

Regulatory Impact Statement

Allowing additional deductions to be made from salary or wages

Agency Disclosure Statement

This Regulatory Impact Statement has been prepared by Inland Revenue.

The question addressed in this statement is how can Inland Revenue more efficiently use information it already holds about the employment of a defaulter in order to recover outstanding payments of tax, child support, gaming duty or student loan repayment obligations.

Requiring an employer to make deductions from wages or salary is one of the most efficient means of debt collection available to Inland Revenue. If deductions are imposed soon after a default is detected, they ensure early recovery of the debt and limit the growth of late payment interest or penalties. However, when Inland Revenue issues a deduction notice to an employer, it is required to issue a notice to the defaulter at the same time. If Inland Revenue does not hold a valid address for the defaulter, it cannot send notification to them and therefore cannot send a deduction notice to the employer.

Inland Revenue has considered a range of options for requiring an employer to make additional deductions from a defaulting employee's salary or wages when there is no valid address held for the employee.

Because of time constraints, Inland Revenue has not consulted with employers on any of the options. Even so, we do not consider that our analysis of the issues is impaired by the lack of external consultation with employers and employees. We note that only a small number of taxpayers are affected (approximately 700 at any time). The Treasury was consulted on the policy proposal.

None of the options identified would impair private property rights or reduce market competition. However, two of the options involve some impairment of the common law principle of natural justice by reducing employees' opportunity to challenge the basis on which the decision to increase wage or salary deductions is made, or to make alternative arrangements to redress any shortfall in PAYE, child support, gaming duty or student loan repayment obligations. We also note that some of the options (not the preferred option) would impose additional costs on business.



Keith Taylor
Policy Manager, Policy and Strategy
Inland Revenue
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STATUS QUO AND PROBLEM DEFINITION

1. Automatic deductions from salary or wages are one of the most efficient means of debt collection available to Inland Revenue. They help to minimise administrative costs for Inland Revenue and compliance costs for taxpayers in a debt situation. If the automatic deductions are imposed soon after a default is detected, they limit the growth of late payment penalties or interest and ensure early recovery of the debt. These deductions are additional to standard PAYE, ACC, child support contributions or student loan repayments.
2. Under current law, Inland Revenue is required to advise a defaulting taxpayer, liable parent, gaming machine operator or student loan borrower of its intention to make automatic additional deductions from salary or wages in order to recover unpaid tax, child support, duty, or student loan repayments. Notification is sent to the individual at the same time as the deduction notice is sent to the employer, giving them a short time (until their next pay day) during which they can contact Inland revenue to challenge the decision or make alternative arrangements to address the debt.
3. The release of the deduction notice to the employer is prevented if a valid address is not held for the defaulter. The system has been designed to protect the right of the employee to be notified of the intended deductions so they can exercise their right to challenge the decision or make alternative arrangements.
4. As at 11 March 2015, the lack of a valid address is preventing recovery of \$718,044 from 545 taxpayers, across all tax types. In addition 170 student loan borrowers have additional repayment obligations that could be met through increased wage or salary deductions if we had valid addresses. The rate of growth as penalties are applied will vary across tax types so that numbers and amounts owed will vary from time to time. The rate of recovery through additional deductions is limited by law to 20% of the wages or salary payable to an individual.
5. The current practice in these situations involves administrative costs for Inland Revenue and for employers, as manual intervention is required. This may include an initial phone call to the employer, followed, if necessary, by a written demand to provide the address details. Address records must then be updated before the deduction notice can be issued to the employer and copied to the defaulting employee.
6. Even so, the current practice seeks to preserve the rights of the employee to be informed about the decision and be able to challenge it or choose how they will redress their non-compliance.
7. Inland Revenue should be able to use information it already holds about a defaulter's employment to recover debt more efficiently when a defaulter has not only failed to meet payment obligations, but also failed to advise a change of address to Inland Revenue.
8. The question addressed in this RIS is how can Inland Revenue more efficiently use information it already holds about employment of a defaulter in order to recover outstanding debt.

