

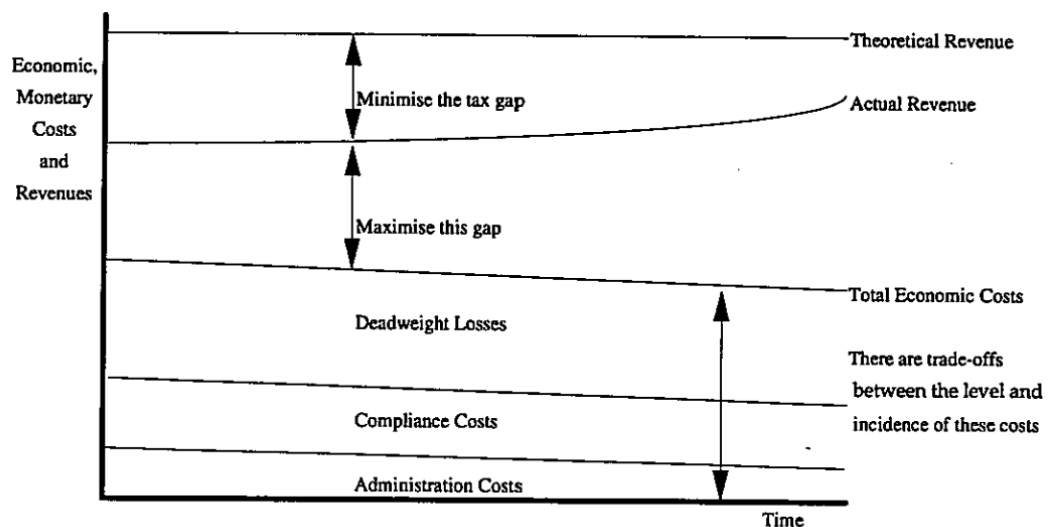
## Matthew Handford

### TLC for the tax system?

An independent Tax Law Commission to restore GTPP and improve the quality of New Zealand's tax laws

## 1. Introduction

- 1.1 In 1994 the Richardson Committee described the overall objective of the tax system as comprising sufficiency of revenue for the Government, *efficiency*, and fairness.<sup>1</sup> An efficient tax system minimises the total economic costs of taxation. Economic costs include “administrative costs incurred by the tax administration, compliance costs borne by taxpayers, and other indirect effects that have an impact on the overall efficiency of the economy ('deadweight losses')”.<sup>2</sup> The Committee illustrated this diagrammatically:<sup>3</sup>



- 1.2 The Committee recognised that to minimise compliance costs and deadweight losses required appropriate external consultation, and that lack of consultation had (at the time) led to “some tax policies and legislation not taking sufficient account of external views and potential problems”.<sup>4</sup> The Committee’s solution was to endorse the Generic Tax Policy Process (GTPP).

<sup>1</sup> Ivor Richardson and Others *Organisational Review of the Inland Revenue Department* (April 1994) at 47.

<sup>2</sup> At 47; see also Robert McLeod and Others *Tax Review 2001 – Issues Paper* (June 2001) at 12-15.

<sup>3</sup> Richardson Committee, above n 1, at 47.

<sup>4</sup> At 78.

- 1.3 While it is generally agreed that the GTPP works well,<sup>5</sup> it only works when it is followed. Time pressure and competing priorities may mean that is not possible (see **section 2**, below). As was observed in the (Inland Revenue commissioned) Smaill Report concerning tax law drafting:<sup>6</sup>

inevitably, the process of producing taxation legislation in New Zealand involves significant pressures on those drafting the legislation to deal with external demands, tight timeframes and a continuously-evolving policy framework.

- 1.4 My proposed solution is an independent Tax Law Commission (**TLC**), modelled on the New Zealand Law Commission (**NZLC**). The TLC would assume an advisory role in respect of certain functions currently held by Inland Revenue's Policy and Regulatory Stewardship division (**PaRS**), including post-implementation reviews (**PIRs**) and remedial amendments. Additionally, the TLC would conduct detailed investigations into the operation of existing or proposed tax laws (with extensive public consultation) and recommend changes to (among other things) minimise compliance costs and deadweight losses (see **sections 3 and 4**, below).

