Inland Revenue
Te Tari Taake

POLICY AND REGULATORY STEWARDSHIP

Tax policy report: **Extending use of money interest relief during COVID-19**

Date:	8 June 2021	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2021/249

Action sought

	Action sought	Deadline
Minister of Finance	**Agree** to recommendations **Note** the fiscal impacts	25 June 2021
Minister of Revenue	**Agree** to recommendations **Note** the fiscal impacts	25 June 2021

Contact for telephone discussion (if required)

Name	Position	Telephone
Bary Hollow	Policy Lead (Acting)	s 9(2)(a)
David Cuellar	Policy Advisor	s 9(2)(a)

8 June 2021

Minister of Finance
Minister of Revenue

Extending use of money interest relief during COVID-19

Executive summary

Purpose

1. This report seeks your agreement to make an Order in Council to extend a COVID-19 scheme that allows Inland Revenue to remit use of money interest (UOMI).

2. If you agree to an extension of the scheme, then officials also seek your agreement to a remedial legislative amendment that will enable the scheme to be extended only for taxpayers in existing instalment arrangements who are currently receiving UOMI suppression.

Background

3. On 25 March 2020, the Government implemented a scheme that allows for UOMI to be remitted for taxpayers that are facing difficulties in paying their tax in full and on time due to COVID-19. This meant that taxpayers could apply to have Inland Revenue write off the interest on their late tax payments once that core tax was paid.

4. As part of this relief measure, Inland Revenue implemented an option to allow UOMI to be suppressed for taxpayers in instalment arrangements. Suppression of interest means that interest is being charged but at a special rate of zero percent (as opposed to being charged at the UOMI underpayment rate, which is currently seven percent). Once a taxpayer's arrangement is complete, their amount of suppressed interest is then remitted. The suppression option was implemented to simplify the administrative impact of the scheme and provide a better customer experience.

5. If a taxpayer does not comply with the terms of their instalment arrangement, UOMI is charged back to the date that the original tax was overdue at.

6. The scheme is due to expire two years after the scheme began, so the last day for remission is 24 March 2022. However, an Order in Council can be made to extend the scheme if desired.

Problem definition

7. When the scheme was developed, officials did not contemplate that UOMI suppression would be made available. This creates a distinction between taxpayers who have paid all their tax and have had their UOMI **remitted** (written off) versus taxpayers who have not yet paid all their tax and are having their UOMI **suppressed** (charged at zero percent).

8. Officials have concluded that the legislation only permits an extension by Order in Council of the scheme as a whole. It does not allow an extension only for those taxpayers currently in instalment arrangements that are having UOMI suppressed.

9. Making an Order in Council to give effect to an extension requires the Minister of Revenue to be satisfied that taxpayers' ability to pay their tax on time is likely to continue to be significantly adversely affected by COVID-19 beyond the current expiry date of 24 March 2022. As time passes, the links between COVID-19 and any associated financial hardships become weaker, barring any further pandemic events or restrictions.

Options

10. The status quo is to **not extend the scheme for anyone** (**Option 1**). If you wish for the scheme to end at its current expiry date of 24 March 2022, then taxpayers in existing instalment arrangements who are having UOMI suppressed will start being charged interest at 25 March 2022 on the balance going forward as well as having their suppressed interest recalculated back to the point at which the tax became overdue. This will be unfair on taxpayers who have acted in good faith to manage their payments of outstanding amounts within the incentive of UOMI remission. Officials do not recommend this option.

11. Instead, you may wish to **extend the scheme for all taxpayers** (**Option 2A**). Under this option, no legislative amendment will be required, and an Order in Council can be made to give effect to extending the scheme generally. Officials consider that this sort of general extension is not currently warranted given the positive economic outlook.

12. However, if you wish to **extend the scheme only for taxpayers in existing instalment arrangements** who are having UOMI suppressed (**Option 2B**), a remedial legislative amendment will be required, and an Order in Council can then be made accordingly.

Recommendation

13. Officials recommend **Option 2B**, which is to extend the scheme by making an Order in Council, but only for taxpayers that will be in existing instalment arrangements with interest supressed when the scheme expires on 24 March 2022. This will ensure that these people are not hit by an interest spike at expiry. We recommend that the scheme be extended until 31 March 2024.

