax forms, did not have the information in his or her *"...knowledge, possession, or control..."* However, the obligation always remains with the taxpayer to provide tax returns or tax forms even if the taxpayer has contracted with a third party to meet that obligation.

The penalty for conviction of an absolute liability offence is:

- a maximum of $4,000 for a first offence;
- a maximum of $8,000 for a second offence;
- a maximum of $12,000 for any subsequent offence.

Knowledge offences

A person may be convicted for a number of offences for knowingly breaching a tax obligation. Section 143A outlines the knowledge offences.

Knowledge offences include instances when a person:

- *knowingly* does not keep the books and documents that must be kept
- *knowingly* does not provide information (including tax returns and tax forms) when required to do so
- *knowingly* provides altered, false, incomplete, or misleading information (including tax returns and tax forms)
- *knowingly* does not account to the Commissioner for an amount of tax deducted or withheld
- *knowingly* does not deduct or withhold tax
- *knowingly* issues two tax invoices (as defined in the GST Act) for the same taxable supply.

Several subsections provide that persons or companies are not liable to conviction if they did not hold the information requested, or any failure to make or account for withholding payments was beyond their control.

The maximum penalties for conviction under section 143A are:

- $25,000 for a first offence
- $50,000 for any subsequent offence.

However, under subsection (8) the penalty for knowingly not accounting to the Commissioner for a deduction or withholding payment made is imprisonment for up to five years, and/or a fine of up to $50,000. This applies for each occasion the person is convicted.

A taxpayer who makes a deduction but fails to return it to Inland Revenue has committed an offence similar to evasion, and will be penalised accordingly. This offence will only require the proof of knowledge.

Evasion or similar offences

Section 143B(1) provides that the following are offences:

- knowingly not keeping the books and documents that must be kept
- knowingly not providing information (including tax returns and tax forms) when required to do so
- knowingly providing altered, false, incomplete, or misleading information (including tax returns and tax forms)
- knowingly not making a deduction or withholding of tax required to be made
- pretending to be another person for any purpose or reason relating to a tax law –

– if a person does them for any of these reasons:

- to evade the assessment or payment of tax by the person or any other person
- to obtain a refund or payment of tax in the knowledge that the person is not lawfully entitled to the refund or payment
- to enable another person to obtain a refund or payment of tax in the knowledge that the other person is not lawfully entitled to the refund or payment.

In addition, section 143B(2) provides that a person who evades or attempts to evade the assessment or payment of tax by the person or another person commits an offence.

The penalty, if convicted under section 143B is imprisonment for up to five years, and/or a fine of up to $50,000.

Offences relating to court orders

Legislation

Under section 143G a person who fails to comply with the terms of a Court order made under section 17A commits an offence. Anyone who is convicted of such an offence is liable to the same penalties that may be imposed under section 112 of the District Courts Act 1947.

Discussion

Section 112(c) of the District Courts Act 1947 sets out the penalty for disobeying the order or direction of any officer of the Court. For each offence, the Judge may sentence the person to prison for up to three months, or to a fine of up to $1,000.

Obstruction

Section 143H states:

a person who obstructs the Commissioner or an officer of the Department acting in the lawful discharge of the duties or in the exercise of the Commissioner's or officer's powers under a tax law commits an offence against this Act.

The penalty for this offence is a maximum fine of $25,000 for the first offence and $50,000 for subsequent offences.

Civil and criminal penalties for obstruction are explained on page 24 of this TIB.

Aiding or abetting

Section 148 states:

(1) A person who aids, abets, incites, or conspires with another person to commit an offence...also commits an offence against this Act.

(2) A person convicted of aiding, abetting, inciting, or conspiring...is liable for up to the same maximum fine or term of imprisonment, or both, that could apply to a person who commits the principal offence.

A person who aids or abets another to commit an offence will be liable to the same penalty as the person who commits the principal offence. This could result in a maximum penalty of five years' imprisonment.

Penalties for offences for which no specific penalty is imposed

Section 145 imposes fines for offences for which no particular penalty is prescribed. It imposes a fine of up to $15,000 for a first offence and up to $25,000 for any subsequent offences.

Other offences

The following sections have been carried over from the previous Inland Revenue Acts:

Section 143C - Offence for failure of Inland Revenue officers to maintain secrecy

Section 143D - Offence for failure of other persons to maintain secrecy

Section 143E - Secrecy requirements where information given by Inland Revenue

Section 143F - Offence in relation to inquiries

Section 144 - Certain offences in relation to Stamp and Cheque Duties Act 1971

Section 150 - Information may charge several offences

Section 150A - Information may be laid within 10 years for income tax and GST offences

Section 150B - Information may be laid within 4 years for stamp duty and gaming duty offences

Section 150C - Authority to lay information

Section 150D - Evidence in proceedings for failure to furnish returns and information

Section 150E - Evidence inconsistent with instrument not admissible to reduce stamp duty

Section 151 - Non-presentation of instrument for stamping

Section 152 - Evidence of financial or property transactions

Publication of names

Section 146 specifies that names of the following must be published in the Gazette:

- anyone liable to pay a shortfall penalty for taking an abusive tax position
- anyone liable to pay a shortfall penalty for evasion or similar act (including knowingly failing to deduct a tax deduction)
- anyone convicted of knowingly failing to account for a tax deduction
- anyone convicted of evasion or similar act
- anyone convicted of aiding, abetting, inciting or conspiring with another person to evade tax or fail to account for a tax deduction.

The section also sets out the details which the Commissioner must publish about each person.

Employees and officers

Legislation

Under section 147 a company's employee, agent, or officer commits an offence if the company commits an offence (the principal offence) and either of the following apply:

- The principal offence was caused by an act or omission of the employee, agent or officer, or through knowledge attributable to him or her.
- The principal offence is evasion committed by the employee, agent, or officer.