- 1.5 The rest of this proposal is structured as follows:

- (a) Problem definition: shortcomings in the tax policy process (**section 2**);
- (b) Proposed solution: a Tax Law Commission for New Zealand (**section 3**); and
- (c) Benefit to New Zealand (**section 4**).

## 2. Problem definition: shortcomings in the tax policy process

- 2.1 The problem with New Zealand's tax policy process lies not in the GTPP itself, but in the competing pressures that lead Inland Revenue to depart from it. As Griffiths and Hartshorn observe "the decision to engage in GTPP is no more than a *political decision* to engage in each of the various stages and phases it prescribes."<sup>7</sup>

- 2.2 This is illustrated by three shortcomings in the policy development process:

- (a) Ministerial priorities: PaRS understandably focuses on implementing ministerial priorities within the time-constraints of a three-year parliamentary term, which can lead to truncated consultation. One example is the Taxation Principles Reporting Act

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<sup>5</sup> Brian Arnold "The Process for Making Tax Policy: An International Comparison" (2013) 61 CTJ 989 at 996.

<sup>6</sup> Graeme Smaill Letter to Inland Revenue enclosing *Report on results of taxation law drafting review and recommendations* (6 October 2021) at 1.

<sup>7</sup> Shelley Griffiths and James Hartshorn "Fragile and Strong: the Oxymoron of Tax Administration and Constitutionality in New Zealand" (2023) 2 Review of International & European Economic Law 198 at 211.

2023, which was criticised both for its truncated consultation process and for various constitutional law issues that proper consultation could have avoided.<sup>8</sup>

- (b) Conflicting functions: Inland Revenue's main function is to maximise tax collections.<sup>9</sup> This creates an incentive to focus on measures that reduce the tax gap or administration costs, sometimes without giving adequate weight to compliance costs and deadweight losses (see paragraph 1.1 above). An example is Inland Revenue's recent BEPS reforms which have had certain unintended consequences including (for example) increasing the costs of securitisation transactions. In two separate Select Committee reports Inland Revenue has acknowledged these unintended consequences but declined to deal with them citing limited resources.<sup>10</sup>
- (c) Marking its own work: Related to point (b) is PaRS's general (if also understandable) reluctance to "change course" once a policy position has been adopted because doing so implicitly concede that its initial approach was problematic.

### Structural issues

- 2.3 New Zealand is "an exception internationally" in that the agency responsible for administering and enforcing tax laws (Inland Revenue) is also principally responsible for tax policy development.<sup>11</sup> This exceptionality is exacerbated by the fact that Inland Revenue is also responsible for both drafting tax legislation (as opposed to the Parliamentary Counsel Office), and interpreting it through its binding ruling and adjudication processes.
- 2.4 Even within New Zealand there is normally some separation between the agencies responsible for designing and enforcing laws (for example, overseas investment laws are developed by the Treasury but administered by the Overseas Investment Office). Nonetheless, Inland Revenue's integrated model does have certain advantages including enabling PaRS to draw upon operational expertise when developing policy.<sup>12</sup>
- 2.5 In summary, PaRS generally works well but there are certain issues and processes (particularly those related to compliance costs and unintended consequences) that it tends not to prioritise given its natural focus on ministerial objectives and initiatives that assist revenue collection. The TLC would fill this gap.

<sup>8</sup> Legislation Design and Advisory Committee "Submission to the Finance and Expenditure Committee on the Taxation Principles Reporting Bill 2023" at [26]-[28]; New Zealand Law Society "Submission to the Finance and Expenditure Committee on the Taxation Principles Reporting Bill 2023" at [2.1]-[2.4].

<sup>9</sup> Tax Administration Act 1994, s 6A.

<sup>10</sup> Inland Revenue *Officials' Report to the Finance and Expenditure Committee on submissions on the Taxation (Annual Rates for 2021-22, GST and Remedial Matters) Bill* (February 2022) at 252-256; Inland Revenue *Departmental Report to the Finance and Expenditure Committee on submissions on the Taxation (Annual Rates for 2023-24, Multinational Tax and Remedial Matters) Bill* (February 2024) at 120-121 and 241-243.

<sup>11</sup> Inland Revenue and the Treasury *The Generic Tax Policy Process: Background Paper for Session 14 of the Tax Working Group* (July 2018) at [21]; Arnold, above n 5, at 992-998.

<sup>12</sup> Richardson Committee, above n 1, at 83.