OBJECTIVES

9. The key objectives are:
- (a) minimise administrative costs for Inland Revenue
 - (b) minimise compliance costs for defaulters and employers
 - (c) reduce or limit the growth of late payment interest or penalties and effect full recovery in the shortest possible time
 - (d) ensure that defaulters' rights to object or make alternative arrangements to redress their default are maintained (fairness).
10. Trade-offs will need to be made across the various objectives. For example, options that seek to minimise administrative costs for Inland Revenue and compliance costs for employers may impair defaulters' rights to object or make alternative arrangements to redress their default.
11. An additional constraint faced by Inland Revenue is its inability to make significant system changes in advance of the relevant stage of development of its Business Transformation.

REGULATORY IMPACT ANALYSIS

12. One administrative and two legislative solutions were considered as alternatives to the status quo. The options are:
- Option 1: Inland Revenue obtains contact details for the defaulter from their employer (status quo).
 - Option 2: Inland Revenue issues notice to the last known address of the defaulter.
 - Option 3: Inland Revenue issues notice to the employer for pass on to the defaulter.
 - Option 4: Inland Revenue dispenses with requirement to issue notice to the defaulter when it holds details of the defaulter's employer (preferred option).

Option 1 – status quo

13. Under the status quo:
- Inland Revenue contacts the employer and requests that the employer provide the defaulter's address details.
 - Inland Revenue then updates the address details of the defaulter in its system.
 - Inland Revenue issues a deduction notice to the employer and a copy to the defaulter.
14. The current practice creates additional compliance costs for Inland Revenue and for employers and an additional step in the recovery process, slowing the commencement of recovery, but preserves the rights of the defaulter (for a very limited time) to challenge the decision or choose how they will redress their non-compliance before any action is taken.

Option 2 – Issue notice to the last known address of defaulter

15. Under this option, Inland Revenue issues a deduction notice to the employer and a copy to the defaulter's last known "invalid" address.

16. The main advantage of this option is that it avoids imposing additional compliance costs on employers (compared with the status quo), as they are not required to provide Inland Revenue with updated address details for defaulters.

17. There are several disadvantages with this option, including:

- The defaulter is unlikely to receive the notice so does not have the opportunity to challenge the decision or choose how they will redress their non-compliance.
- The address held for the defaulter remains invalid.
- There is potential for a breach of tax secrecy, as someone other than the intended recipient may open the mail (even though it is an offence under the Postal Services Act 1998 for a person to open mail addressed to another).
- It could generate complaints from residents who have sent back previous pieces of correspondence, creating resource implications through additional work for call centres.
- It would create extra work for Inland Revenue through manual activity in what is intended to be an automated process, with further resource implications.
- Employers would be required to bear the compliance cost of dealing with employees who complain about reduction in pay.
- There would be some delay in the commencement of debt recovery.
- There may also be an increase in contacts to Inland Revenue call centres of complaints about the unexpected deduction from pay.

Option 3 – Issue notice to employer for pass on to defaulter

18. Under this option, Inland Revenue takes manual action to issue the notice to the employer and a copy of the notice for the employer to pass on to the defaulter.

19. The main advantage of this option over the status quo is that it would limit growth of late payment interest and penalties and contribute to the earliest possible recovery of debt. In addition, the defaulter would retain the limited right to challenge the decision or choose how they will redress their non-compliance before any action is taken.

20. The main disadvantages are:

- It would impose additional compliance cost on employers.
- There would be systems implications, which may be significant and could not be implemented until Inland Revenue's Business Transformation reaches the relevant stage of development. Until then, manual intervention would be needed.
- The address details of the defaulter remain invalid unless the defaulter contacts Inland Revenue and updates them.

Option 4 – Dispense with requirement to issue notice to the defaulter

21. Under this option, Inland Revenue would issue the notice to employer when there has been a default on payment obligations, even though it is not possible to issue a copy of the notice to the defaulter. Ultimately, the defaulter can regain the right to challenge the

decision or choose how they will redress their non-compliance by re-engaging with Inland Revenue and updating their address records.

