

KEYNOTE ADDRESS

TAX DISPUTES IN NEW ZEALAND

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I OVERVIEW

When I was invited to present a paper at this conference, the topic was left to me (providing, of course, that it was about tax and ideally had a sustainability theme). “Free choice” of this kind usually puts me in state of terminal indecision. In this instance, however, I had no difficulty deciding on the New Zealand tax disputes process. The reason is simple enough. It is the area of tax law that I now know best and am most comfortable discussing with an audience of tax teachers. This, in turn, reflects what I regard as the dispiriting reality that most tax cases are about process.

It used to be very different. I was appointed to the bench in late 1997. For the preceding 19 years, tax advice and litigation formed an appreciable and, at times, significant part of my professional practice. During this time all I needed to know about the tax disputes resolution procedure could have been written on the back of an envelope.

The change between then and now has been immense. In this paper I will discuss why and how this change occurred and its practical implications and possible reforms and at the same time offer a gentle critique based on my current and admittedly limited perspective as an appellate judge. My discussion will focus primarily but not exclusively on the pre-assessment procedures which have attracted more debate than the post-assessment challenge process.

II A SHORT HISTORY

The relevant history is well known.¹ Prior to 1996, the statutory scheme for the resolution of tax disputes was simple. The key provisions were four sections in the Income Tax Act 1976² and three sections in the Inland Revenue Department Act 1974.³ The process was initiated by a letter of objection, which could be broadly expressed and thus in short form. The Commissioner was required to consider the objection. If the objection was not wholly allowed, the taxpayer could require the objection to be heard and determined by the Taxation Review Authority or, in some instances, by the High Court. The primary infelicity in legal framework (at least to my way of thinking) was that objections reached the High Court via the rather cumbersome case stated procedure. In practice, however, tax disputes were often drawn out over many years. I suspect

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¹ It is thoroughly discussed in G Blanchard, “The Case For A Simplified Tax Disputes Process” (2005) 11 *New Zealand Journal of Taxation Law and Policy* 417.

² Sections 30 – 33.

³ Sections 34 – 36.

that this was a function of a number of factors: some inefficiencies within the Inland Revenue Department; aspects of the system which at one time incentivised foot-dragging by taxpayers; and little or no case management of tax disputes within the court system.

In 1994, the Organisational Review Committee recommended major procedural changes.⁴ The Committee considered that insufficient care was being taken to ensure that assessments were correct before they were issued. A taxpayer who did not have a full understanding of the basis of an assessment could be expected to object in very general terms. The key areas of dispute were thus not necessarily identified at an early stage in the process. In practice, the officer responsible for the audit considered objections (although a decision to disallow an objection was made by a superior). The costs of the objection process were such that either the Department or taxpayers often conceded disputes. When litigation was pursued, the process could be inefficient, with judges required to determine cases which had not been appropriately considered at the assessment stage. As well, there were unacceptable delays associated with the resolution of tax disputes.

At the time, around 29 percent of objections were allowed in full and 19 percent were allowed in part. The Commissioner also conceded (at least in part) in 30 percent of the disputes in which a case stated was requested. The Committee's formal recommendations were in these terms:⁵

A revised tax disputes resolution process should be introduced with a revised approach to the pre-assessment phase.

Legislative changes should be made to introduce 'all cards on the table' and appropriate evidence exclusion provisions, to remove the legal requirement for a taxpayer to lodge an objection with the Commissioner and to provide for taxpayer initiated litigation to be subject to standard judicial timetabling.

A review of the operation of the new procedures for disputes resolution should be carried out two years after all the elements of the proposals are in place.

A simple, 'fast track', non-precedential procedure for dealing with small claims should be introduced as part of the jurisdiction of the Taxation Review Authority.

The Committee also expressed the following conclusion:⁶

The audit investigation and final quantification of liability should, as far as practicable, be clearly separated. The purpose is to provide an impartial application of tax law and greater application of technical expertise to the affairs of individuals prior to the issue of an assessment. In turn this will decrease the likelihood and grounds for disputes... .

The pre-assessment procedural recommendations of the Committee formed the basis of the 1996 amendments to the Tax Administration Act 1994 which inserted a new Part 4A into that Act. Section 89A(1) explained the purpose of the new Part:

(1) The purpose of this Part is to establish procedures that will—

⁴ Organisational Review Committee *Organisational Review of the Inland Revenue Department* (Wellington, April 1994).

⁵ See n 4, 70-71.

⁶ See n 4, 67.

- (a) Improve the accuracy of disputable decisions made by the Commissioner under certain of the Inland Revenue Acts; and
- (b) Reduce the likelihood of disputes arising between the Commissioner and taxpayers by encouraging open and full communication—
 - (i) To the Commissioner, of all information necessary for making accurate disputable decisions; and
 - (ii) To the taxpayers, of the basis for disputable decisions to be made by the Commissioner; and
- (c) Promote the early identification of the basis for any dispute concerning a disputable decision; and
- (d) Promote the prompt and efficient resolution of any dispute concerning a disputable decision by requiring the issues and evidence to be considered by the Commissioner and a disputant before the disputant commences proceedings.

