ABSTRACT: This study investigates approaches to the management of tax debt in New Zealand and Australia. Levels of tax debt are high in both countries: 12 per cent of total tax revenue collected in New Zealand and 9 per cent in Australia. While both countries have a wide range of options to collect debt, Australia uses more of the available options and on a more frequent basis.

This study also investigates the recognition and reporting of tax debt in the government financial statements in Australia and New Zealand. International Financial Reporting Standards are used as the base line for the reporting of tax debts.

Three issues are identified in this study. First, while tax authorities have a range of tools to assist with tax debt collection, both the New Zealand and Australian tax authorities hold large amounts of tax receivables. This suggests that either the current tools are not being utilised to the greatest extent to reduce tax debt or that the tools are insufficient to achieve the objective of collecting the maximum amount of tax revenue taking into account available resources. Second, both countries have differences in the value of tax debt as defined by the tax authority and tax debt as determined in the government financial statements. Third, both countries have considerable amounts of tax debt that is defined by the tax authority as uncollectable. However, portions of these amounts appear to remain as assets in the balance sheets of the Crown. This appears to contradict the appropriate accounting treatment, where they would be impaired and written-off. The impact on the balance sheets and income statements is materially significant.

1.0 INTRODUCTION

This study compares the approaches to debt management of the tax authorities in Australia and New Zealand. Tax debts held by each agency are high. In New Zealand, the value of total tax debt held by the Inland Revenue Department (IRD) is 12 per cent of total annual tax revenue. In Australia, the equivalent value of tax debt held by the Australian Tax Office
(ATO) is 9.1 per cent. Thus, these are economically significant sums in both countries. However, large sums of debt are not collected, and significant amounts of penalties and interest that are imposed when tax is unpaid are also uncollected. This has a number of effects. First, it potentially undermines the integrity of the tax system. Second, it is likely to impact on the goodwill of compliant taxpayers towards the tax system to the extent that they are aware of the large amount of tax that is not collected. Third, the impact of the penalty regime is diluted in encouraging taxpayers to pay their tax on time and in full when tax is frequently uncollected.

It is acknowledged that tax debt is not solely a function of tax debt management. A range of other factors combine to impact on total tax debt levels, including the numerous factors that impact on a taxpayer’s decision of whether or not to pay tax, including their financial capacity to meet their obligations. However, tax debt management is an important function of tax administration and tax debt collection is an economically significant activity in society.

In New Zealand and Australia, once tax debts are due, they are deemed to be a debt to the government and payable to the tax authority. Where the debt is not settled at the due date, the tax authority will generally engage in some action to recover the debt. The first research issue addressed in this study relates to the debt management approaches in New Zealand and Australia. The study investigates the differences in approaches in the two countries and asks the question of what can be learned from the different methods adopted in each country. In addressing this question, the study does not include compliance measures. Instead it considers the processes that exist to collect tax debts once taxpayers have outstanding obligations with the tax authority. The second research question addressed in this study is whether the mechanisms for reporting tax debt by the respective tax agencies in New Zealand and Australia meet the requirements as outlined in International Financial Reporting Standards (IFRS).

The article commences in section two with some contextual information on tax debt in New Zealand and Australia. Section three follows and provides an outline of the IFRS that are relevant to the measurement and recognition of tax debt. This is followed by two sections, four and five, that explain the current approaches to debt management by the tax authorities in New Zealand and Australia. Section six engages in both a comparative discussion of the different treatments of tax debt in New Zealand and Australia, together with how well their reporting practices meet the requirements of IFRS as outlined in section three. Conclusions are drawn in section seven.

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3 Tax revenue collected in Australia in 2011/12 was A$301 billion, while tax debt is A$27.5 billion. The tax debt figure used in the calculation includes all tax debt, including that which is subject to appeal or investigation, and also includes debt that is likely to be uncollectable.
2.0 BACKGROUND

This section provides some background information on the tax debt situations of the two countries, commencing with New Zealand. The section outlines the general approach to debt management adopted by the IRD and the ATO, together with current levels of tax debt in each country.

2.1 New Zealand

The mission of the IRD is to ‘contribute to the economic and social wellbeing of all New Zealanders by collecting and distributing money’. The revenue collection function is the largest task of IRD, with responsibility for collecting approximately 89 per cent of government revenue.4 In the most recently reported period (2011/12), the IRD collected tax revenue of NZ$49.2 billion. The distribution function of IRD relates to some social assistance programs, such as Working for Families Tax Credits, Child Support and Paid Parental Leave. In addition, IRD are involved in the collection and redistribution of funds relating to KiwiSaver superannuation savings schemes and collection of Student Loan repayments. The IRD have additional functions in relation to providing policy advice. The overriding obligations for the IRD are to maintain the integrity of the tax system and to collect the highest net revenue that is practicable within the law having regard to available resources.5

IRD debt as at 30 June 2012, and for the two previous periods, is outlined in Table 1. Outstanding tax debt in the most recently reported period is $5.9 billion. This is approximately 12 per cent of the total tax collected in New Zealand in 2011/12.6 Of the total debt, NZ$2.1 billion, or 36 per cent is classified as non-collectable.7 Debt that is categorised as collectable is 7.6 per cent of total revenue collected. A large proportion of total debt is made up of interest and penalties at nearly 46 per cent in 2011/12.

Table 1: Inland Revenue Department Debt (2009/10 to 2011/12)8

<table>
<thead>
<tr>
<th>Debt type</th>
<th>2009/10 (NZ $M)</th>
<th>2010/11 (NZ $M)</th>
<th>2011/12 (NZ $M)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt under arrangement</td>
<td>$937.7</td>
<td>$1,146.6</td>
<td>$1,176.3</td>
</tr>
<tr>
<td>Other collectable debt</td>
<td>$2,548.6</td>
<td>$2,663.5</td>
<td>$2,582.7</td>
</tr>
<tr>
<td>Total collectable debt</td>
<td>$3,486.3</td>
<td>$3,810.2</td>
<td>$3,759.0</td>
</tr>
<tr>
<td>Total non-collectable debt</td>
<td>$1,664.3</td>
<td>$1,711.9</td>
<td>$2,157.4</td>
</tr>
<tr>
<td>Total debt</td>
<td>$5,150.6</td>
<td>$5,522.1</td>
<td>$5,916.4</td>
</tr>
<tr>
<td>Penalties and interest</td>
<td>$2,149.7</td>
<td>$2,359.0</td>
<td>$2,711.3</td>
</tr>
</tbody>
</table>

5 Tax Administration Act 1994, (TAA) ss.6(1) and 6A(3).
6 This figure includes all tax debts, that is, debts from all entities as well as individuals. The IRD cannot provide a breakdown of debt by debtor type.
7 Non-collectable debt is comprised of deferred debt, debt under dispute in the courts, assessments raised by the IRD when a tax return has not been filed by a taxpayer or debt that is with the Official Assignee or Liquidator.
Table 2 shows the aged debt of IRD over the same three-year period. Most of the individual cases (55 per cent) are less than one year old. However, the majority of the value of the debt (61 per cent) is older than two years, with only 21 per cent of total debt value less than one year old. A large proportion of this amount is comprised of interest and penalties. In the most recent year, the proportion of older debt increased. This is due to the change of focus on early intervention and debt prevention by the IRD.\(^9\) Despite this focus, total overdue debt increased by NZ$394 million (7 per cent) to NZ$5.9 billion in the 2011/12 period.\(^10\) The average value of outstanding debt per tax debtor in the most recently reported period is NZ$14,479.