An employee or officer of a company includes anyone who is responsible for undertaking an action on the company's behalf. If such a person is convicted, he or she is liable for up to the same maximum fine and/or term of imprisonment that apply for committing the principal offence.

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Discussion

This section imposes a penalty upon a company's employee, agent or officer if that person was responsible for the company committing a breach. Such a person is liable to the same fine as any other person who would have committed the offence. The penalty could include a fine or term of imprisonment, or both.

For a fine to be imposed upon a company's employee, agent or officer, the Commissioner would have to prove to the standard of "beyond reasonable doubt" that the person had knowingly or intentionally committed the breach. Obviously, a clerk who follows instructions given by a senior officer and does not know that a breach is being committed would not be liable to a fine or imprisonment if the company was found to have committed a breach.

Court orders

Legislation

Section 17A gives the Commissioner an additional power to obtain information or tax returns which are necessary to administer or enforce the Inland Revenue Acts.

If a taxpayer fails to provide information or tax returns requested under section 17, the Commissioner may apply to the District Court for an order requiring the person to produce the information for review. A court order can be used instead of or in conjunction with prosecution for failure to furnish information or a return, or after prosecution has occurred and the information or return is still outstanding.

Discussion

Application

The Commissioner can apply to the District Court for an order asking the person named in the application to provide information or a return. The court will then issue notice to the person, who will have the opportunity to appear at the hearing of the application. On hearing the application, the court may order the person to produce the documents or may vary the order.

Appeal rights

A taxpayer may appeal the District Court decision to the High Court, as the High Court has jurisdiction over any District Court decisions. Likewise the Court of Appeal has jurisdiction over High Court decisions.

Legal professional privilege

A court order cannot require the production of documents which are subject to legal professional privilege. This is in line with section 20. In general, claims to legal professional privilege are expected to be determined by the court in the course of hearing the Commissioner's application for the court order.

Subsection (7) authorises the courts to review the information requested to determine:

- whether or not to make an order requiring the taxpayer to produce the information requested
- whether or not the information required is subject to legal professional privilege.

Subsection (8) authorises the court to order production of information or any part for review by the Commissioner if the court is satisfied that the information is not subject to legal professional privilege, and meets either of these conditions:

- It is likely to be relevant for a purpose relating to administering or enforcing any Inland Revenue Act.
- It involves a matter connected with another function conferred on the Commissioner.

Forms of legal professional privilege other than that established in section 20 may be claimed for tax purposes. For example, litigation privilege under which information obtained from third parties for the purposes of litigation against the Commissioner of Inland Revenue is protected from disclosure, even though it does not strictly fall within section 20.

Standard of proof

When deciding whether or not to grant a court order the court considers whether the request is reasonable. The standard of proof required in proving that the request is reasonable is the balance of probabilities.

Interaction with section 17

Section 17 allows the Commissioner to obtain information which is necessary to administer or enforce the Inland Revenue Acts. This provision will be used first to obtain information. If the information is not forthcoming the Commissioner can either prosecute the taxpayer or seek a court order. The imposition of a court order is an additional incentive for the taxpayer to provide the information. A taxpayer who fails to provide the information could be liable to a harsher sanction than that provided by section 17, including a term of imprisonment.

Onus and standard of proof

Section 149A sets out the standard and onus of proof as follows:

Penalty	Standard of proof	Onus of proof
Civil penalty except evasion or obstruction	Balance of probabilities	Taxpayer
Civil penalty for evasion or obstruction	Balance of probabilities	Commissioner
Criminal penalties	Beyond reasonable doubt	Commissioner
Application of Court Orders under sec. 17A	Balance of probabilities	Commissioner

Civil standard and criminal standard - the difference

The difference between the two standards is clearly established in case law. The standard in criminal cases is proof "beyond reasonable doubt" and the civil standard is proof "on the balance of probabilities".

The difference cannot be any more clearly defined than the often quoted exposition by Lord Denning in *Miller v Minister of Pensions* [1947] 2 All ER 372, at 373-374.

His lordship began with the criminal standard:

> That degree is well settled. It need not reach certainty, but it must carry a high degree of probability. Proof beyond reasonable doubt does not mean proof beyond the shadow of a doubt. The law would fail to protect the community if it admitted fanciful possibilities to deflect the course of justice. If the evidence is so strong against a man as to leave only a remote possibility in his favour, which can be dismissed with the sentence "of course it is possible but not in the least probable" the case is proved beyond reasonable doubt, but nothing short of that will suffice.

In relation to the civil standard, Lord Denning said:

> That degree is well settled. It must carry a reasonable degree of probability but not so high as is required in a criminal case. If the evidence is such that the tribunal can say: 'We think it more probable than not', the burden is discharged, but if the probabilities are equal, it is not.

Garrow and McGechan's *Principals of Law of Evidence* (1984 7 ed, at p.27) commented:

> ...in a civil action the standard is merely 'more likely than not', permitting a reasonable doubt nevertheless whether the finding is correct; whereas in a criminal case the Court must be 'sure' in the sense that no reasonable doubt remains. It is to be emphasised that doubt, to be effective to preclude proof, in a criminal case must be 'reasonable', as distinguished from fantastic or purely speculative or irrational.

Garrow and McGechan (at p.29) also cautioned on the use of substitutes for beyond reasonable doubt:

> Epithets such as 'morally certain' should not be used. The expression 'giving the prisoner the benefit of the doubt' should not be used. It is not a question of giving the benefit of doubt; if the jury are left with any degree of doubt that the prisoner is guilty, then the case has not been proved: *R v Onufrejczyk* [1955] 1 QB 388.