14. The 2021 baseline forecasts should be adjusted to account for revenue gained when interest is backdated under the status quo. This will have a positive impact of $3.7 million. The proposed extension will then remit UOMI for taxpayers that would otherwise have not received remission, with a cost of $2.9 million. The net impact of the proposal relative to 2021 Budget baseline forecasts is therefore $0.7 million.

Consultation

15. The Treasury was consulted on this report.

Next steps

16. If you agree to extending the scheme, officials will issue drafting instructions to the Parliamentary Counsel Office so that the Order in Council can be drafted.

17. If you also agree to a legislative amendment that specifies this extension can be made only for people in existing instalment arrangements, then officials will progress this change within the upcoming omnibus tax Bill scheduled for introduction in August 2021.

Recommended action

We recommend that you:

18. **note** that for an extension of the scheme allowing Inland Revenue to remit use of money interest (UOMI) during COVID-19, the Minister of Revenue must be satisfied that the ability of taxpayers to pay tax on time is likely to continue to be significantly adversely affected by COVID-19 beyond the current expiry date of 24 March 2022;

    Noted Noted

19. **agree** to **one of the following options** relating to extending Inland Revenue's ability to remit UOMI for underpayments of tax related to COVID-19:

    19.1 **Option 1**: Do not extend the scheme; or

    Agreed/Not agreed Agreed/Not agreed

    19.2 **Option 2A**: Extend the scheme for all taxpayers until 31 March 2024; or

    Agreed/Not agreed Agreed/Not agreed

    19.3 **Option 2B**: Extend the scheme only for taxpayers in existing instalment arrangements until 31 March 2024 (**officials' recommendation**);

    Agreed/Not agreed Agreed/Not agreed

20. **note** that the Crown's revenue forecasts have been updated to reflect the additional $3.7 million in revenue that can be expected were COVID-19 UOMI relief to end after two years, as shown below;

	$m – increase/(decrease)				
Vote Revenue **Minister of Revenue**	**2020/21**	**2021/22**	**2022/23**	**2023/24**	**2024/25 & outyears**
Tax Revenue: Interest	0	18.4	0	0	0
Expense: Impairment of debt and bad debt write-offs	0	14.7	0	0	0
Total Operating	**0**	**(3.7)**	**0**	**0**	**0**

    Noted Noted

21. **note** that agreeing to recommendation 19.1 (**Option 1**) will have no fiscal impact, for a net effect (when considered in conjunction with the above forecast change) of $3.7 million;

    Noted Noted

22. **note** that agreeing to recommendation 19.2 (**Option 2A**) could have a cost of up to $22 million, subject to a number of conservative assumptions about behaviour and uptake of the scheme, and that this upper bound is highly uncertain;

    Noted Noted

23. **note** that agreeing to recommendation 19.3 (**Option 2B**) will result in the following fiscal impact, with a corresponding impact on the operating balance, for a net effect (when considered in conjunction with the above forecast change) of $0.7 million;

	$m – increase/(decrease)				
Vote Revenue **Minister of Revenue**	**2020/21**	**2021/22**	**2022/23**	**2023/24**	**2024/25 & outyears**
Tax Revenue: Interest	0	(14.7)	0	0	0
Expense: Impairment of debt and bad debt write-offs	0	(11.8)	0	0	0
Total Operating	**0**	**2.9**	**0**	**0**	**0**

Noted Noted

24. if recommendation 19.3 is agreed to, **agree** to include an amendment that gives effect to this extension in the upcoming omnibus tax Bill scheduled for introduction in August 2021;

Agreed/Not agreed Agreed/Not agreed

25. if recommendation 19.2 or 19.3 is agreed to, **agree** for Inland Revenue to issue drafting instructions to the Parliamentary Counsel Office to draft an Order in Council that gives effect to this extension.

Agreed/Not agreed Agreed/Not agreed

Bary Hollow
Policy Lead (Acting)
Policy and Regulatory Stewardship

Hon Grant Robertson
Minister of Finance
/ /2021

Hon David Parker
Minister of Revenue
/ /2021

Background

Introduction

26. The purpose of this report is to seek your agreement to extend the scheme that allows Inland Revenue to remit use of money interest (UOMI) for taxpayers that have been significantly adversely affected by COVID-19.

27. If you agree to an extension of the scheme, then officials also seek your agreement to a remedial legislative amendment that will enable the scheme to be extended only for taxpayers in existing instalment arrangements who are currently receiving UOMI suppression.