As well, a new Part 8A was inserted into the Tax Administration Act which provided for challenge proceedings. The new procedures in operation were assessed in 2003⁷ and have been subject to some amendment. Most significantly, the amendments limit the discretion of the Commissioner to take short-cuts in relation to the pre-assessment dispute resolution process. This applies even where the time bar is imminent, although the Commissioner may apply to the High Court for permission to truncate the process.⁸ In this paper I address the relevant legislative provisions as they now stand, but it is important to recognise that most of the cases were decided under the less prescriptive procedures as introduced in 1996.

III THE PRE-ASSESSMENT DISPUTE PROCEDURE

A Commissioner initiated adjustments

The usual starting point is a notice of proposed adjustment (NOPA).⁹ Leaving aside cases where the small claims jurisdiction of the Taxation Review Authority is invoked,¹⁰ the next step is a notice of response (NOR),¹¹ in the absence of which the taxpayer is deemed to have accepted the NOPA.¹²

As a matter of practice (but not law), the NOR is usually followed by a conference.¹³ If a dispute is not resolved at a conference (because there is no conference or a conference is unsuccessful), the Commissioner must, except in specified circumstances,¹⁴ issue a disclosure notice together with his statement of

⁷ Inland Revenue Department *Resolving Tax Disputes: A Legislative Review* (Wellington, July 2003).

⁸ Section 89N(3). Where such an application is made, the time bar is extended until the application is determined, see s 89N(5).

⁹ Limited exceptions are provided for in s 89C.

¹⁰ See s 89E.

¹¹ Section 89G.

¹² Section 89H(1).

¹³ See SPS 08/01: *Disputes Resolution Process Commenced by the Commissioner of Inland Revenue* at [219] and ff.

¹⁴ See ss 89M(2) and 89N(1)(c).

position (SOP).¹⁵ The taxpayer is then required to issue the Commissioner with a SOP.¹⁶ SOPs must set out the facts, evidence and propositions of law on which the party intends to rely and must identify the issues the party considers will arise.

This exchange of documents triggers the evidence exclusion rule, which is found in s 138G(1) and (2). In simple terms, the rule limits the parties in any challenge to the facts, evidence, issues and propositions of law that are disclosed in the SOPs.¹⁷ Jurisdiction to allow a party to go beyond that disclosed is limited to where the omitted facts, evidence, issues or propositions of law could not have been, with due diligence, discovered or discerned at the appropriate time and their admission is necessary to avoid “manifest injustice”.¹⁸

In general, and with limited exceptions,¹⁹ the Commissioner must “consider” the taxpayer’s SOP before issuing an amended assessment.²⁰ The details of this consideration are not spelt out in the statute, but customarily involve a reference to the Inland Revenue Department’s Adjudication Unit.²¹ The courts, however, will not require the Commissioner to go through the conference and adjudication processes.²² As Mark Keating has pointed out,²³ in this respect the courts are less demanding than the Commissioner’s own policy statement (which indicates that, wherever practicable, all disputes must be referred to the Adjudication Unit).²⁴

If the Adjudication Unit’s decision is in favour of the taxpayer, it will be final. If not, the Commissioner will then issue an assessment that is in accordance with the Adjudication Unit’s determination. This assessment is then subject to the challenge procedure.

In cases that involve factual disputes, the utility of the adjudication phase (in which no attempt is made to resolve such disputes) is well open to question.²⁵ I should note that most of the cases that have so far come before the courts have not involved the disclosure notice/SOP processes.²⁶ So how the evidence exclusion rule will work in practice has yet to be seen.

B *Taxpayer-initiated disputes*

Broadly similar processes apply in the case of taxpayer-initiated disputes.²⁷ The original purpose of providing for taxpayer-initiated NOPAs was to provide for circumstances in which either the Commissioner had proceeded to an assessment without issuing a NOPA or the taxpayer wished to correct a

¹⁵ See s 89M(1) and (3).

¹⁶ See s 89M(5).

¹⁷ Section 138G(1).

¹⁸ Section 138G(2).

¹⁹ See s 89N(1)(c).

²⁰ See s 89N(2).

²¹ See n 20.

²² See *Commissioner of Inland Revenue v ANZ National Bank Ltd* (2007) 23 NZTC 21,167 (CA).

²³ M Keating “New Zealand’s Tax Dispute Procedure – Time for a Change” (2008) 14 *New Zealand Journal of Taxation Law and Policy* 425 at 442.

²⁴ Inland Revenue, SPS 08/01: *Disputes Resolution Process Commenced by the Commissioner of Inland Revenue* at [202].

²⁵ See J Coleman “Tax Update” [2007] *New Zealand Law Journal* 407.

²⁶ This is true for instance of *Commissioner of Inland Revenue v Zentrum Holdings Ltd* [2007] 1 NZLR 145 (CA).