### Table 2: Inland Revenue Department Aged Debt (2009/10 to 2011/12)\(^11\)

<table>
<thead>
<tr>
<th></th>
<th>2009/10</th>
<th>2010/11</th>
<th>2011/12</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>NZ $M</td>
<td>Cases</td>
<td>NZ $M</td>
</tr>
<tr>
<td>&lt; 1 year</td>
<td>$1,500.3</td>
<td>216,815</td>
<td>$1,377.7</td>
</tr>
<tr>
<td>1-2 years</td>
<td>$1,386.4</td>
<td>84,000</td>
<td>$1,387.7</td>
</tr>
<tr>
<td>2-5 years</td>
<td>$1,542.0</td>
<td>50,839</td>
<td>$1,787.7</td>
</tr>
<tr>
<td>&gt; 5 years</td>
<td>$721.9</td>
<td>13,660</td>
<td>$969.0</td>
</tr>
<tr>
<td>Total</td>
<td>$5150.6</td>
<td>363,814</td>
<td>$5,522.1</td>
</tr>
</tbody>
</table>

### 2.2 Australia

Similarly to the IRD in New Zealand, the ATO is the primary revenue collection agency in Australia, as well as acting in a redistribution role. The ATO has a broader range of tasks than the IRD, also being responsible for the key components of Australia’s compulsory superannuation system, managing the business operations of the Australian Valuation Office, and being custodian of the Australian Business Register. The role of the ATO is to ‘ensure the community has confidence in the administration of Australia’s taxation and superannuation systems’.\(^12\)

Current levels of tax debt held by the ATO are outlined in Table 3. Similarly to the IRD, the ATO has also experienced an increase in collectable debt.\(^13\) Collectable debt in Australia in 2011/12 represents 5.5 per cent of total collections, as shown in the last row of Table 3.\(^14\) This figure has remained relatively steady over the past three periods. However, collectable debt...

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\(^9\) Above, n.8, p.24.
\(^10\) Above, n.8, p.25.
\(^11\) Above, n.8, p.25.
\(^14\) Above, n.13, p.8.
debt increased by 18 per cent in the most recent period, while the number of collectable debt cases also increased by 10.5 per cent.\textsuperscript{15}

Table 3: Australian Tax Office Debt (2009/10 to 2011/12)\textsuperscript{16}

<table>
<thead>
<tr>
<th>Debt type</th>
<th>2009/10 (A $\text{BN})</th>
<th>2010/11 (A $\text{BN})</th>
<th>2011/12 (A $\text{BN})</th>
</tr>
</thead>
<tbody>
<tr>
<td>Collectable debt</td>
<td>$14.7</td>
<td>$14.1</td>
<td>$16.6</td>
</tr>
<tr>
<td>Debt subject to objection or appeal</td>
<td>$8.9</td>
<td>$8.1</td>
<td>$8.9</td>
</tr>
<tr>
<td>Insolvency debt</td>
<td>$3.9</td>
<td>$5.3</td>
<td>$6.2</td>
</tr>
<tr>
<td>Total debt</td>
<td>$27.5</td>
<td>$27.5</td>
<td>$31.7</td>
</tr>
<tr>
<td>Ratio of collectable debt to total cash collections</td>
<td>5.8%</td>
<td>5.2%</td>
<td>5.5%</td>
</tr>
</tbody>
</table>

Modelling undertaken by the ATO looks at over six billion items of data each week to determine the likelihood of payment across approximately three million cases.\textsuperscript{17} The objective of this analytical process is to improve ways of interacting with taxpayers in debt situations. In addition, all debts are risk-scored to estimate a particular taxpayer’s likelihood of repaying their debt, together with their capacity to do so.\textsuperscript{18}

### 3.0 INTERNATIONAL FINANCIAL REPORTING STANDARDS

This section outlines the financial reporting standards that govern the preparation and presentation of financial reports in New Zealand and Australia. As New Zealand and Australia both follow IFRS, the reporting requirements are identical in both countries. As the focus of this study is on the recognition of tax debts, these are typically reported in the category of ‘receivables’ in government financial statements. Thus, the focus of this section is on the recognition and measurement criteria of assets on the statement of financial position (balance sheet).

The objective of general purpose financial reporting is to:

\emph{provide financial information about the financial position, performance and changes in financial position of an entity that is useful to a wide range of users in making economic decisions...users of financial statements of New Zealand entities may also be interested in how well an entity has demonstrated its accountability in relation to a range of obligations including the entity’s financial performance and position.}

\textsuperscript{15} Above, n.13, p.53/58.
\textsuperscript{16} Above, n.13. Information has been requested from the ATO on the proportion of interest and penalties that comprise total debt, as well as the numbers of customers in debt.
\textsuperscript{17} Above, n.13, p.84.
\textsuperscript{18} Above, n.13, p.124.
compliance with legislation, regulations, common law and contractual arrangements.19

The preparation of financial statements is underpinned by a range of qualitative characteristics that are desirable in financial statements. In New Zealand, these include understandability; relevance, including materiality; faithful representation; and verifiability. These qualitative characteristics are used as a framework for analysis in section six.

An asset is defined in the New Zealand Framework as ‘a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity’.20 Paragraph NZ B49.1 of the Framework provides a definition of ‘future economic benefits’ for public entities as having the same meaning as the term ‘service potential’.21 Thus, tax receivable is recognised as an asset in the government financial statements.

Paragraph 54 of NZ IAS 1 Presentation of Financial Statements22 requires trade and other receivables to be shown as a separate line item on the Statement of Financial Position, while paragraph 55 requires ‘additional line items, headings and subtotals in the statement of financial position when such presentation is relevant to an understanding of the entity’s financial position’.23 Both New Zealand and Australia provide an expansion of the detail of their tax debt in the notes to the accounts. This is replicated in Tables 4 and 5 for New Zealand and Australia respectively.

Receivables are categorised for financial accounting as a financial asset. A financial asset is an asset that is either cash, or the contractual right to receive cash. Initial recognition of financial assets is established by NZ IFRS 9 Financial Instruments.24 Paragraph 3.1.1 of this standard states that an entity should recognise a financial asset when the entity ‘becomes party to the contractual provisions of the instrument’. Initial recognition is at fair value.25 Subsequent measurement of financial assets is either fair value or amortised cost. At the end of each reporting period, an entity is required to assess whether a financial asset is impaired.26

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20 Above, n.19, para B49.
21 ‘Assets provide a means for entities to achieve their objectives. Assets that are used to deliver goods and services in accordance with an entity’s objectives but which do not directly generate net cash inflows are often described as embodying “service potential”. Assets that are used to generate net cash inflows are often described as embodying “future economic benefits”’. Above, n.19, para NZ B49.1
22 New Zealand Equivalent to International Accounting Standard 1, Presentation of Financial Statements (NZ IAS 1), Issued November 2007 and incorporating changes up to and including 30 June 2011. This is the authoritative standard at the time the Financial Statements of the Government of New Zealand for the Year Ended 30 June 2012 were prepared.
23 The equivalent in Australia is para 54 of AASB 101 Presentation of Financial Statements, Australian Accounting Standards Board.
25 Above, n.24, para 4.1.
26 The equivalent in Australia is AASB 9 Financial Instruments, para 3.1.1 and 4.1.
Paragraph 8 of NZ IAS 36 *Impairment of Assets* states that ‘an asset is impaired when its carrying amount exceeds its recoverable amount’. Under paragraph 9 of the same standard, an entity should assess at the end of each reporting period whether there is any indication that an asset is impaired. Where an asset is impaired, the recoverable amount of the asset should be estimated. Under IAS 39 *Financial Instruments: Recognition and Measurement*, factors that indicate that a financial asset is impaired include default in payment. Where there is evidence that an impairment loss on financial assets has incurred, the entity must revise its estimate of payments or receipts. Specifically ‘the entity shall adjust the carrying amount of the financial asset ... to reflect actual and revised estimated cash flows’. Paragraph 63 of IAS 39 clarifies the impairment process:

> if there is objective evidence that an impairment loss on loans and receivables ... carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset’s carrying amount and the present value of future cash flows...discounted at the financial asset’s original effective interest rate.... The carrying amount of the asset shall be reduced either directly or through use of an allowance account. The amount of the loss shall be recognised in profit or loss.