Context

28. The purpose of UOMI is to compensate the government for the loss of use of money from taxpayers underpaying their tax. It applies to all tax types administered by Inland Revenue as well as Working for Families debt. The UOMI rates track against market indices published by the Reserve Bank of New Zealand. The UOMI rate charged on underpayments of tax is currently seven percent.

29. As part of the Government's response to the economic impacts of COVID-19, a legislative amendment was made to allow Inland Revenue to write off UOMI for taxpayers that were significantly adversely affected by COVID-19 in their ability to pay tax. This is applicable to interest that has accrued after 14 February 2020 and was made available to taxpayers from 25 March 2020. To be eligible for UOMI remission, a taxpayer must have asked for the remission as soon as practicable and made the payment of tax as soon as practicable.

30. This became a useful measure to allow taxpayers affected by COVID-19 to manage their tax debt. Comments from tax practitioners have noted that the imposition of UOMI on late/unpaid tax during COVID-19 would have compounded hardship for taxpayers, and so UOMI remission was a welcome development.

31. It was initially intended that this remission was made available to those taxpayers that had paid their tax owing but had accrued UOMI due to late payment. However, to assist other taxpayers who were struggling to pay their tax in full, another option was implemented whereby taxpayers who had not yet paid all their tax could enter into an instalment arrangement with Inland Revenue and have their interest suppressed at zero percent. Interest is still calculated in the background during the arrangement, but it is remitted at the end of the arrangement if the taxpayer was compliant with its terms.

32. The practical difference between UOMI remission and UOMI suppression is that suppressed interest can be reversed if necessary. For example, a taxpayer may currently be in an arrangement where their interest is suppressed, but if they fail to meet their obligations under the arrangement, that suppressed interest can be recalculated at the UOMI underpayment rate such that they no longer get any UOMI relief. In contrast, remitting interest under this scheme is only available once the tax owing has been fully paid so the compliance issue does not arise for remission as it does for suppression.

33. As of 8 June 2021, the UOMI figures under the scheme are as follows:

    33.1 $14.4 million of interest has been remitted for 86,409 taxpayers (who have paid all their tax), and

    33.2 $58.7 million of interest has been suppressed for 21,727 taxpayers (who are in instalment arrangements to pay down the remainder of their tax owing).

34. Suppression has the benefit of being administratively simple and customer friendly, as taxpayers do not see the interest accruing while they are meeting their obligations.

Problem definition

35. The ability for Inland Revenue to remit UOMI expires on 24 March 2022. Extending this scheme would be done for the purposes of continuing to provide UOMI relief to taxpayers who are significantly adversely affected in their ability to pay their tax because of COVID-19. It is a requirement in the legislation that an extension can only be made if the Minister of Revenue believes that taxpayers' obligations will continue to be affected by COVID-19. As time passes, the links between the pandemic and any associated financial hardships become weaker, barring any further pandemic events or restrictions.

36. The other issue to consider is whether recipients of UOMI remission or UOMI suppression are equally deserving of an extension, or should one group be prioritised over the other. When the scheme was developed, officials did not contemplate that UOMI suppression would be made available. This creates a distinction between taxpayers who have paid all their tax and have had their UOMI **remitted** (written off) versus taxpayers who have not yet paid all their tax and are having their UOMI **suppressed** (charged at zero percent).

37. Officials have concluded that the legislation only permits an extension by Order in Council of the scheme as a whole. It does not allow an extension only for those taxpayers currently in instalment arrangements that are having UOMI suppressed. If you would like to extend the scheme solely to allow those in existing instalment arrangements to finish their arrangements without having interest charged, then a remedial legislative amendment would be required. If an extension is not granted for those taxpayers, UOMI will be charged back to the original due date for payment once the remission power expires.

Options

38. Officials have considered the options in two steps:

    38.1 Whether the scheme should be extended at all (**Option 1** versus **Option 2**), and

    38.2 If the scheme is extended, whether it should be extended for everyone (**Option 2A** versus **Option 2B**).

39. **Option 1** is the status quo, which is to **not extend the scheme**. This means that Inland Revenue's ability to remit UOMI will expire on 24 March 2022.

40. **Option 2** is to extend the scheme and has two versions. Note that taking either of these options to extend the scheme requires that the Minister of Revenue is satisfied that the ability of taxpayers to pay tax on time is likely to continue to be significantly adversely affected by COVID-19 beyond the current expiry date.

41. **Option 2A** is to **extend the scheme for all taxpayers**.