### 3. Proposed solution: a Tax Law Commission for New Zealand

- 3.1 For nearly 40 years, the NZLC has provided “first-class” advice on the reform of technical and “unsexy” areas of law.<sup>13</sup> The TLC therefore has an advantage over previous proposals for an independent tax policy body in that it is based on a statutory model with broad political support and a proven track record of effective law reform. As Griffiths observes:<sup>14</sup>

There are probably many insights that could be brought to bear on developing [a] tax specific body from New Zealand’s experience with a permanent body designed, as its purpose states, for the ‘systematic review, reform and development of the law in New Zealand’.

- 3.2 This section: (i) describes the NZLC’s statutory model; (ii) proposes a statutory model for the TLC based on the NZLC; and (iii) compares the TLC to other tax policy bodies.

#### The NZLC

##### *Purpose, functions and independence*

- 3.3 The NZLC is an independent Crown entity (**ICE**) established under the Law Commission Act 1985 (**LCA**). Its purpose is to “promote the systematic review, reform, and development of the law of New Zealand” (LCA, s 3). Section 5 of the LCA sets out its functions (emphasis added):

#### 5 Functions

- (1) The principal functions of the Commission are—
- (a) to take and keep under review in a systematic way the law of New Zealand:
  - (b) to make recommendations for the reform and development of the law of New Zealand:
  - (c) to advise on the review of any aspect of the law of New Zealand conducted by any government department or organisation (as defined in section 3A) and on proposals made as a result of the review:
  - (d) to advise the Minister of Justice and the responsible Minister on ways in which the law of New Zealand can be made as understandable and accessible as is practicable.
- (2) In making its recommendations, the Commission—

<sup>13</sup> Christopher Finlayson “Reforming New Zealand’s Legal Infrastructure” (2024 Lecretia Seales Lecture in Law Reform, Victoria University of Wellington, 6 June 2024).

<sup>14</sup> Shelley Griffiths “Foreword” in Adrian Sawyer *The Effectiveness of Tax Reviews in New Zealand: An Evaluation and Proposal for Improvement* (University of Canterbury, Christchurch, 2020) at iv.

- (a) shall take into account te ao Maori (the Maori dimension) and shall also give consideration to the multicultural character of New Zealand society; and
- (b) shall have regard to the desirability of simplifying the expression and content of the law, as far as that is practicable.
- (3) Except as expressly provided otherwise in this or any other Act, the Commission must act independently in performing its statutory functions and duties, and exercising its statutory powers under—
  - (a) this Act; and
  - (b) any other Act that expressly provides for the functions, powers, or duties of the Commission (other than the Crown Entities Act 2004).

3.4 The Crown Entities Act 2004 (**CEA**) provides that the Minister must not direct an ICE like the NZLC:

- (a) to have regard to or to give effect to a government policy unless specifically provided in another Act (CEA, s 105); or
- (b) in relation to the NZLC's statutorily independent functions (CEA, s 113).

3.5 The NZLC has three to six commissioners. They do not have prescribed qualifications, although the president must be a judge, retired judge or experienced lawyer (LCA, s 9). The commissioners are assisted by a small team of legal and policy advisers (approximately 16.5 FTE) and support staff (4.8 FTE).<sup>15</sup>

#### *Work programme*

3.6 The NZLC has the power (LCA, s 6(2)):

- (a) to initiate proposals for the review, reform, or development of any aspect of the law of New Zealand and to receive and consider any such proposals made or referred to it by any person:
- (b) to initiate, sponsor, and carry out such studies and research as it thinks expedient for the proper discharge of its functions:
- (c) to publicise such parts of its work in such manner as it thinks expedient, to conduct public hearings, to seek comments from the public on its proposals, and to consult with any persons or classes of persons:
- (d) to provide advice and assistance to, and to request information from, any government department or organisation considering the review, reform, or development of any aspect of the law of New Zealand.

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<sup>15</sup> Law Commission *Briefing for Incoming Minister* (December 2023) at [6].