### Table 4: Extract from the Financial Statements of the Government of New Zealand

<table>
<thead>
<tr>
<th>Type</th>
<th>30 June 2012 (SM)</th>
<th>30 June 2011 (SM)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax receivables</td>
<td>7,257</td>
<td>7,104</td>
</tr>
<tr>
<td>Levies, fines and penalty receivables</td>
<td>3,267</td>
<td>3,440</td>
</tr>
<tr>
<td>Social benefit receivables</td>
<td>502</td>
<td>480</td>
</tr>
<tr>
<td><strong>Sovereign Receivables</strong></td>
<td>11,026</td>
<td>11,024</td>
</tr>
<tr>
<td>Recovered from Deposit Guarantee Scheme receiverships</td>
<td>270</td>
<td>729</td>
</tr>
<tr>
<td>Trade and other receivables</td>
<td>9,660</td>
<td>9,927</td>
</tr>
<tr>
<td><strong>Total Receivables</strong></td>
<td><strong>20,956</strong></td>
<td><strong>21,690</strong></td>
</tr>
</tbody>
</table>

**By Maturity**

<table>
<thead>
<tr>
<th></th>
<th>30 June 2012 (SM)</th>
<th>30 June 2011 (SM)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expected to be realised within one year</td>
<td>15,173</td>
<td>14,916</td>
</tr>
<tr>
<td>Expected to be outstanding for more than one year</td>
<td>5,783</td>
<td>6,774</td>
</tr>
<tr>
<td><strong>Total Receivables</strong></td>
<td><strong>20,956</strong></td>
<td><strong>21,690</strong></td>
</tr>
</tbody>
</table>

---


28 The equivalent in Australia is paras 8 and 9 of AASB 136, *Impairment of Assets*, Australian Accounting Standards Board.


30 Above, n.29, para AG8. The Australian equivalent is para AG 8 of AASB 139 *Financial Instruments: Recognition and Measurement*.

31 However, para AG79 clarifies that short-term receivables with no stated interest rate may be measured at original cost if the effect of discounting is immaterial, as would be the case with tax debt.

32 The Australian equivalent is para 63 of AASB 139 *Financial Instruments: Recognition and Measurement*.

Table 5: Extract from the Consolidated Financial Statements for the Commonwealth of Australia

<table>
<thead>
<tr>
<th>Type</th>
<th>30 June 2012 ($M)</th>
<th>30 June 2011 ($M)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goods and services receivable</td>
<td>1,017</td>
<td>925</td>
</tr>
<tr>
<td>Recoveries of benefit payments</td>
<td>3,033</td>
<td>3,024</td>
</tr>
<tr>
<td>Taxes receivable</td>
<td>33,100</td>
<td>28,609</td>
</tr>
<tr>
<td>Other financial assets</td>
<td>59</td>
<td>108</td>
</tr>
<tr>
<td>Other</td>
<td>8,013</td>
<td>7,857</td>
</tr>
<tr>
<td>Less: Provision for doubtful debts – goods and services and other</td>
<td>(2,626)</td>
<td>(2,423)</td>
</tr>
<tr>
<td>Less: Provision for doubtful debts – personal benefits receivable</td>
<td>(671)</td>
<td>(841)</td>
</tr>
<tr>
<td>Less: Provision for doubtful debts – taxes receivable</td>
<td>(11,564)</td>
<td>(10,082)</td>
</tr>
<tr>
<td>Less: Provision for credit amendments</td>
<td>(2,882)</td>
<td>(1,299)</td>
</tr>
<tr>
<td>Total Other Receivables</td>
<td>27,479</td>
<td>25,878</td>
</tr>
</tbody>
</table>

Extract for Tax Receivables Only

| Taxes receivable                                                  | 33,100            | 28,609            |
| Less: Provision for doubtful debts – taxes receivable             | (11,564)          | (10,082)          |
| Total Taxes Receivable                                            | 21,536            | 18,527            |

The figures that are reported by the respective tax authorities as tax debt differ from those reported by the Crown as tax debts. Reconciliations were requested from the New Zealand Treasury and the Department of Finance in Australia for clarification of these figures. The New Zealand Treasury advised that the difference between the figure of $7.2 billion disclosed in the government accounts and the $5.9 billion disclosed by IRD is due to the consolidated view of taxes receivable reported by the Government. The consolidated view ($7.2 billion) incorporates two key components that result in differences in how the figures are reported. The first is receivables from the New Zealand Customs Service (e.g. excise duties) and the Ministry of Transport (e.g. motor vehicle registration). These figures are incorporated within the overall tax receivables figure thereby increasing the tax receivables figure. Second, receivables that are owed by other entities within the Crown (such as state-owned enterprises) are eliminated in the consolidated accounting process. This figure reduces the overall receivables amount.

A similar response was received from the Department of Finance in Australia. The consolidated Government financial statements include tax receivables of other agencies that collect tax (such as Customs and Border Protection) and exclude tax receivables owing by other government entities (which are eliminated on consolidation).

34 Commonwealth of Australia, 2012, Consolidated Financial Statements for the Year Ending 30 June 2012. Canberra: Commonwealth of Australia. Note 17: Advances Paid and Receivables. For greater clarity, tax information is reported separately at the end of the table as well as replicated in the format provided in the financial statements.
THE NEW ZEALAND APPROACH TO DEBT MANAGEMENT

Both the IRD and the ATO have a similar approach to debt recovery, which is to maximise the collection of tax debt. Under the Tax Administration Act 1994 (TAA) the Commissioner of Inland Revenue must collect the highest net revenue that is practicable within the law, having regard to: available resources; the promotion of compliance by all taxpayers; and the compliance costs incurred by taxpayers. However, recovery of tax must not place the taxpayer in a position of serious hardship or be an inefficient use of IRD resources.

IRD claim a ‘customer-centred approach’ that focuses on preventing debt from arising in the first instance; early intervention when debt does arise; and a focus of collection efforts on the cases that have the greatest prospect of collection. Where debt does arise, the IRD focus their efforts on early settlement of debt. This is because penalties and interest can quickly accumulate, resulting in the debt becoming unmanageable for the taxpayer. Moreover, the debt becomes more expensive for IRD to collect as it becomes older.

The most recent IRD annual report, communicates ‘a mix of new and innovative interventions for managing debt’. These include sending text messages and online advertising, including on social media outlets such as Facebook, to remind customers of payment deadlines. When payments are not made on time, calls are made to customers including the use of automatic dialler technology. This technology, together with the recruitment of extra specialist staff is claimed to have ‘significantly improved the capacity and effectiveness of our outbound calling campaigns’. In 2011/12, 81 per cent of tax due on 7 February was paid on time.