42. **Option 2B** is to **extend the scheme only for taxpayers in existing instalment arrangements** who are having UOMI suppressed.

Option 1: Do not extend the scheme

43. This option is the status quo. It does not require a legislative amendment and will result in the scheme expiring on 24 March 2022.

44. Taxpayers who have had UOMI remitted before expiry have already received the benefit of the scheme.

45. Taxpayers who are in instalment arrangements with interest suppressed at the time of expiry will see UOMI charged on the overdue tax. This balance will increase from zero to an amount recalculated using the prevailing UOMI underpayment rate.

46. Note that this will be backdated to the point at which the tax payment was initially due, rather than being prospective from expiry of the scheme. This means that, although the taxpayer was not obliged to pay interest for the duration of the arrangement until the scheme's expiry, they will now be liable for the UOMI that would have been charged if not for the UOMI relief. This means that they will have received no benefit from the scheme apart from deferring an amount of UOMI. This was not an intended outcome of the scheme, as officials considered that those eligible for UOMI relief during the period of the scheme should not have that relief reversed once the scheme ends.

47. We do not recommend this option as we consider the backdating of the interest charge to be excessively punitive. This is because taxpayers have, in good faith, entered into instalment arrangements with the expectation that UOMI would be remitted if they comply with the terms of that arrangement.

Option 2A: Extend the scheme for all taxpayers

48. The first option for extending the scheme is a general extension for all taxpayers. This requires an Order in Council to be passed but does not require a legislative amendment. Under this option, we recommend extending the scheme for a duration of two years until 31 March 2024.

49. This is the most generous option to taxpayers of those proposed in this report. It will allow taxpayers to have interest remitted on tax accrued on and after 25 March 2022. It will also allow people in existing instalment arrangements to have their interest suppressed beyond the expiry date, and will allow anyone to set up a new instalment arrangement with suppressed interest after that date.

50. Officials consider that the link between COVID-19 and taxpayers' ability to pay their tax in full and on time is much weaker now than it was during 2020. We expect that this link will have weakened further by March 2022. We accept that COVID-19 still creates and will continue to create difficulties for some industries in particular, but we do not recommend targeting this measure at specific sectors.

Option 2B: Extend the scheme only for taxpayers in existing instalment arrangements

51. The second option for extending the scheme is a targeted extension for the group of taxpayers who are already in instalment arrangements with interest suppressed. Because the existing legislation only allows for a general extension of the scheme, a legislative amendment would be required. This would allow for an Order in Council to be made that specifies a group of people for which the scheme is extended for.

52. As per **Option 2A**, we recommend extending the scheme for a duration of two years until 31 March 2024. This is long enough to ensure that the majority of taxpayers in instalment arrangements running past the current expiry date are able to complete their arrangement and therefore have their interest fully remitted. We do not consider it appropriate to extend the scheme until all instalment arrangements are finished, which is not until at least 2030.

53. **Option 2B** allows taxpayers in existing instalment arrangements with suppressed interest to complete their tax payments and ultimately receive the benefit of

remission. However, it does not allow taxpayers to set up new instalment arrangements or make new applications for remission after the current expiry date. This option is therefore more generous than **Option 1** but less generous than **Option 2A**.

54. This option is less concerned with the question of whether taxpayers are still being significantly adversely affected by COVID-19 compared to **Option 2A**. The intention of this option is to ensure that those who are receiving a benefit under the scheme are able to lock that benefit in, rather than to continue to provide COVID-19-related relief for everyone. This is consistent with the original policy intent, which means this would be a remedial amendment. This option also eliminates the main disadvantage of **Option 1** concerning the backdating of UOMI.

Conclusion

55. Officials recommend proceeding with **Option 2B** to extend UOMI relief only for taxpayers in existing instalment arrangements with interest being suppressed. We believe this strikes a balance between ensuring that those affected by COVID-19 are able to benefit from the scheme (and are not hit with an interest spike at the scheme's expiry) while also recognising that UOMI relief must be tied to taxpayers being significantly adversely affected by COVID-19.

56. As of 3 June 2021, 12,794 instalment arrangements with $46.6 million of suppressed UOMI are not scheduled to be completed before the current expiry of the scheme. However, 11,733 of those arrangements (92 percent) would be completed within a two-year extension, with current suppressed interest of $44.4 million. The actual number completed will depend on how compliant taxpayers are with the terms of their arrangements.