- 3.7 These powers are flexible by design. The NZLC generally uses them to develop and carry out a work programme consisting of four or five large projects at any given time. The Commission develops its work programme based on referrals by the responsible Minister, public suggestions and its own independent judgment. The responsible Minister may not “direct” the Commission as to the content of its work programme but may “request” the inclusion or prioritisation of particular topics (LCA, s 7(2) and (3)).
- 3.8 The Cabinet Office suggests NZLC projects should:<sup>16</sup>
- involve issues that span the interests of a number of government agencies and professional groups;
  - require substantial, long term commitment or fundamental review;
  - involve extensive public or professional consultation;
  - need to be done independently of central government agencies because of the existence of vested interests, or a significant difference of views;
  - require independent consideration in order to promote informed public debate on future policy direction; or
  - involve technical law reform of what is often called “lawyer’s law” that would be likely otherwise to escape attention.
- 3.9 In carrying out its work programme the NZLC undertakes extensive consultation, including:
- (a) the publication of Issues Papers;
  - (b) public submissions;
  - (c) consultation with government departments; and
  - (d) the appointment of “an advisory group of leading experts with professional experience relevant to the area being reviewed”.<sup>17</sup>
- 3.10 The NZLC must submit finalised reports to the Minister of Justice and the relevant portfolio Minister. These reports must be published and laid before Parliament (LCA, s 16). The Government must then respond by introducing a Bill or presenting a response to Parliament.<sup>18</sup>
- 3.11 Recent NZLC projects have included reviews of the law relating to trusts (leading to the enactment of the Trusts Act 2019) and incorporated societies (leading to the enactment of the Incorporated Societies Act 2022), as well as three reviews of the Evidence Act 2006.

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<sup>16</sup> Cabinet Office Circular “Law Commission: Processes for Setting the Work Programme and Government Response to Reports” (24 April 2009) CO (09) 1 at [8].

<sup>17</sup> Law Commission “What we do” <<https://www.lawcom.govt.nz/about-us/what-we-do/>>.

<sup>18</sup> Cabinet Office, above n 16, at [18].

## The TLC

### *Statutory framework*

- 3.12 Parliament would establish the TLC as an ICE under a Tax Law Commission Act (**TLCA**) based on the LCA with necessary modifications.<sup>19</sup> The TLCA's purpose would be "to promote the systematic review, reform, and development of the tax law of New Zealand".<sup>20</sup> In particular, the TLCA would contain the following provisions (with all references to "the law of New Zealand" modified to refer to "the tax law of New Zealand"; and the Minister of Revenue rather than the Minister of Justice as "responsible Minister"):
- (a) a "Functions" section based on section 5 of the LCA (compare paragraph 3.3 above) with references to the Minister of Justice removed, and subsection (2)(b) expanded to provide that, in making its recommendations, the Commission -
    - (b) shall have regard, as far as is practicable, to the desirability of:
      - (i) simplifying the expression and content of the tax law;
      - (ii) minimising compliance costs; and
      - (iii) avoiding unintended consequences.
  - (b) a "Powers" section based on section 6 of the LCA (compare paragraph 3.6 above);
  - (c) a "Responsibilities" section based on section 7 of the LCA (compare paragraph 3.7 above);
  - (d) a "Membership of Commission" section based on section 9 of the LCA (compare paragraph 3.5 above). This section would be largely unmodified because the LCA already permits non-lawyers (including accountants, economists, academics and other persons with tax expertise) to be appointed as commissioners, and the requirement that the president be a judge or senior lawyer remains appropriate for a tax *law* commission; and
  - (e) a "Reports" section based on section 16 of the LCA (compare paragraph 3.10 above).
- 3.13 The Minister's ability to direct the TLC would be limited by sections 105 and 113 of the CEA (compare paragraph 3.4 above).

### *Work programme*

- 3.14 Compared to the NZLC, the TLC would focus on smaller remedial projects and post-implementation reviews with large projects undertaken from time to time at the TLC's discretion or the Minister's request (rather than focusing on a small number of large projects).

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<sup>19</sup> Compare LCA, s 4.

<sup>20</sup> Compare LCA, s 3.

This reflects the breadth and complexity of tax legislation, the frequency of amendments, and the particular pressures facing drafters of tax legislation (see paragraph 1.3 above), and is reinforced by the TLCA requirement to have regard to minimising compliance costs and avoiding unintended consequences.