IRD disclose priority areas for recovery and enforcement areas, which currently include audit-assessed debt, the top high-risk customers, debt associated with large enterprises and high-wealth individuals. The IRD also acknowledge that these areas are those where the best prospect for debt collection exists.

4.0 THE NEW ZEALAND APPROACH TO DEBT MANAGEMENT

An instalment arrangement may be entered into by the IRD and the taxpayer. All taxpayers have the option to request an instalment arrangement when they are unable to meet their tax obligations in full and when entering into an instalment arrangement is likely to assist in maximising tax debt collection. The advantage, for the IRD, of entering into instalment arrangements is that it provides some certainty of timing of revenue collection. Moreover, the earlier the collection process commences, the more likely the debt will be collected as

35 TAA, s 6A(3).
36 TAA, s.176(2)(a)-(b).
37 Above, n.8, p.25.
38 Above, n.8, p.24.
39 Above, n.8, p.24.
40 Above, n.8, p.24.
41 Above, n.8, p.24.
42 Above, n.8, p.25.
additional penalties will not accrue while the instalment arrangement is being adhered to. Additional penalties will not accrue while the instalment arrangement is being adhered to.\textsuperscript{43} Interest will continue to be charged throughout the duration of the instalment arrangement. The IRD will negotiate with the taxpayer to determine what method of payment best suits the tax debtor’s financial circumstances.\textsuperscript{44}

The value of debt in instalment arrangements is currently NZ$1.2 billion, or approximately 20 per cent of total current debt. As at June 2012, 53,187 taxpayers were paying their tax by instalment arrangement.\textsuperscript{45}

### 4.2 Deduction Notices

Deduction notices may be used by the IRD under certain circumstances. A deduction notice requires a third party to make deductions from amounts that are ‘payable or will become payable by that third party to a taxpayer who has tax arrears’.\textsuperscript{46} Deduction notices can ‘require any person’ to deduct the amount owed in full or in part and require the deduction to be paid to the IRD.\textsuperscript{47} Deduction notices may be used where taxpayers have defaulted on payment of income tax, interest, or civil penalties. The TAA places some limits around the amounts permitted to be deducted. For example, for employers the amount must be the lesser of 10 per cent per week of the income tax due or 20 per cent of the wages or salary payable, and $10 per week.\textsuperscript{48} Deduction notices are usually issued to banks or employers. The IRD can prosecute banks for non-compliance with a deduction notice.\textsuperscript{49}

Information was requested from the IRD pertaining to the use of deduction notices. Specifically, an \textit{Official information Act 1982} request was made asking for the number of deduction notices that were issued by the IRD over the past three years. The IRD advised that they were unable to extract information from their systems that would isolate only outstanding tax. For the purposes of this research, only deduction notices relating to outstanding tax were relevant, rather than, for example, deduction notices that were issued in relation to child support or student loan debt. Therefore, it has not been possible to ascertain how frequency deduction notices are used for the purposes of assisting with tax collection in New Zealand.

### 4.3 Writing-Off Penalties and Interest

Use-of-money interest is charged at 8.4 per cent on underpayments or non-payments of tax.\textsuperscript{50} However, there are a range of circumstances where the IRD may write off penalties and interest. These remission provisions exist to allow the IRD to ‘accommodate circumstances

\textsuperscript{44} Above, n.43, para 11. This will also include frequency and method of payment (para 74).
\textsuperscript{45} Data received under the \textit{Official Information Act 1982}, 9 May 2013.
\textsuperscript{46} Inland Revenue Department, 2011, Standard Practice Statement SPS 11/04 \textit{Compulsory Deductions from Bank Accounts}, para 5.
\textsuperscript{47} TAA, s.157
\textsuperscript{48} TAA, s.157(3)(a)(i).
\textsuperscript{49} TAA, s.157(A)(1)(b).
\textsuperscript{50} Rate applicable as at November 2013.
in which charging a penalty of interest is inappropriate'. Penalties and interest may be remitted where the events leading to their existence can be reasonably justified or where a ‘qualifying event’ exists.

The IRD will consider certain factors in deciding whether remission is appropriate. These include whether the penalty or interest was charged correctly. Situations where the IRD somehow contributed to the problem, such as by providing incorrect advice to the taxpayer or through a delay in processing will also be taken into account. In addition, consideration will be given to whether the penalty was the result of genuine oversight or a one-off situation.

The amounts of penalties and interest that were applied, collected and written-off in New Zealand over the three most recently reported periods are outlined in Table 6. What is visible from the highlighted rows is that in each of the three years, over half of the penalties applied were written off. Moreover, in the two most recent periods, nearly half of the interest applied was also written off.

Table 6: Penalties and Interest Applied, Collected and Written-off in New Zealand (2009/10 to 2011/12)

<table>
<thead>
<tr>
<th></th>
<th>2009/10</th>
<th>2010/11</th>
<th>2011/12</th>
</tr>
</thead>
<tbody>
<tr>
<td>Penalties applied</td>
<td>$343.0</td>
<td>$346.2</td>
<td>$451.6</td>
</tr>
<tr>
<td>Penalties collected</td>
<td>$110.0</td>
<td>$121.9</td>
<td>$146.1</td>
</tr>
<tr>
<td>Penalties written off</td>
<td>$198.6</td>
<td>$193.0</td>
<td>$244.3</td>
</tr>
<tr>
<td>Interest applied</td>
<td>$500.7</td>
<td>$263.2</td>
<td>$280.9</td>
</tr>
<tr>
<td>Interest collected</td>
<td>$412.1</td>
<td>$147.2</td>
<td>$158.1</td>
</tr>
<tr>
<td>Interest written off</td>
<td>$104.4</td>
<td>$120.1</td>
<td>$130.5</td>
</tr>
<tr>
<td>% Penalties collected</td>
<td>32.1%</td>
<td>35.2%</td>
<td>32.4%</td>
</tr>
<tr>
<td>% Penalties written off</td>
<td>57.9%</td>
<td>55.7%</td>
<td>54.1%</td>
</tr>
<tr>
<td>% Interest collected</td>
<td>82.3%</td>
<td>55.9%</td>
<td>56.3%</td>
</tr>
<tr>
<td>% interest written off</td>
<td>20.9%</td>
<td>45.6%</td>
<td>46.5%</td>
</tr>
</tbody>
</table>

Values of penalties and interest written off as a proportion of total tax collected are low at less than two per cent of total tax collected in each year. However, these values as a proportion of outstanding debt are reasonably high: penalties and interest are 16.4 per cent, 11 per cent and 12.4 per cent in 2009/10, 2010/11 and 2011/12 respectively.