57. Note that these figures are snapshots and do not capture any instalment arrangements with UOMI suppression set up between 3 June 2021 and 24 March 2022.

Financial implications

58. When the UOMI remission scheme was originally developed, no fiscal impact was estimated. This was because the baselines at the time did not contemplate COVID-19 and its implications for making it difficult for taxpayers to pay their tax in full and on time. Consequently, extra UOMI was predicted to become payable that had not previously been anticipated, and so writing that UOMI off simply returned revenue to what was originally expected.

59. Over a year has passed since the scheme was set up and Inland Revenue now has data on figures concerning remission and suppression under the scheme. However, the Budget 2021 baseline forecasts do not include any positive revenue impact arising from UOMI being recalculated and payable at the end of the scheme.

60. A fiscal impact can be calculated for the cost of extending the scheme for taxpayers in existing instalment arrangements, since Inland Revenue holds information about the arrangements that exist. This is made up of two changes:

    60.1 The first change to existing baselines arising from the fact that UOMI remission has been allowed but will end on 24 March 2022, resulting in some taxpayers having UOMI backdated (status quo); and

    60.2 The second change to those adjusted baselines arising from the current recommendation to extend the scheme for taxpayers in existing instalment arrangements.

61. The first change recognises that a number of taxpayers have arrangements running past the current expiry date and, without an extension, will lose the benefit of their UOMI being suppressed as the interest will be recalculated back to when the tax became due. This will result in a forecasting adjustment upward in the 2021/22 year of $3.7 million. If you do not agree to an extension, this adjustment will still be required.

	$m – increase/(decrease)				
Vote Revenue **Minister of Revenue**	**2020/21**	**2021/22**	**2022/23**	**2023/24**	**2024/25 & outyears**
Tax Revenue: Interest	0	18.4	0	0	0
Expense: Impairment of debt and bad debt write-offs	0	14.7	0	0	0
Total Operating	**0**	**(3.7)**	**0**	**0**	**0**

62. The second change then recognises that a two-year extension for taxpayers in existing instalment arrangements will allow those taxpayers with an arrangement falling between 25 March 2022 and 31 March 2024 to receive remission of UOMI at the end of their arrangements, when they otherwise would have had interest recalculated and backdated to when tax became overdue if not for the extension. This has a fiscal cost of $2.9 million.

	$m – increase/(decrease)				
Vote Revenue **Minister of Revenue**	**2020/21**	**2021/22**	**2022/23**	**2023/24**	**2024/25 & outyears**
Tax Revenue: Interest	0	(14.7)	0	0	0
Expense: Impairment of debt and bad debt write-offs	0	(11.8)	0	0	0
Total Operating	**0**	**2.9**	**0**	**0**	**0**

63. The net impact of these adjustments relative to Budget 2021 baselines is therefore $0.7 million in the 2021/22 year.

64. This costing relies on a number of assumptions, including:

64.1 UOMI suppressed a year from now will be close to double the current amounts;

64.2 If there is no extension, people with arrangements ending soon after the current expiry date are more likely to take actions to finish their arrangement early to receive the benefit of remission compared to taxpayers whose arrangements end later; and

64.3 UOMI figures are impaired at 80 percent.

65. If you wish to extend the scheme for everyone (**Option 2A**), there will be a cost to the Government that officials have been unable to quantify. This is because Inland Revenue does not hold information on the number of taxpayers who may enter into future instalment arrangements or make a new application for remission after the current expiry date.

66. Based on current uptake of the scheme and extrapolation, there could be an upper bound on the cost of this option of $22 million. This assumes that all suppressed interest is eventually remitted, and that uptake of the scheme over the extension period is the same as uptake over the original period. Both of these assumptions are conservative and highly unlikely to be true.

Administrative implications

67. Implementing the recommendation outlined in this report is straightforward and will require communication to taxpayers and tax agents, as well as education for Inland Revenue staff. There are no systems changes required and existing processes will continue. Any implementation costs that arise can be met through baseline funding.

Consultation

68. The Treasury was consulted on this report.

Next steps

69. Subject to your approval of an extension, we will issue drafting instructions to the Parliamentary Counsel Office to draft the required Order in Council.

70. If you agree to the extension only applying to taxpayers in existing instalment arrangements, then a remedial legislative change will need to be made prior to the drafting of the Order in Council. We will include this in the drafting of the upcoming omnibus taxation Bill scheduled for introduction in August 2021.