Clearly, the standard of proof for imposing a criminal penalty is much higher than that required to impose a civil penalty.

Onus of proof

When challenging the imposition of a civil penalty, except for evasion or obstruction, the onus of proof will lie with the taxpayer. This is considered reasonable as matters raised by way of defence by a taxpayer are primarily within the knowledge of the taxpayer. In these circumstances it would be extremely difficult for the Commissioner to discharge the onus. Proper record keeping, full and honest disclosure to agents and conformity with the advice of agents are all matters within a taxpayer's control.

However, the onus rests with the Commissioner for civil penalties for evasion and obstruction and all criminal penalties. These are more serious breaches of the Inland Revenue Acts, and before imposing penalties for such breaches the Commissioner should be required to have gathered sufficient evidence to discharge the onus of proof.

The Commissioner must also satisfy the onus of proof for court orders.

Imposition of civil and criminal penalties

Legislation

Section 149 sets down the following rules about imposing a penalty:

- Each time a taxpayer breaches a tax obligation he or she may be liable to a civil penalty, and/or to a criminal penalty (if convicted).
- A taxpayer is liable to only one shortfall penalty for each tax shortfall.
- If a taxpayer could be liable to more than one shortfall penalty for a tax shortfall, the highest shortfall penalty is to be imposed.
- The Commissioner may assess and impose civil penalties after a taxpayer has been prosecuted for an offence under the Act, whether or not the prosecution is successful.
- If a shortfall penalty has been imposed on a taxpayer for taking an incorrect tax position, the Commissioner may not subsequently prosecute the taxpayer for taking the incorrect tax position.

Discussion

There are instances when a single breach will make the taxpayer liable to both a civil and a criminal penalty. Examples are evasion and failure to file a tax return.

The Commissioner may impose both civil and criminal penalties for the same breach provided that the Commissioner prosecutes the taxpayer before imposing the civil penalty.

A new section 94A provides that when assessing civil penalties, the Commissioner must use the same processes as apply to the tax on which the penalty is imposed.

Section 94A states:

> (1) The Commissioner may make or amend an assessment of a civil penalty in the same way as the Commissioner may make or amend an assessment of the tax in respect of which the penalty is imposed;
>
> (2) The Commissioner must assess a shortfall penalty in the same way as the tax to which it relates, but separately from the tax;
>
> (3) The Commissioner may assess a shortfall penalty before or after unpaid tax has been assessed, or has become assessable or payable, or has been paid.

Late filing penalties and late payment penalties will be imposed at the time that the non-compliant action occurs. These penalties will not be subject to the new disputes resolution rules. Section 138K(2) provides that a taxpayer has no right to challenge charging or amount of a civil penalty assessed by the Commissioner for late filing of a tax return or late payment of tax.

Taxpayers may dispute the imposition of shortfall penalties, but they cannot dispute the amount.

Part 6 - Remissions

Introduction

Remission provisions are needed to allow the Commissioner to accommodate circumstances when a penalty is not appropriate. The main remission provisions the Act provides are:

- remission for reasonable cause
- remission consistent with collecting the highest net revenue over time.

Provisions that apply to specific situations, such as the provisional tax underestimation provision, will remain.

The new provisions will apply to all the Inland Revenue Acts and the Accident Rehabilitation and Compensation Insurance Act.

Provisions to remit late payment penalties, late filing penalties and interest accommodate circumstances in which it was not equitable to impose penalties or interest.

There is no provision to remit shortfall penalties. This is because a taxpayer's circumstances are taken into account before a shortfall penalty for lack of reasonable care, gross carelessness or evasion is imposed.

Background

The Inland Revenue Acts currently provide for the remission of penalties if the Commissioner considers remission "equitable". If a penalty can be imposed because a taxpayer has failed to meet an obligation, but not applying it can be justified on equity grounds, the penalty is remitted. Remission is initiated by a taxpayer and results in the debt being legally forgiven.

Key features

- Late payment penalties and late filing penalties may be remitted when taxpayers have "reasonable cause beyond their control".
- Shortfall penalties will not be remitted.
- Interest may be remitted or cancelled in limited circumstances.
- There is a general discretionary remission consistent with the Commissioner's objective to collect the highest net revenue over time.
- There are specific legislative guidelines for instalment arrangements.

Legislation

Under section 183A the Commissioner may remit a late filing penalty, a late payment penalty, any imputation penalty tax or any dividend withholding penalty tax if both of these conditions are met:

- The taxpayer has reasonable cause for paying late or not filing a return on time.
- The taxpayer pays the unpaid tax as soon as practicable.

Reasonable cause could include an event such as accident or disaster, or illness or emotional or mental distress. It does not include an omission by an agent, unless caused by an event or circumstance beyond the agent's control which could not have been avoided by following accepted business standards and professional conduct. Reasonable cause also excludes the taxpayer's financial position.

Section 183B provides that the Commissioner may cancel incremental late payment penalties if taxpayers have satisfied the terms of an instalment arrangement entered into with the Commissioner. If taxpayers arrange to pay a tax debt by instalment before the due date for the tax (knowing they are in financial difficulty) the initial late payment penalty will also be reduced from 5% to 2%.

Section 183C provides that interest will be cancelled for the period from the date of the notice until the due date specified in the notice if tax is paid by the due date stated in the notice.

It also provides that late payment penalties on deferrable tax in the period of deferral will be cancelled if the taxpayer makes a competent objection or starts proceedings to challenge an assessment.

Section 183D states that the Commissioner may remit a late filing penalty, late payment penalty or interest if it is consistent with the collection of the highest net revenue over time.

Section 183E states that if the unpaid tax is remitted, the interest relating to that tax will be remitted.

Section 183F states that late payment penalty and interest will not be charged if the related unpaid tax is $100 or less on a specific due date.