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52 Above, n.51, paras 6 and 7. There are a number of events that meet the criteria of a qualifying event, including where records have been destroyed or are unable to be accessed; or other priorities created by a qualifying event result in taxpayers being unable to make payments or file returns.
53 Above, n.51, para 46.
54 Data on penalties and interest provided by the New Zealand IRD under the Official Information Act 1982, 22 February 2013.
55 Penalties and interest written off and collected will not total 100 per cent as there are timing differences in the year that the penalty is applied and the year that it is collected or written off.
In order for remission requests to be actioned, the tax that the penalty or interest applies to must have been paid.\(^{56}\) In addition, there are some penalties where remission will not be considered, such as for shortfall penalties, except for those imposed under section 141AA of the TAA.\(^{57}\)

### 4.4 Writing-Off Outstanding Debt

A further remission option for the IRD is to write-off outstanding tax debt. While the duty remains to collect the maximum amount of tax revenue over time, in some situations the only cost-effective outcome is to write-off all or some of the unpaid amounts, for example, in situations where it may utilise significant resources to pursue the tax debt. However, the IRD have a duty to protect the integrity of the tax system and the Commissioner of Inland Revenue must have regard to the importance of the penalty and interest in promoting compliance by other taxpayers.\(^{58}\) Where tax has been remitted, interest will also be remitted.\(^{59}\)

A taxpayer may apply for financial relief when recovery of outstanding tax will place them in a position of serious hardship.\(^{60}\) Similarly to the criteria for remission of penalties and interest, outstanding tax cannot be written off where the taxpayer has been liable for a shortfall penalty for taking an abusive tax position under section 141D(2), tax evasion under section 141E(1) or a similar act, even where this will place the taxpayer in a position of serious hardship.\(^{61}\)

While all cases are decided on their own merit, some circumstances provide for the IRD to write off outstanding amounts. These circumstances are outlined in the TAA. In the first instance, the Commissioner may write off outstanding tax that cannot be recovered.\(^{62}\) Specific circumstances include bankruptcy, liquidation, or when a taxpayer’s estate has been distributed.\(^{63}\) However, it is possible for tax debt to be reinstated after it has been written off if a taxpayer’s financial circumstances change.\(^{64}\)

The IRD Standard Practice Statement relating to writing off outstanding tax outlines a number of factors that have been established by case law as relevant to the decision. These include the circumstances that led to the tax debt; the nature and extent of co-operation and

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\(^{56}\) Above, n.51, para 10.

\(^{57}\) Section 141AA of the TAA relates to non-resident contractors.

\(^{58}\) TAA, s.183D(2).

\(^{59}\) TAA, s.183E(a).

\(^{60}\) TAA, s.177. Serious hardship is defined in section 177A of the TAA as including significant financial difficulties that arise due to the taxpayer’s inability to meet minimum living expenses according to normal community standards; the costs of medical treatment; serious illness suffered by the taxpayer or the taxpayer’s dependants; or the cost of education for the taxpayer’s dependants.

\(^{61}\) Inland Revenue Department, Standard Practice Statement SPS 06/02 Writing off outstanding tax, Retrieved from www.ird.govt.nz, March 2013, paras 11 and 75.

\(^{62}\) TAA, 1994, s.177C(1). Small amounts, not exceeding $100 will be written off (s.177C(1C)).

\(^{63}\) TAA, s.177C(2)(a)-(c).

\(^{64}\) TAA, s.177C(4)
negotiation entered into by the taxpayer; the speed and extent of information provided by the taxpayer; and IRD duties under the TAA.\(^{65}\)

Tax debt written off in New Zealand, and this figure as a proportion of collectable debt, over the past three years is shown in Table 7. Typically, around ten per cent of collectable debt is written off in each year.

Table 7: Tax Debt Written-off in New Zealand (2009/10 to 2011/12)\(^{66}\)

<table>
<thead>
<tr>
<th></th>
<th>2009/10</th>
<th>2010/11</th>
<th>2011/12</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt written off</td>
<td>$316M</td>
<td>$424M</td>
<td>$435M</td>
</tr>
<tr>
<td>Debt written off as a proportion of collectable debt</td>
<td>9%</td>
<td>11.1%</td>
<td>11.6%</td>
</tr>
</tbody>
</table>

4.5 Other Options

Prosecution is a measure of last resort for the IRD. However, it may occur where ‘flagrant and on-going failure to comply with the taxpayers’ obligations and where recovery is dubious or is likely to result only in a relatively minor proportion of the overall outstanding debt being recovered’.\(^{67}\) The IRD take only a small number of criminal prosecutions each year, generally averaging around 60-70 per annum.

A further option for those who cannot meet their tax debts in New Zealand is to apply for bankruptcy or a ‘no asset procedure’.\(^{68}\) Filing for bankruptcy or entering into a no asset procedure will stop the IRD from seeking further payments from the taxpayer and outstanding debts will be written off.\(^{69}\) In the year ending June 2012, 578 taxpayers declared bankruptcy and had tax debts written off.\(^{70}\)

5.0 THE AUSTRALIAN APPROACH TO DEBT MANAGEMENT

Similarly to New Zealand, the approach of the ATO is to attempt to collect debt in its early stages, before it becomes unmanageable with accumulation of interest and penalties. The individual circumstances of each taxpayer will be taken into account when determining the options that are available to that taxpayer, including their historical patterns of payment and filing. There are a range of options available to individual taxpayers and small businesses that are experiencing short term financial difficulty. A key focus of debt management in Australia is small business, as these debts account for around two-thirds of collectable debt.\(^{71}\)

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\(^{65}\) Above, n.61, para 42.
\(^{66}\) Data received under the Official Information Act 1982, 3 May 2013.
\(^{67}\) Above, n.61, para 43.
\(^{68}\) A ‘no asset procedure’ is an alternative to bankruptcy for individuals who are insolvent.
\(^{70}\) Advised by the IRD under an Official Information Act 1982 request, 3 May 2013.
\(^{71}\) Above, n.13, p.58.
Debt collection activity will normally commence with the issuance of a notice calling for payment of the outstanding amount. This occurs prior to the debt being referred for collection activity. Three primary stages in the debt collection process follow. The first is early intervention, which incorporates telephone, written or text message contact with the taxpayer; entering into instalment arrangements; and may involve the engagement of an external debt collection agency. The second stage is firmer action including garnishee notices, director penalty notices and statutory demands. The third, and most serious stage, is where legal action may be taken, including bankruptcy proceedings or liquidation. These, together with other options, are discussed in the sub-sections below.

5.1 Instalment Arrangements

Under section 255-15 of Schedule 2 to the *Tax Administration Act 1953*, the Commissioner of Taxation may ‘permit you to pay an amount of tax-related liability by instalments under an arrangement between you and the Commissioner’. Instalment arrangements are often referred to as ‘tailored payment arrangements’ by the ATO. As at 30 June 2012, there were 280,000 payment arrangements in place with a total value of A$3.8 billion. Of these, 35,900 were interest free arrangements worth A$688 million. Interest-free arrangements are discussed in section 5.3.

When deciding whether to enter into an instalment arrangement with a taxpayer, the Commissioner will make this decision in accordance with the risk management guidelines as established for the ATO. A range of factors will be taken into account in making the decision including the circumstances that led to the creation of the debt, the taxpayer’s financial situation, the stage that legal recovery action has reached, ability to make payment, risk to the tax authority in accepting an instalment payment arrangement, solvency of the taxpayer, the historical pattern of compliance of the taxpayer, alternative collection options and willingness of the taxpayer to enter into repayment arrangements.

For taxpayers with debts of less than A$25,000 there is no need to speak to a tax officer to commence an instalment arrangement. This may be done online, with the use of online calculators to assist in calculating suitable payment arrangements. Where the taxpayer is a business, the ATO may require demonstration of business viability. This requires the provision of information on the financial performance and position of the entity to the ATO within an agreed timeframe. Additional information may be sought on how the debt arose and steps taken to mitigate the debt. For taxpayers with debts in excess of A$25,000 it is necessary to talk to an ATO tax officer and provide information in relation to the debt, how it

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73 Above, n.13, p.44.
74 Above, n.13, p.44.
76 Above, n.75.
arose, details relating to capacity to pay instalments, income, expenses, assets and liabilities, other financing options, and details of debtors and other creditors where applicable.