#### *Remedial amendments*

- 3.15 The TLC would report to the Minister on remedial issues raised by members of the public and Inland Revenue. The TLC would (i) record submitted issues in a log; (ii) carry out consultation to determine whether the issue should be addressed by way of a remedial amendment and, if not, whether it should be considered as part of a larger TLC project or referred to PaRS; and (iii) present an annual report containing a list of remedial amendments to the Minister in the manner contemplated by paragraph 3.18 below.

#### *Post-implementation reviews*

- 3.16 The TLC would undertake PIRs at its own discretion based on public feedback or requests from the Minister. The TLC would: (i) identify new laws that do not appear to be functioning as intended or which have the potential to produce unintended consequences (for example changes to the taxation of close companies); (ii) carry out consultation; and (iii) present a report to the Minister containing proposed amendments in the manner contemplated by paragraph 3.18 below.

#### *Project reports*

- 3.17 The TLC would from time to time undertake in-depth consultation and analysis on a particular aspect of New Zealand's tax law and prepare a report containing detailed proposals for the reform or development of that area of tax law. The TLC would: (i) choose topics based on public feedback or requests from the Minister; (ii) carry out consultation similar to that undertaken by the NZLC (compare paragraph 3.9 above); and (iii) present a report to Minister in the manner contemplated by paragraph 3.18 below.

#### *Reporting requirements*

- 3.18 The TLC would present three kinds of reports to the Minister as contemplated by paragraphs 3.15, 3.16. and 3.17 above. Each would contain a list of recommendations. The Minister (with advice from Inland Revenue) would accept, reject or vary each of the TLC's recommendations. Accepted recommendations would be included in the next practicable tax Bill. The Minister would be expected to explain each rejection or variation in writing (compare paragraph 3.10 above).

#### *Taxpayer information*

- 3.19 Inland Revenue would provide information to the TLC (subject to taxpayer secrecy requirements). TLC commissioners and staff would be subject to taxpayer secrecy requirements like those in Part 3 of the Tax Administration Act 1994 (in addition to adhering to confidentiality agreements and codes of conduct that apply in relation to all Crown entities).



*Commissioners, staff and funding*

- 3.20 The TLC would have 3-6 commissioners appointed periodically by the Governor-General on the Minister's recommendation. The president would be a judge or senior lawyer. Other commissioners could be senior lawyers, accountants, economists, academics or others with relevant expertise (see paragraph 3.12(d) above).
- 3.21 The commissioners would serve in a full-time capacity to manage the TLC's work programme (which would be comparable in volume to that of the NZLC). The TLC would employ a similar number of legal, technical and policy advisors and support staff to the NZLC (approximately 22 FTE in total). Some advisors would be permanent staff while others would be seconded from government departments or the private sector. Some PaRS staff could be transferred or seconded to the TLC to reflect PaRS's reduced workload.
- 3.22 The TLC should have a lean budget of approximately \$4,205,000. This is based on the NZLC's appropriation for FY2024/25.<sup>21</sup> The TLC's budget may slightly exceed this amount given: (i) its responsibilities may require more resourcing than the NZLC; and (ii) the NZLC estimates that its current funding will become insufficient in FY2025/26.<sup>22</sup> This appropriation would be partially offset by cutting Inland Revenue's policy advice appropriation (\$13,912,000 for FY2024/25<sup>23</sup>) to reflect PaRS's reduced workload.

*Relationship with Inland Revenue*

- 3.23 The TLC would not replace PaRS. Rather it would assume responsibility for areas of tax policy that PaRS tends not to prioritise, that are particularly technical or that require a high level of public consultation. PaRS would retain responsibility for all tax policy other than remedial items, PIRs, and projects specifically referred to the TLC. Inland Revenue could also advise against TLC recommendations, acting as an operational counterweight to TLC recommendations that might not be operationally practical.

**Comparison to past, present and proposed tax policy bodies***Rewrite Advisory Panel*

- 3.24 The TLC is a spiritual successor to the Rewrite Advisory Panel (**RAP**) in respect of its remedial function which included consultation and the publication of a log of remedial items. The TLC goes further than the RAP because it has a wider mandate (not being limited to unintended changes and maintenance items) and greater independence (being an ICE rather than part of Inland Revenue).<sup>24</sup>

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<sup>21</sup> The Treasury *The Estimates of Appropriations for the Government of New Zealand for the Year Ending 30 June 2025* (30 May 2024) at 113.

<sup>22</sup> Law Commission, above n 15, at [10].