Section 183G states that if the Commissioner remits an amount of penalty or tax and the taxpayer has already paid it, the amount will be refunded to the taxpayer or applied towards meeting another tax liability.

Section 183H states that a taxpayer who wishes to apply for remission or cancellation must apply in writing, and must produce any information the Commissioner requires about the request.

Discussion

Late payment penalties and late filing penalties may be remitted under two categories: reasonable cause, or if remission will result in collecting the highest net revenue over time. Interest may only be remitted if remission will result in collecting the highest net revenue over time. Shortfall penalties cannot be remitted.

Difference between remission, cancellation and reversal

Remission: occurs when the tax, penalty or interest is correctly imposed at the time but a decision has been made to relieve the taxpayer of the liability to pay.

Cancellation: occurs when the tax, penalty or interest was correctly imposed at the time but a provision of the legislation relieves the taxpayer from the obligation to pay, such as, adhering to an instalment arrangement.

Reversal: the tax, penalty or interest should not have been charged in the first place.

Reasonable cause

A late filing penalty or late payment penalty can be remitted if the Commissioner is satisfied that late filing or late payment was caused by an event or circumstance beyond the taxpayer's control. The taxpayer is responsible for filing and paying, so specific action or inaction by a tax agent will not constitute reasonable cause.

The legislation gives guidance as to what could be considered to be events or circumstances beyond a taxpayer's control, as well as events or circumstances which would not fall within that category. The events and circumstances set out in the legislation are not exhaustive, so the Commissioner may consider other matters on a case by case basis.

Collecting highest net revenue over time

The Commissioner has a discretion to remit late filing penalty, late payment penalty and interest if it is consistent with the duty to collect, over time, the highest net revenue that is practicable within the law.

The intent is to allow for genuine circumstances if those circumstances are not consistent with reasonable cause. With regards to the late filing and late payment penalties, the sort of situation which may be given favourable consideration would be if non-payment is caused by genuine oversight. However, in these situations payment of the underlying tax should have been made as soon as the oversight was recognised. With interest, the sort of situation which may be given favourable consideration would be if non-payment is caused by Inland Revenue error.

The provision to remit is discretionary, so prior consideration may be given to the taxpayer's circumstances, liquidity and assets and liabilities.

Only in exceptional circumstances will interest be remitted, as it is compensation for the use of crown money.

Cancellation of interest

When the Commissioner issues a notice of assessment and the amount specified in the notice (assessment plus interest) is paid by the due date, the interest applying from the date of the notice until the due date specified in the notice will be cancelled.

Cancellation if instalment arrangement made

Late payment penalty can be cancelled if a taxpayer makes a payment arrangement which requires two or more instalments.

Sixty percent of the initial late payment penalty may be cancelled if the arrangement is entered into before the due date for payment and all the terms of the arrangement are strictly adhered to. This would reduce the initial late payment penalty from 5% to 2% and cancel any incremental late payment penalties.

If the arrangement is made after the due date of the tax or after a notice under section 157 of the TAA or section 43 of the GST Act is issued, all incremental late payment penalties imposed after the date of the arrangement or notice may be cancelled if the arrangement is adhered to.

The penalties will only be cancelled if the taxpayer keeps all terms of the arrangement. This means that if, as part of the arrangement, returns must be filed or current taxes kept up to date, and the taxpayer does not meet these obligations, the Commissioner can enforce payment of penalties incurred after the date of the arrangement.

Application dates

Late payment penalty remissions considered after 1 April 1997, regardless of the period they apply to, will be considered under the new rules.

Any instalment arrangements entered into before 1 April 1997 will come under the current rules, regardless of when the arrangement ends.

Part 7 - Amendments to other Acts

Other Acts

As discussed earlier, the new penalties apply to all the Inland Revenue Acts and the premiums of earners, employers and the self-employed under the Accident Rehabilitation and Compensation Insurance Act, not just to the Income Tax Act and Goods and Services Tax Act. Broadly speaking, the old penalty provisions in those Acts were repealed and replaced with the new generic penalty provisions in the Tax Administration Act. The exception is the Student Loan Scheme Act and the Child Support Act - in these the new penalty provisions apply only to employer obligations.

In addition, some minor changes were made to aspects of various Inland Revenue Acts. These changes are discussed below.

Stamp and Cheque Duties Act

Stamp duty is now payable six months after a document is executed or received in New Zealand. However, if a document is presented for stamping more than six months after execution because of delay in approval from, say, the Land Tribunal or the Overseas Investment Commission, the new remission provisions will generally apply.

Estate and Gift Duties Act

Gift duty is now payable six months after the making of a dutiable gift.

Approved issuer levy (AIL)

The new penalty rules do not explicitly apply to AIL. This is because if the issuer of a security does not comply with the requirements of AIL, the taxpayer automatically defaults back to the non-resident withholding tax (NRWT) rules. The new penalties apply to any non-compliance with the NRWT requirements.

Gaming Duties Act

The due date for paying totalisator duty is now the 20th of the month following the last race. Accordingly, if totalisator duty is not paid by this due date, late payment and interest will apply.