5.2 Deduction Notices

Section 260-5 of Schedule 2 to the *Tax Administration Act 1953* provides the Commissioner of Taxation with the authority to require a third party to pay money to the Commissioner, rather than paying it to the tax debtor. This is known as a ‘garnishee power’ and is actioned by a ‘garnishee notice’ issued under the *Tax Administration Act 1953*.77 The garnishee notice will specify the timing and value of payments. The garnishee notice may be issued to an employer for deduction of a proportion of the taxpayer’s wages or salary, or it may be issued to a financial institution for a lump sum amount. Garnishee notices may also be issued to parties such as solicitors.

Where the garnishee notice relates to wages or salaries, the ATO will not usually seek to garnish more than 30 cents in the dollar of the salary or wages payable.78 However, a higher proportion may be sought where the tax debtor has alternative sources of income or where it would be fair and equitable to do so.79

A garnishee notice may also be served on a superannuation fund. However, this will not become effective until the tax debtor’s benefits are payable under the rules of the fund, i.e. when the debtor reaches the age of retirement or dies. Similarly, a notice may be served in respect of the proceeds of life insurance policies80 or a company in which the tax debtor holds shares.81

Garnishee notices appear to be used reasonably frequently by the ATO. Table 8 shows the number of garnishee notices issued in 2007/08 and the two subsequent periods.82

**Table 8: Garnishee Notices Issued by the ATO**

<table>
<thead>
<tr>
<th></th>
<th>2007/08</th>
<th>2008/09</th>
<th>2009/10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Garnishee Notices</td>
<td>10,356</td>
<td>10,761</td>
<td>9,428</td>
</tr>
</tbody>
</table>

5.3 Writing-Off Penalties and Interest

The General Interest Charge, currently charged at 9.6 per cent,83 will accrue from the date the tax obligation is due until the amount is settled in full. However, section 8AAG of the *Tax Administration Act 1953* provides for remission of the General Interest Charge. The Commissioner of Taxation may only remit this under three circumstances:

77 Section 260-5(2).
78 Above, n.72, para 108.
79 Above, n.72, para 108.
80 Above, n.72, para 118/119.
81 Above, n.72, para 122.
82 More recent data has been requested from the ATO under a *Freedom of Information* request.
83 The General Interest Charge is updated quarterly. This is the rate for the October - December 2013 quarter.
(1) Where the circumstances that contributed to the delay in payment were not caused by an act or omission of the taxpayer, and the taxpayer took reasonable action to mitigate the effects of the circumstance.

(2) Where it would be fair and reasonable to remit all or part of the charge, having regard to the circumstances of the case.

(3) Where special circumstances exist that mean that it is fair and reasonable to remit the charge, or it is otherwise appropriate to do so. 84

Taxpayers must generate a request for all or part of the General Interest Charge to be remitted and the onus is generally on the taxpayer to demonstrate that remission is warranted. 85

Factors that will be taken into account in the outcome are the individual circumstances of the taxpayer and the factors that generated the late payment.

Where the circumstances of the taxpayer do not qualify to have the General Interest Charge written off, it will continue to accrue on outstanding amounts in most cases. However, small businesses may qualify for an interest-free repayment arrangement if they meet certain criteria. These criteria include having annual turnover under A$2 million; tax debt of less than A$50,000, which has been outstanding for less than 12 months; a good payment and filing record; an inability to obtain short-term financing from other sources; the ability to show that the business is a viable entity; and the ability to enter into a repayment arrangement that will result in the outstanding debt being repaid within 12 months. The maximum time the taxpayer will qualify for the interest-free period is 12 months.

The value of penalties and interest written off in the most recently reported period was A$2.0 billion. 86 The breakdown of penalties and interest that was applied, remitted and collected in Australia over the three most recent periods is outlined in Table 9. The table indicates that, in general, lower amounts of both interest and penalties are written off in Australia than in New Zealand.

Table 9: Penalties and Interest Applied, Remitted and Collected in Australia (2009/12) 87

<table>
<thead>
<tr>
<th></th>
<th>2009/10</th>
<th>2010/11</th>
<th>2011/12</th>
</tr>
</thead>
<tbody>
<tr>
<td>Penalties applied</td>
<td>$1,444.0</td>
<td>$1,221.0</td>
<td>$1,729.0</td>
</tr>
<tr>
<td>Interest applied</td>
<td>$2,639.0</td>
<td>$3,331.0</td>
<td>$4,782.0</td>
</tr>
<tr>
<td>Penalties collected</td>
<td>$440.0</td>
<td>$270.0</td>
<td>$564.0</td>
</tr>
<tr>
<td>Penalties written off</td>
<td>$439.0</td>
<td>$544.0</td>
<td>$391.0</td>
</tr>
<tr>
<td>Interest collected</td>
<td>$2,202.0</td>
<td>$2,935.0</td>
<td>$2,402.0</td>
</tr>
</tbody>
</table>

84 Tax Administration Act 1953, s.8AAG(1)-(5).
86 Above, n.13, p.62.
87 Above, n.13; and Australian Tax Office, 2011, Annual Report 2010/11, Retrieved from www.ato.gov.au, February 2013. Due to the sampling approach used, and the differences in timing between the period penalties were applied, collected and/or remitted, the figures will not add up to 100% in any year.
### 5.4 Writing-Off Outstanding Debt

The Minister for Finance has the power to waive a tax debt. However, the Commissioner of Taxation can approve release from payment of some tax debts where serious hardship exists. Taxpayers who are experiencing ‘serious hardship’ have the right to apply for some relief on their tax liabilities. Serious hardship exists when ‘you are unable to provide food, accommodation, clothing, medical treatment, education or other necessities for you or your family or other people for whom you are responsible’. The most common condition under which debt relief is provided is where there is a moral obligation, rather than a legal obligation to do so. Information on expenses, assets, income, and other supporting evidence is required to demonstrate that serious hardship exists for a taxpayer.

Where serious hardship is established, it is possible for taxpayers to apply for relief from payment of income tax, fringe benefit tax, pay-as-you-go instalments, and some of the penalties and interest associated with these taxes. This option is only available to individual taxpayers and taxpayers operating as a sole trader, i.e., it is not available to companies, trusts and partnerships. The tax release provisions do not apply to amounts of pay-as-you-go deductions that have not been remitted or paid to the ATO; interest on judgment costs; legal costs; sales tax; company tax instalments; indirect taxes; higher education contributions; child support payments; and court imposed fines and costs, among others.