<sup>23</sup> The Treasury, above n 21, at 323.

<sup>24</sup> Compare Inland Revenue *Tax Information Bulletin Vol. 21, No. 5* (July 2009) at 22.

### *Board of Taxation*

- 3.25 The TLC is similar to the Australian Board of Taxation (**BoT**) in that it reports on technical areas of law, conducts PIRS, consults extensively and investigates unintended outcomes and disproportionate compliance and administration costs. However, the TLC would enjoy greater legal legitimacy and independence than the BoT due to its status as an ICE as opposed to a non-statutory body, and the fact that it would not have government officials on its board.<sup>25</sup>

### *New Zealand Tax Review Commission*

- 3.26 The TLC is similar to Adrian Sawyer's proposed New Zealand Tax Review Commission (**NZTRC**) in that it is an ICE that reports on aspects of the New Zealand tax system. However, the TLC differs from the NZTRC in that it is modelled on the NZLC – an institution that specialises in the reform of technical or “unsexy” areas of law – with a focus on improving consultation and reducing compliance costs and deadweight losses. In contrast, Sawyer envisages the NZTRC as a replacement for ad hoc tax reviews (Sawyer suggests, for example, that the NZTRC might undertake a review of the social security system).<sup>26</sup> The TLC's focus on technical tax law would complement, rather than replace, ad hoc committees.

## **4. Benefit to New Zealand**

### **Impact on the New Zealand economy, including GDP and business growth**

- 4.1 The TLC would improve New Zealand's tax policy process by:
- (a) providing a vehicle for detailed policy consideration on matters other than those prioritised by the Government of the day;
  - (b) providing a vehicle for Ministers and Inland Revenue to receive advice that gives greater weight to the perspectives of stakeholders outside of Inland Revenue (which is particularly important for simplification, compliance cost reduction and international competitiveness, and consistent with the purpose of the GTPP); and
  - (c) avoiding Inland Revenue “marking its own work” when conducting PIRs and proposing remedial amendments.
- 4.2 As noted at paragraph 1.2 above, appropriate consultation is necessary for an efficient tax system. The TLC's benefit to New Zealand arises not from one big policy change, but from its ability to recommend improvements that reduce compliance costs and deadweight losses, improving the efficiency of the tax system as whole. This means businesses will be more productive and can make better decisions, leading to higher GDP in the long run.

<sup>25</sup> Compare Board of Taxation *Charter* <<https://taxboard.gov.au/about/governance>>; see for example Board of Taxation *Post Implementation Review of Division 7A of Part III of the Income Tax Assessment Act 1936* (November 2014) at [1.7].

<sup>26</sup> Compare Sawyer, above n 14, at 110-121.

### **Social (including distributional equity) and environmental acceptability**

- 4.3 While PaRS currently considers the social and environmental consequences of policies within its work programme, the TLC's independence would enable it to consider (and consult on) the social and environmental outcomes of less politically or administratively "sexy" areas.

### **Feasibility of introduction, including political and public acceptability**

- 4.4 The TLC should be politically and publicly acceptable given its focus on non-political aspects of tax policy, and the fact it is modelled on the "first class" NZLC. The main arguments against the TLC are cost and the duplication of PaRS functions. These are addressed below.

#### *Cost*

- 4.5 As outlined at paragraph 3.22 above the TLC would require a modest additional appropriation. Over the medium term this should be outweighed by reducing tax-related inefficiencies in the economy, leading to a more productive allocation of resources and higher tax revenues.

#### *Duplication of functions*

- 4.6 As outlined at paragraph 3.23 above:
- (a) the TLC's remedial, PIR and project reporting roles would not be shared with PaRS; and
  - (b) the TLC's independent consultative model counterbalances Inland Revenue's institutional expertise.

### **Impact on simplicity of tax system**

- 4.7 The TLC should promote the simplification of tax laws for the reasons set out at paragraphs 4.1 and 4.2 above.

## **5. Conclusion**

- 5.1 New Zealand's tax policy process has long overlooked the NZLC model. The NZLC has enjoyed a 40-year track record of first-class law reform while competing priorities and a recent collection focus have undermined the GTPP. By adapting the NZLC model to tax, the TLC can fill the gaps in PaRS's policy process and contribute to the enactment of tax laws that are sufficient, *efficient*, and fair.