Summary tables - changes between current rules and new rules under Tax Administration Act

Table 1 - income tax

Charge	Current rules	New TAA rules
Additional tax	Additional tax applies to all taxpayers (section 139, TAA)	Late payment penalty applies to all taxpayers - (section 139B)
	10% additional tax imposed day after due date for payment	5% late payment penalty imposed day after due date for payment
	10% incremental additional tax every six months thereafter	2% incremental penalty every month thereafter
	Not charged if additional tax amount $5.00 or less.	Not charged if overdue tax is $100 or less
Interest	Applies to provisional taxpayers only	Applies to all taxpayers (section 120A-U)
	Credit interest calculated from first, second or third instalment	Credit interest calculated from first, second or third instalment for provisional taxpayers. From later of due date or date return filed for other taxpayers
	Debit interest calculated from first, second or third instalment	Debit interest calculated from first, second or third instalment for provisional taxpayers. From original due date for other taxpayers.
	Interest not charged on penalties	Calculated including penalties
	Calculated to earlier of date tax paid/refunded or terminal tax date	Calculated until date tax paid or overpayment refunded
	Calculated on a daily basis	Calculated on a daily basis
	Payments applied to tax debt first	Payments applied to interest first before reducing tax debt
	Credit interest assessable income for all taxpayers	Credit interest assessable income for all taxpayers
	Debit interest deductible under normal tax rules	Debit interest deductible under normal tax rules
	No legislated threshold or minimum amount	Not charged if overdue tax is $100 or less
Civil penalty: evasion	Penalty imposed by IRD: penal tax up to three times the deficient tax (section 186[1], TAA). Other penal provision NRWT (section 197), RWT (section 196), SSCWT (section 195), PAYE and ACC (section 194)	Penalty imposed by IRD under section 141E: 150% of tax understatement
	ICA - imputation penalty tax (section 153, TAA) 10% of amount of further income tax that gives rise to the liability for the imputation penalty tax.	
	DWT - dividend withholding payment penalty (section 154, TAA). 10% of further dividend withholding payment giving rise to the liability for the dividend withholding payment penalty tax.	
Civil penalty: abusive tax position[2]	Nil	Penalty imposed by IRD under section 141D: 100% of tax understatement.

1. Inland Revenue has a policy on imposing penal tax. We generally use a guide of 150% for income tax and GST offences.
2. Section BB 9 of the Income Tax Act 1994 (general anti-avoidance provision) and other specific anti-avoidance provisions allow reconstruction of an arrangement to counteract any tax advantage. They are intended to protect tax liability established under other sections, but do not provide for any form of penalty.

Table 1 - income tax (continued)

Charge	Current rules	New TAA rules
Civil penalty: gross careless-ness	Penalty imposed by IRD - 10% additional tax under section 139, TAA	Penalty imposed by IRD under section 141C: 40% of tax understatement
	ICA - imputation penalty tax (section 153, TAA) 10% of amount of further income tax that gives rise to the imputation penalty tax liability	
	DWT - dividend withholding payment penalty (section 154, TAA): 10% of further dividend withholding payment giving rise to the liability for dividend withholding payment penalty tax.	
Civil penalty: unacceptable interpretation	Nil	Penalty imposed by IRD under section 141B: 20% of tax understatement
Civil penalty: lack of reason-able care	Penalty imposed by IRD - 10% additional tax (section 139, TAA)	Penalty imposed by IRD under section 141A: 20% of tax understatement
	ICA - imputation penalty tax (section 153, TAA) 10% of amount of further income tax that gives rise to imputation penalty tax liability	
	DWT - dividend withholding payment penalty (section 154, TAA): 10% of further dividend withholding payment giving rise to the liability for dividend withholding payment penalty tax.	
Criminal penalty: evasion	Prosecution imposed by the Courts (sec 222(4)) 1st conviction a fine up to $15,000; further convictions a fine up to $25,000.	Prosecution imposed by Courts under section 143: 1st conviction a fine up to $25,000 or prison for up to five years; further convictions a fine up to $50,000 or prison for up to five years.
	Foreign investments/income & trust offences (section 222(3), TAA): for each conviction a fine up to $50,000 and/or prison for up to two years[3].	
	Trust money offences (PAYE, RWT, etc) (section 222(1), TAA), 1st conviction a fine up to $15,000 or prison for up to 12 months; Further convictions a fine up to $25,000 or prison for up to 12 months.	
Criminal penalty: gross carelessness	Penalty imposed by Courts: not specifically referred to in the Act but would be prosecutable under section 222(1), TAA	
Criminal penalty: lack of reasonable care	Penalty imposed by Courts under section 222(4), TAA: 1st conviction a fine up to $15,000; further convictions a fine up to $25,000[4]	

3. Includes cases when a taxpayer *knowingly* fails to disclose information about foreign investment funds and trusts.

4. Section 416(1)(b) sets out offences for "wilfully" or "negligently" making false returns. Charges laid by Inland Revenue are usually for wilfulness; we do not usually prosecute for negligence unless there is evidence that the negligence is serious enough to impute wilfulness.

Table 2 - Goods and services tax

Charge	Current rules	New TAA rules
Additional tax	Applies to all GST persons (sec 41, GST Act)	Late payment penalty applies to all GST persons: section 139B
	10% additional tax imposed day after payment due date	5% late payment penalty imposed day after payment due date
	2% incremental additional tax every month thereafter	2% incremental penalty every month thereafter
	Not charged if additional tax amount $5.00 or less	Not charged if overdue tax is $100 or less
Interest	Applies to credit assessments of GST persons (section 46, GST Act)	Applies to debit and credit assessments - (sections 120A-U)
	The day following 15 working days after information or returns supplied	If the return is supplied before the due date, the day following 15 working days after return or information is supplied. In all other cases, the later of: • the day after the day on which the return is provided • the day after the day on which the payment is made
	Debit interest not applicable	Debit interest from original due date for tax
	Calculated on amount to be refunded by IRD	Calculated including penalties
	Calculated to the earlier of the date of refund or the end of 12 month period	Calculated until date tax paid/overpayment refunded
	Calculated on a daily basis	Calculated on a daily basis
	Payments applied to tax debt first	Payments applied first to interest before reducing tax debt
	Credit interest assessable income	Credit interest assessable income for all taxpayers
	Debit interest not applicable	Debit interest deductible under normal tax rules
	Interest not paid if amount below $5.00	Not charged if overdue tax is $100 or less
Civil penalty: evasion	Penalty imposed by IRD - Penal tax up to three times the amount of deficient tax (section 67, GST Act)	Penalty imposed by IRD (section 141E): 150% of tax understatement
Civil penalty: abusive tax position	Nil	Penalty imposed by IRD (section 141D): 100% of tax understatement
Civil penalty: gross careless-ness	Penalty imposed by IRD (section 41, GST Act): 10% additional tax plus monthly incrementals of 2%	Penalty imposed by IRD (section 141C): 40% of tax understatement
Civil penalty: unacceptable interpretation	Nil	Penalty imposed by IRD (section 141B): 20% of tax understatement
Civil penalty: lack of reason-able care	Penalty imposed by IRD (section 41, GST Act): 10% additional tax plus monthly incrementals of 2%	Penalty imposed by IRD (section 141A): 20% of tax understatement
Criminal penalty: evasion	Fine imposed by the Courts (section 62(4), GST Act) - 1st conviction a fine up to $15,000, further convictions a fine up to $25,000.	Fine imposed by the Courts (section 143): for 1st conviction a fine up to $25,000 or prison for up to five years. for further convictions a fine up to $50,000 or prison for up to five years.