Where core tax debt is written off by the ATO, it may be because it has become irrecoverable (e.g. due to insolvency or bankruptcy) or uneconomical to collect (e.g. where the taxpayer has no assets and there is little chance of collection). Factors that are taken into account in determining whether a debt is uneconomical to pursue include: the amount of revenue involved; the length of time the debt has been outstanding, including steps taken to recover the debt; the likely costs of continuing action to recover the debt, including likely recovery of any costs awarded; advice provided by the ATO solicitor; and the type of revenue involved. Debts may be considered uneconomical to pursue where the debtor has no assets, where notification has been received from a trustee or administrator that the debtor’s estate has

<table>
<thead>
<tr>
<th></th>
<th>$1,681.0</th>
<th>$1,889.0</th>
<th>$1,643.0</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest written off</td>
<td>30.5%</td>
<td>22.1%</td>
<td>32.6%</td>
</tr>
<tr>
<td>% Penalties collected</td>
<td>30.4%</td>
<td>44.6%</td>
<td>22.6%</td>
</tr>
<tr>
<td>% Penalties written off</td>
<td>83.4%</td>
<td>88.1%</td>
<td>50.2%</td>
</tr>
<tr>
<td>% Interest collected</td>
<td>63.7%</td>
<td>56.7%</td>
<td>34.4%</td>
</tr>
</tbody>
</table>

91 Above, n.89.
92 Above, n.13, p.59.
93 Above, n.89.
insufficient assets to settle the debt; or where a company has ceased operating and no assets remain.\textsuperscript{94}

In the most recently reported period (2011/12), the ATO wrote off A$2.6 billion.\textsuperscript{95} In the previous period, A$3.8 billion was written off. However, while debts may be written off the Commissioner retains the ability to reinstate debts where it becomes likely that recovery action may be successful.\textsuperscript{96}

5.5 Other Options

The ATO use external debt collection agencies to collect low-value debts. Debts are only referred to debt collection agencies where taxpayers have failed to work with the ATO to arrange settlement of the outstanding debt. In the most recent period, 300,020 cases, with a total value of A$1.6 billion, were referred to debt collection agencies.\textsuperscript{97} This resulted in collections of A$1.3 billion.\textsuperscript{98}

A further option that may be facilitated by the ATO where some or all of the tax debt is under dispute is known as a ‘50/50 arrangement’. The expectation is that the taxpayer will pay at least 50 per cent of any disputed amounts, in addition to other outstanding tax debts. The balance of payment may be deferred until the dispute is settled.\textsuperscript{99} Where the taxpayer’s objection is unsuccessful, only 50 per cent of the General Interest Charge will be charged from the date that the 50 per cent payment was made. In situations where taxpayers have been selected as a test case and a 50/50 arrangement is entered into, the General Interest Charge remission will reduce.

Legal action may also be taken by the ATO where tax debt remains outstanding despite attempts by the ATO to collect the amount. This may involve the ATO filing a claim or summons with the relevant court in the state of the taxpayer. This will result in the court recognising the debt, which allows the ATO to execute the judgment debt. One of the options that may result from this process is the ATO filing a bankruptcy notice. This requires the taxpayer to settle the obligation within 21 days and if this is not achieved, a creditor’s petition may follow, which will result in the taxpayer being made bankrupt. Alternatively, the taxpayer may voluntarily declare bankruptcy.

The ATO may also issue a statutory demand where a company has not met its tax debts. This will require a company to settle their tax debt within 21 days; otherwise the ATO may use the act of non-payment as evidence that the entity is insolvent. In these situations, the ATO have three months from the compliance date specified in the statutory demand to file an application in the Federal Court to liquidate the company. The ATO will usually issue

\textsuperscript{94} Above, n.89.
\textsuperscript{95} Above, n.13, p.59.
\textsuperscript{96} Above, n.13, p.238.
\textsuperscript{97} Above, n.13, p.59.
\textsuperscript{98} Above, n.13, p.59
\textsuperscript{99} Above, n.75. Not all debts may be eligible for inclusion in a 50/50 arrangement. For example, debts arising under the\textit{Superannuation Guarantee (Administration) Act 1992}.}
director penalty notices (discussed below) before seeking to have a company liquidated, where the debts are due to withholding tax provisions.  

Table 10 outlines the figures on ATO-initiated bankruptcy and liquidations in Australia. The figures indicate significant increases in the numbers of both ATO-initiated bankruptcies and company liquidations in Australia over the three year period investigated. This pattern may reflect the harsher economic conditions that have existed over this period.

**Table 10: ATO-Initiated Bankruptcy and Wind-ups in Australia**

<table>
<thead>
<tr>
<th></th>
<th>2009/10</th>
<th>2010/11</th>
<th>2011/12</th>
</tr>
</thead>
<tbody>
<tr>
<td>ATO-initiated bankruptcies</td>
<td>397</td>
<td>462</td>
<td>519</td>
</tr>
<tr>
<td>Total bankruptcies</td>
<td>27,507</td>
<td>23,102</td>
<td>22,176</td>
</tr>
<tr>
<td>ATO-initiated bankruptcies as a percentage of total bankruptcies</td>
<td>1.4%</td>
<td>2.0%</td>
<td>2.34%</td>
</tr>
<tr>
<td>ATO-initiated liquidations</td>
<td>493</td>
<td>1,066</td>
<td>1,555</td>
</tr>
<tr>
<td>Total liquidations</td>
<td>9,365</td>
<td>9,780</td>
<td>10,818</td>
</tr>
<tr>
<td>ATO-initiated liquidations as a percentage of total wind-ups</td>
<td>5.26%</td>
<td>10.9%</td>
<td>14.4%</td>
</tr>
</tbody>
</table>

The ATO have ‘director penalty notices’ that may be issued to company directors when the company fails to meet its pay-as-you-go and superannuation guarantee charge withholding obligations. In these situations, the director becomes personally liable for a penalty equal to the unpaid amount. The issuing of a director penalty notice allows the ATO to commence legal action to recover the penalty.

Part IVA of the *Tax Administration Act 1953* provides the Commissioner of Taxation with the power to issue a departure prohibition order, which will stop the tax debtor from departing Australia until the tax obligation is settled in full, or acceptable repayment arrangements are established. Certain conditions must exist for the Commissioner to exercise this power, including the belief that a departure prohibition order is necessary to ensure that the tax debtor does not depart Australia without discharging the tax liability or making arrangements to settle the liability.

Finally, a ‘freezing order’ may be used when tax debtor actions to dispose of assets are likely to result in an unacceptable level of risk to payment of a tax liability, or enforcement of a judgement. A freezing order is ‘a form of injunction that is used to restrain the respondent or their agents from removing assets from the jurisdiction or otherwise disposing of or

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102 Data has been requested from the ATO on how many director penalty notices were issued in recent periods.

103 Above, n.71, para 129.

104 Data has been requested from the ATO on how many departure prohibition orders were issued in recent periods.

105 Above, n.72, para 171. These are also known as Mareva injunctions or asset preservation orders.
dealing with those assets pending further orders by the court’. It appears that freezing orders are used infrequently in Australia. For example, the ATO report that only one of these injunctions was undertaken in 2007/08, five in 2008/09 and nine in 2009/10.

6.0 DISCUSSION

This section discusses both issues addressed in the study. It starts with an analysis of the different approaches to tax debt management in New Zealand and Australia, addressing measures of efficiency and general approaches to tax debt management. The section later discusses the recognition and measurement approaches of tax debt by the two tax authorities, and considers how well these meet the requirements of IFRS as outlined in section three.

6.1 Efficiency

IRD expenditure on management of debt and outstanding returns in 2011/12 was NZ$109 million. The proportion of expenditure on debt management to outstanding debt in IRD is 1.84 per cent. From an efficiency of collection perspective, IRD are highly efficient at collecting debt. At June 2012, the tax debt recovery cost is $2.86 for collecting $100 of overdue revenue. The average amount owed per IRD debtor as at June 2012 was $14,479.

IRD expenditure on taxpayer audit in 2011/12, which includes identifying risks to revenue and undertaking audit activities, was $169 million. Expenditure on this category of expenditure as a percentage of total debt is 2.86 per cent for the IRD.