22. The main advantages of this option are:

- It ensures that growth in late payment interest or penalties is limited by early intervention.
- It contributes to the earliest possible recovery of outstanding debt.
- It will ultimately retain the automation of the process when systems changes are possible.
- In the interim, it can be implemented manually on a case-by-case basis with no additional administrative resources over the status quo.

23. The main disadvantages are:

- By removing the requirement for formal notification to the employee it further limits the defaulter's opportunity to dispute the outstanding amounts or make other arrangements for repayment.
- Employers would be required to bear the compliance cost of dealing with those employees who complain about the unexpected reduction in their pay.
- There may also be an increase in contacts to Inland Revenue call centres of complaints about the unexpected deduction from pay.

24. This is officials' preferred option.

Summary of impact analysis

25. The table below summarises our analysis of the options (including the status quo).

Table: Summary of analysis

<i>Option</i>	<i>Meets objectives a, b, c, or d?</i>	<i>Impacts</i>				<i>Net impact</i>
		<i>Economic / revenue impact</i>	<i>Administrative impact</i>	<i>Compliance impact</i>	<i>Fairness</i>	
1. Inland Revenue obtains contact details for the defaulters from their employers (status quo)	Meets (d). Partially meets (c) but not (a) or (b).	None	Inland Revenue must obtain valid address details of defaulters, which slows the debt recovery process	Employers must provide address details for defaulters	Right of defaulters to be informed is preserved	Does not address the problem definition and fully meets only one of the four objectives
2. Inland Revenue issues notice to the last known "invalid" address of defaulters	Meets (c). Partially meets (b). Does not meet (a) or (d).	None	Inland Revenue must manually over-ride its system to issue the notices, deal with returned mail and handle additional complaints to call centres.	Employers may have to deal with employee complaints about reduction in pay	Defaulters are unaware of intention to deduct	Does not address the problem definition and fully meets only one of the four objectives
3. Inland Revenue issues notice to the employers for passing on to the defaulters	Meets (d). Partially meets (c). Does not meet (a) or (b).	None	Inland Revenue must manually over-ride its system to issue the notices	Employers have to pass on notice to defaulters	Right of defaulters to be informed is preserved	Addresses the problem definition but fully meets only one of the four objectives
4. Inland Revenue dispenses with notices to the defaulters (preferred option)	Meets (a) and (c). Partially meets (b). Does not meet (d).	None	An administrative saving compared with the status quo.	Employers may have to deal with employee complaints about reduction in pay	Defaulters are unaware of intention to deduct	Addresses the problem definition and fully meets two of the four objectives

OTHER IMPACTS

26. There are no social, cultural or environmental impacts.

CONSULTATION AND IMPACT

27. Inland Revenue has not consulted with employers due to time constraints and the preferred option would reduce compliance costs over the status quo for the small number likely to be affected (approximately 700 in March 2015). The Treasury was consulted on the policy proposal.

CONCLUSIONS AND RECOMMENDATIONS

28. We recommend Option 4 because it offers the biggest administrative cost reduction for Inland Revenue while offering improvements in efficiency of debt recovery and a reduction in compliance costs for employers. We consider these efficiency gains outweigh the impairment in the defaulters' right to natural justice because that impairment can be redressed by the defaulters taking action to update their address records.

IMPLEMENTATION

29. Options 1 and 2 do not require legislation to implement. Legislative change is required to implement options 3 and 4.

30. Amendments will be included in the proposed Taxation (Business Transformation and Simplification) Bill, which is scheduled for introduction in June 2015, and could be implemented from the date of enactment.

31. The preferred option would be automated when Inland Revenue's system changes are at a suitable stage of development. In the interim, it could be implemented manually on a case-by-case basis.

32. Inland Revenue will communicate any legislative changes to employers through its existing channels, such as its guides and the Tax Information Bulletin.

MONITORING, EVALUATION AND REVIEW

33. There are no specific plans to monitor, evaluate and review the changes to give effect to additional recovery of outstanding payments of tax, child support, gaming duty or student loan repayment obligations. If any detailed concerns are raised in relation to these changes, Inland Revenue will determine whether there are substantive grounds for review under the Generic Tax Policy Process.