Table 3 - Fringe benefit tax

Charge	Current rules	New TAA rules
Additional tax	Additional tax applies to all FBT employers (section 139, TAA)	Late payment penalty applies to all FBT employers (section 139B)
	10% additional tax imposed day after due date for payment	5% late payment penalty imposed day after due date for payment
	10% incremental additional tax every six months thereafter	2% incremental penalty every month thereafter
	Not charged if additional tax amount $5.00 or less	Not charged if overdue tax is $100 or less
Interest	Employers who pay FBT on an annual or income year basis	Applies to all FBT employers regardless of filing basis (sections 120A-U)
	Credit interest not applicable	Credit interest from later of due date for payment or date return filed
	Debit interest from first quarterly due date	Debit interest from original due date for tax
	Calculated excluding penalties	Calculated including penalties
	Calculated to annual or income year due date	Calculated until date tax paid/overpayment refunded
	Calculated on a daily basis	Calculated on a daily basis
	Payments applied to tax debt first	Payments applied to interest first before reducing tax debt
	Credit interest not applicable	Credit interest assessable income for all taxpayers
	Debit interest a deduction for employers	Debit interest deductible under normal tax rules
	No minimum amount of interest applies	Not charged if overdue tax is $100 or less
Civil penalty: evasion	Penalty imposed by IRD: penal tax up to three times the deficient tax (section 186, TAA)	Penalty imposed by IRD (section 141E) 150% of tax understatement.
Civil penalty: abusive tax position	Nil	Penalty imposed by IRD (section 141D): 100% of tax understatement.
Civil penalty: gross carelessness	Penalty imposed by IRD TAA (section 139): 10% additional tax.	Penalty imposed by IRD (section 141C) 40% of tax understatement
	10% incremental additional tax every six months thereafter.	
Civil penalty: unacceptable interpretation	Nil	Penalty imposed by IRD (section 141B (20% of tax understatement
Civil penalty: lack of reason-able care	Penalty imposed by IRD TAA (section 139): 10% additional tax.	Penalty imposed by IRD (section 141A): 20% of tax understatement
	10% incremental additional tax every six months thereafter.	
Criminal penalty: evasion	Prosecution imposed by the Courts (sec 222(4), TAA): 1st conviction a fine up to $15,000. Further convictions a fine up to $25,000, or prison for up to 12 months.	Prosecution imposed by the Courts (section 143): 1st conviction a fine up to $25,000; further convictions a fine up to $50,000.
		Maximum prison term of five years for evasion.

Table 4 - Student Loans

Charge	Current rules	New TAA rules
Penalty	Additional tax applies to all Student Loan borrowers (section 44, SL Act)	No change
	2% penalty day after payment due date	
	2% incremental penalty every month thereafter	
	Not charged if additional tax amount $5.00 or less	
Interest	Applies to Student Loan borrowers (section 42, SL Act)	No change
	Credit interest not applicable	
	Debit interest from day loan is drawn	
	Calculated excluding penalties	
	Calculated until date loan is paid in full or called up	
	Calculated on a daily basis and compounded once a year	
	Payments applied to the loan balance first	
	No credit interest, debit interest not deductible	
	No minimum amount of interest to be charged	
Civil penalty: evasion[5]	Penalty imposed by IRD (section 86, SL Act): penal tax up to three times the amount of deficient repayment deduction. (sections 186-199 and 193 of TAA apply as if the penal repayment deduction were penal tax which the Commissioner had assessed under section 188, TAA.)	Penalty imposed by IRD (section 141E): 150% of tax understatement
Civil penalty: abusive tax position[5]	Nil	Not applicable
Civil penalty: gross carelessness[5]	2% additional tax day after due date for payment (section 44, SL Act)	Penalty imposed by IRD (section 141C): 40% of tax understatement
	2% incremental additional tax every month thereafter.	
Civil penalty: unacceptable interpretation[5]	Nil	Not applicable
Civil penalty: lack of reasonable care[5]	2% additional tax day after payment due date (section 44, SL Act)	Penalty imposed by IRD (section 141A): 20% of tax understatement
	2% incremental additional tax every month thereafter.	
Criminal penalty: evasion[5]	Fines imposed by Courts (section 78, SL Act) Using deductions for other purposes: 1st conviction - prison for up to 12 months or a fine up to $15,000. Further convictions - prison for up to 12 months or a fine up to $25,000.	Penalty imposed by Courts (section 143): Prosecution imposed by Courts:1st conviction a fine up to $25,000; further convictions a fine up to $50,000.
	Failing to deduct or pay - 1st conviction - a fine up to $15,000; further convictions a fine up to $25,000.	Maximum prison term of five years for evasion.