Collectable debt as a proportion of total tax revenue collected is higher in New Zealand than in Australia. This measure is 7.65 per cent in New Zealand, and 5.5 per cent in Australia. While this measure may indicate that New Zealand is less efficient at debt collection than Australia, it is also influenced by other actions, such as the amounts of tax debt that are written off in each country. Moreover, the policy arrangements that influence overall tax compliance have a significant impact on tax debt that is generated in the first instance, which similarly impacts on levels of tax debt. Collectable debt in New Zealand has remained similar over the past two periods, whereas it has increased by 18 per cent in Australia. The ATO suggests that this reflects the harsher economic conditions in recent periods. The IRD

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106 Above, n.72, para 172.
107 Data has been requested from the ATO on how many freezing orders were issued in recent periods.
109 Data has been requested from the ATO on the cost of collection of outstanding debt.
111 Data provided under the Official Information Act 1982, 9 May 2013. Equivalent data has been requested from the ATO under a Freedom of Information request.
113 Equivalent data has been requested from the ATO under a Freedom of Information request.
also report a stronger focus on new debt and attempting to address this as early as possible, which may impact on levels of new debt that is generated.

Total amounts written off in New Zealand in 2011/12 are NZ$809 million, and in Australia over the same time period are A$4,634 million. These figures include interest and penalties written off, as well as core tax. The values written off in Australia are 5.7 times the amount written off in New Zealand and would appear to be a reasonable approximation for the difference in population size. As a proportion of total tax collected, the New Zealand write-offs are slightly higher at 1.65 per cent of total tax revenue collected, while Australia is 1.54 per cent of total tax revenue collected.

6.2 General Approach to Debt Management

Both the IRD and the ATO have relatively straightforward systems to allow taxpayers to enter into instalment arrangements. In the most recently reported period, approximately 20 per cent of New Zealand’s total outstanding debt was under an instalment arrangement. In Australia the proportion was lower, at around 12 per cent.

The IRD write-off higher proportions of penalties and interest than the ATO. In the most recent period, 54 per cent of penalties were written off and 47 per cent of interest was written off in New Zealand. By way of comparison 22 per cent and 34 per cent of penalties and interest were written off, respectively, in Australia.

Similar proportions of core tax are written off in each country. In New Zealand, NZ$435 million was written off in 2011/12, which is approximately 7.4 per cent of total debt. In Australia, a slightly higher proportion was written off, at 8.2 per cent of total debt.

In New Zealand, 578 taxpayers declared bankruptcy in 2011/12 and had tax debts written off as a result. This number is higher than the total number of ATO-initiated bankruptcies in Australia, which totalled 519 in the same period. As the population of Australia is approximately 5.2 times that of New Zealand, it was expected that tax related bankruptcies in Australia would be around five times greater than that in New Zealand, rather than less. When ATO-initiated liquidations are included, this totals 2,074 in 2011/12, which is still relatively lower than New Zealand when adjusted for the differences in population size.

In summary, both the IRD and the ATO have high levels of tax debt. However, debt held by the IRD as a proportion of total tax revenue is higher in New Zealand than in Australia. Both tax agencies have similar tools available to them to address debt management. However, these tools appear to be used differently. The IRD has a significantly higher proportion of debtors in instalment arrangements. However, the ATO have higher measures in some of the more punitive forms of debt collection. Notwithstanding this, the IRD initiate higher proportions of tax-related bankruptcies than the ATO.

6.3 Reporting in Financial Statements

When taking into account the size, nature and function of the tax debt, it was expected that it would be disclosed with a high level of detail. In addition, it was expected that it would be
possible to reconcile the information in the tax authority’s annual reports to that reported in
the government’s annual reports. While it was possible, it was only possible after
clarification and explanation was sought from the government department responsible for the
production of the financial statements for the Crown. The qualitative characteristics of
financial statements, as outlined in the New Zealand Framework, are used to frame the
discussion in this sub-section.

6.3.1 Understandability

While it is generally accepted that financial information may be complex, there is an
expectation that the information will be presented sufficiently clearly and concisely that it is
understandable. As noted in the New Zealand Framework: ‘financial reports are prepared for
users who have a reasonable knowledge of business and economic activities’. Thus, while
there is not the expectation that every individual will understand every component contained
within financial reports, the information should allow for general understanding. The
information provided in the annual reports in relation to tax debts in both countries was
presented in a way that did allow for general understanding of the overall debt position in
each country. However, as no explanation was provided on the impacts of consolidation and
the increases and decreases in debt that resulted from this process, it was difficult to reconcile
the tax authority debt with tax debt reported by the government. Thus, it was not possible to
determine, without further investigation and clarification, the accurate value of the tax debt.

6.3.2 Relevance

Information needs to be relevant to ensure that those referring to the financial information can
make appropriate decisions based on the information provided. Materiality is included under
the qualitative characteristic of relevance. It is evident that tax receivables in both New
Zealand and Australia are highly material, as tax debts are 12 per cent and 9 per cent of total
tax revenue in New Zealand and Australia, respectively. Given the materiality of the
outstanding amounts, it was expected that the values would be disclosed differently from
current methods used. For example, tax debts are still held by the tax authorities, even when
they are classified as uncollectable. Under IFRS, assets are deemed to be impaired when the
carrying amount decreases below the recoverable amount of the asset. In the case of tax debt,
a large proportion of the debt is classified as uncollectable, but remains unadjusted in the
disclosures made by both the tax authorities and the government financial statements. The
differences in both the income statement and the balance sheet of the government are likely
to be materially changed if debt classified as uncollectable was impaired and written-off.

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114 Above, n.19. Timeliness and comparability are not discussed here as there is no discretion relating to the
timing of information disclosure, and comparability is less relevant for the financial statements of the
government.
115 Above, n.19, para QC 32.
6.3.3 Faithful Representation

The New Zealand Framework describes faithful representation as information that is ‘complete, neutral and free from error’.\(^{116}\) While it is not suggested that the financial statements examined in this study contain errors, it is suggested that the information is not presented in a neutral manner. Reconciliation of the information presented by the tax authority and the government cannot be done without additional information; and amounts that are classified as uncollectable are classified as assets in the balance sheet, instead of being written-off through profit and loss. These factors impede the faithful representation of the information provided in the financial statements.

6.3.4 Verifiability

The concept of verifiability is intended to provide assurance to users of financial information that information presented is a faithful representation of what it purports to represent. In particular, it suggests that different observers of the information could come to some consensus about the depiction of the data. It is difficult to verify many of the items that are included in the financial statements investigated in this study. This places greater importance on the other qualitative characteristics, that is, information needs to have greater understandability, relevance and faithful representation where it is difficult for those using the information to verify its accuracy.

7.0 CONCLUSION

This study highlights a number of issues with the way that tax authorities and governments collect tax debt and communicate this tax debt to stakeholders. The tax authorities have a range of tools that are available to assist with tax debt collection. However, both the New Zealand and Australian tax authorities hold large amounts of tax receivables. This suggests that either the current tools are not being utilised to achieve the best outcome or that the tools are insufficient to meet the objective of collecting the maximum amount of tax revenue taking into account available resources.

The second issue highlighted in this study is the valuation and communication of tax debt by the tax authorities and the government. In both countries there are discrepancies between tax debt as defined by the tax authority and tax debt as communicated by the government. This leads to different disclosures in the financial reports and some difficulty in reconciling the two amounts. More significant is the apparent trend in both countries for tax debt to be classified as uncollectable, but to remain recorded as an asset in the balance sheets of the Crown.

\(^{116}\) Above, n.19, para QC 10.