5. Applies to employer obligations only.

Table 5 - Child Support

Charge	Current rules	New TAA rules
Penalty	Additional tax applies to all custodian and liable parents (section 134, CS Act)	No change
	10% penalty day after payment due date	
	2% incremental penalty every month thereafter	
	Not charged if penalty amount $5.00 or less	
Interest	Interest on underestimation is applied to liable parents only (section 46, CS Act)	No change
	Calculated on the amount of underestimated Child Support payments that remain unpaid on any day	
	Calculated from 21 April to day of payment	
Civil penalty: evasion[6]	Penalty imposed by IRD (section 173, CS Act) Penalty for late deductions, failing to make deductions or failing to pay deductions to IRD: greater of 10% of the amount in default or $5, plus 2% monthly of any remaining unpaid deductions.	Penalty imposed by IRD (section 141E): 150% of tax understatement
Civil penalty: abusive tax position[6]	Nil	Not applicable
Civil penalty: gross careless-ness[6]	10% additional tax day after payment due date (section 134, CS Act)	Penalty imposed by IRD (section 141C): 40% of tax understatement
	2% incremental penalty every month thereafter	
Civil penalty: unacceptable interpretation[6]	Nil	Not applicable
Civil penalty: lack of reason-able care[6]	10% additional tax day after payment due date (section 134, CS Act)	Penalty imposed by IRD (section 141A): 20% of tax understatement
	2% incremental penalty every month thereafter	
Criminal penalty: evasion[6]	Fine imposed by Courts (section 210 CS Act) using deductions for other purposes: 1st conviction prison for up to 12 months or a fine up to $15,000.	Fine imposed by Courts (section 143 CS Act) Prosecution imposed by the Courts:1st conviction a fine up to $25,000
	Further convictions prison for up to 12 months or a fine up to $25,000.	Further convictions a fine up to $50,000.
	Failing to deduct or to pay deductions: 1st conviction a fine up to $15,000. Further convictions a fine up to $25,000.	Maximum prison term of five years for evasion.

6. Applies to employer obligations only.

Table 6 - Stamp and cheque duties

Charge	Current rules	New TAA rules
Additional tax	Penalty applies to persons liable to pay stamp duty.	Late payment penalty applies to persons liable to pay stamp duty (section 139B)
	Penalty for late presentation (sec 57, S&CD Act) and penalty for unpaid duty (Sec 58) each 1 cent for each complete $1 of unpaid duty	5% late payment penalty imposed day after due date for payment.
	No late payment penalty for cheque duties.	2% incremental penalty every month thereafter
	Penalty not charged if under 25 cents.	Not charged if overdue duty is $100 or less
Interest	No provisions to charge interest	Applies to persons liable to pay stamp duty (sections 120A-U)
		Credit interest from later of payment due date or date return filed
		Debit interest from original due date for tax
		Calculated including penalties
		Calculated until date tax paid/overpayment refunded
		Calculated on a daily basis
		Payments applied to interest first before reducing tax debt
		Credit interest assessable income for all taxpayers
		Debit interest deductible under normal tax rules
		Not charged if overdue duty less than $100
Civil penalty: evasion	Nil	Penalty imposed by IRD (section 141E) 150% of tax understatement
Civil penalty: abusive tax position	Nil	Penalty imposed by IRD (section 141D) 100% of tax understatement.
Civil penalty: gross carelessness	Penalty imposed by IRD. Section 57, S&CD Act penalty for late presentation = 1 cent for each complete $1 of the stamp duty payable.	Penalty imposed by IRD (section 141C): 40% of tax understatement.
	Section 58 penalty on unpaid duty = 1 cent for each complete $1 of all stamp duty remaining unpaid for every month.	
Civil penalty: unacceptable interpretation	Nil	Penalty imposed by IRD (section 141B): 20% of tax understatement
Civil penalty: lack of reasonable care	Penalty imposed by IRD. Section 57, S&CD Act penalty for late presentation = to 1 cent for each complete $1 of the stamp duty payable.	Penalty imposed by IRD (section 141A): 20% of tax understatement
	Section 58 penalty on unpaid duty = 1 cent for each complete $1 of all stamp duty remaining unpaid for every month.	
Criminal penalty: evasion	Sections 16,53,70,81 to 84,86D,86N, S&CD Act all contain subsections making particular failures to meet an obligation an offence. Fine on conviction up to $2,000 for S16 and up to $500 for all other sections. These subsections have been repealed.	Penalty imposed by Courts (section 143): 1st conviction a fine up to $25,000. Further convictions a fine up to $50,000. Prison for up to five years for evasion. Duties legislation amended to include criminal offences in TAA (new section 144, TAA)
	Sections 87,88,89,90,92A,93 and 94 and the subsections which relate to offences under sections 90 and 91.	All these offences under the Duties legislation are now covered by the generic penalties or specific penalties contained in the TAA 1994.
		S&CD Act - new section 102 applies offence and penalty provisions now contained in TAA to offences under S&CD Act

Table 7 - Gaming duty

Charge	Current rules	New TAA rules
Additional tax	No provisions to charge penalty	Late payment penalty applies to all (section 139B)
		5% late payment penalty imposed day after due date for payment
		2% incremental penalty every month thereafter
		Not charged if overdue duty less than $100
Interest	Interest on unpaid GMD (section 12F, Gaming Duties Act) and interest on unpaid casino duty (section 12Q)	Applies to all (sections 120A-U)
	Applies to all	
	No credit interest paid	Credit interest from later of payment due date or date return filed
	Debit interest from due date for paying duty	Debit interest from original due date for tax
	Penalties not applicable	Calculated including penalties
	Calculated to the date the duty is paid	Calculated until date tax paid/overpayment refunded
	Calculated monthly	Calculated on a daily basis
	Payments applied to unpaid duty first	Payments applied to interest first before reducing tax debt
	Credit interest not applicable, debit interest not an allowable deduction	Credit interest assessable income for all taxpayers; debit interest deductible under normal tax rules
	No minimum amount of interest to be charged	Not charged if overdue duty less than $100
Civil penalty: evasion	Nil	Penalty imposed by IRD (section 141E) 150% of tax understatement
Civil penalty: abusive tax position	Nil	Penalty imposed by IRD (section 141D) 100% of tax understatement
Civil penalty: gross careless-ness	Nil	Penalty imposed by IRD (section 141C) 40% of tax understatement
Civil penalty: unacceptable interpretation	Nil	Penalty imposed by IRD (section 141B) 20% of tax understatement
Civil penalty: lack of reason-able care	Nil	Penalty imposed by IRD (section 141A) 20% of tax understatement
Criminal penalty: evasion	Section 12L(8), Gaming Duties Act - failing to deduct or to pay deductions to IRD: if convicted a fine up to $500.	New section 18, Gaming Duties Act - provides for transition to new disputes resolution and penalty rules.
	Section 1: • Wilfully or negligently giving false information or misleading or attempting to mislead the Commissioner - if convicted a fine up to $1,000.	Penalty imposed by Courts (section 143): 1st conviction a fine up to $25,000; further convictions a fine up to $50,000.
	• Racing club failing to comply with sections 5(1) or 6(2) - if convicted a fine up to $200.	Prison up to five years for evasion.
	• Gaming machine operator failing to comply with section 12(D), or casino operator failing to comply with section 12(O) - if convicted a fine up to $200.	
	• Lottery organiser failing to comply with section 10 - if convicted a fine up to $200.	

Table 8 - Estate and gift duty

Charge	Current rules	New TAA rules
Additional tax	Penalty applies to all donors of dutiable gifts (section 51, E&GD Act for estate duty, section 83 for gift duty).	Late payment penalty applies to all donors of dutiable gifts
	5% penalty imposed 6 months after making gift	5% late payment penalty imposed day after payment due date; 2% incremental penalty every month thereafter
	No minimum amount to be charged	Not charged if overdue duty less than $100
Interest	All donors of dutiable gifts (sec 52, E&GD Act)	Applies to all donors of dutiable gifts
	No credit interest paid	Credit interest from later of payment due date or date return filed
	Debit interest from duty payment due date	Debit interest from original due date for tax
	Calculated including penalties	Calculated including penalties
	Calculated to the date the duty is paid refunded	Calculated until date duty paid/overpayment
	Calculated monthly	Calculated on a daily basis
	Payments applied to unpaid duty first	Payments applied to interest first before reducing tax debt
	No credit interest; debit interest not deductible	Credit interest assessable income for all taxpayers; debit interest deductible under normal tax rules
	No minimum amount of interest to be charged	Not charged if overdue duty less than $100
Civil penalty: evasion	Penalty imposed by IRD (section 51 for estate duty; section 83 f or gift duty). Both rates 5%	New section 95 of E&GD Act refers to the TAA offence provisions.
		Penalty imposed by IRD (section 141E): 150% of tax understatement
Civil penalty: abusive tax position	Nil	Penalty imposed by IRD (section 141D): 100% of tax understatement.
Civil penalty: gross careless-ness	Penalty imposed by IRD (section 51 for estate duty; section 83 for gift duty). Both rates 5%.	Penalty imposed by IRD (section 141C): 40% of tax understatement
Civil penalty: unacceptable interpretation	Nil	Penalty imposed by IRD (section 141B): 20% of tax understatement
Civil penalty: lack of reason-able care	Penalty imposed by IRD (section 51 for estate duty; section 83 for gift duty). Both rates 5%.	Penalty imposed by IRD (section 141A): 20% of tax understatement
Criminal penalty: evasion	Section 95, E&GD repealed. It dealt with offences for evasion.	Penalty imposed by Courts (section 143): 1st conviction a fine up to $25,000; further convictions a fine up to $50,000.
		Prison for up to five years for evasion.

Table 9 - Remissions

Current rules	New section 183A rules
If it is considered equitable to do so, the Commissioner may remit the additional tax and/or incremental additional tax	Reasonable cause: If the Commissioner is satisfied that the payment was not made or the return was not filed on time because of an event beyond the taxpayer's control (e.g., disaster, accident, illness, emotional or mental distress). An event is not an omission by an agent unless caused by an event that couldn't be anticipated and "could not have been avoided by compliance with accepted standards of business organisation and professional conduct". A taxpayer's financial position is not an excuse for non-payment. Reasonable cause only applies to late payment penalties and late filing penalties.
Remission could be carried out in limited circumstances only.	Late payment penalties, late filing penalties and interest may be remitted where the Commissioner is satisfied that it is consistent with his duty to collect the highest net revenue over time.
Additional tax may not be remitted over $5,000 without approval from the Minister of Finance.	Remission of late payment penalty, late filing penalty and interest will be at the Commissioner's discretion.
All incremental additional taxes from the date that the arrangement is entered into or section 157 of the TAA or similar are invoked, are remitted provided all payments are made in accordance with the agreement. This does not apply to the initial additional tax.	If an arrangement is entered into before the due date, 60% of the initial late payment penalty can be cancelled. All incremental additional tax after the date the arrangement is entered into or s157 or similar is invoked are to be cancelled. Cancellation is upon the taxpayer adhering to all the terms of the arrangement.
Application must be in writing.	Application must be made in writing.