²⁷ See Inland Revenue, SPS 08/02: *Disputes Resolution Process Commenced by A Taxpayer*.

mistake in a return.²⁸ In practice, however, this process is usually resorted to where the taxpayer has filed a conservative return and then seeks an adjustment. Adopting this approach has the advantage (from the point of view of the taxpayer) of avoiding penalties.²⁹

IV POST-ASSESSMENT PROCESSES

Part 8A of the Tax Administration Act provides for a challenge process under which the taxpayer may challenge an assessment either before the Taxation Review Authority or the High Court. It is clear enough that this process was intended by the legislature to be the primary – indeed those of a literal frame of mind might think the only – way of challenging an assessment. I say this given ss 109 and 114, which relevantly provide:

109 Assessments deemed correct except in proceedings

Except in... a challenge under Part 8A,—

- (a) No disputable decision may be disputed in a court or in any proceedings on any ground whatsoever; and
- (b) Every disputable decision and, where relevant, all of its particulars are deemed to be, and are to be taken as being, correct in all respects.

114 Validity of assessments

An assessment made by the Commissioner is not invalidated—

- (a) Through a failure to comply with a provision of this Act or another Inland Revenue Act; or
- (b) Because the assessment is made wholly or partially in compliance with—
 - (i) A direction or recommendation made by an authorised officer on matters relating to the assessment;
 - (ii) A current policy or practice approved by the Commissioner that is applicable to matters relating to the assessment.

Consistently with the recommendations of the Organisational Review Committee, a challenge in the High Court is now dealt with in the same way as other civil litigation. The implementation of this recommendation, along with the enactment of the care and management provisions of the Tax Administration Act,³⁰ have had major impacts on the way in which tax litigation is conducted. This is exemplified by:

The (now routine) use of discovery, in contradistinction to past practice;³¹

Changes in the practice as to costs³² and an associated recognition that the Commissioner is entitled to take a commercial approach to the settlement of tax litigation;³³ and

²⁸ Inland Revenue Department *Resolving Tax Disputes: A Legislative Review* (Wellington, July 2003) at 5.3.

²⁹ See n 1 at 425.

³⁰ See ss 6 and 6A.

³¹ Compare *Cates v Commissioner of Inland Revenue* [1982] 1 NZLR 530 at 533 (CA) per Cooke J, where the jurisdiction to order discovery was seen as one which would rarely be exercised and was appropriate only for “an occasional tax case”.

³² See *Auckland Gas Co Ltd v Commissioner of Inland Revenue* [1999] 2 NZLR 409 (CA).

³³ See for instance *Accent Management Ltd v Commissioner of Inland Revenue* (2007) 23 NZTC 21,366 (CA).

An open justice approach to publicity in relation to the affairs of taxpayers who litigate in the High Court.³⁴

Uncertainty remains as to the scope for judicial review in tax disputes. The New Zealand appellate decisions support the proposition that it is open to a taxpayer to challenge what purports to be an assessment which in fact does not represent the genuine assessment of the Commissioner as to the tax position of the taxpayer.³⁵ Generally the courts have accepted that the correctness of a tax assessment can only be challenged in challenge proceedings³⁶ and that judicial review is reserved for exceptional cases.³⁷ Running through the cases, however, has been something of a reluctance to treat ss 109 and 114 of the Tax Administration Act as meaning what they say. A taxpayer who seeks judicial review of an assessment might be thought to be disputing it and doing so in defiance of s 109(a). Section 109(b) deems an assessment to be “correct in all respects”, which might be thought to extend to its validity. On a literal approach it is difficult to reconcile the statutory requirement that a disputed assessment be taken as “correct in all respects” with judicial review on grounds of invalidity.

The relevant Australian legislative provisions (ss 175, 175A and 177 of the Income Tax Assessment Act 1936 (Cth)) are similar to ss 109 and 114 of the Tax Administration Act. Recently the High Court of Australia has re-emphasised the primacy of the objection and appeal processes, observing:³⁸

[24] Section 175 must be read with s 175A and s 177(1). If that be done, the result is that the validity of an assessment is not affected by failure to comply with any provision of the Act, but a dissatisfied taxpayer may object to the assessment in the manner set out in Pt IVC of the Administration Act; in review or appeal proceedings under Pt IVC the amount and all the particulars of the assessment may be challenged by the taxpayer but with the burden of proof provided in s 14ZZK and s 14ZZO of the Administration Act. Where s 175 applies, errors in the process of assessment do not go to jurisdiction and so do not attract the remedy of a constitutional writ under s 75(v) of the Constitution or under s 39B of the Judiciary Act.

[25] But what are the limits beyond which s 175 does not reach? The section operates only where there has been what answers the statutory description of an “assessment”. Reference is made later in these reasons to so-called tentative or provisional assessments which for that reason do not answer the statutory description in s 175 and which may attract a remedy for jurisdictional error. Further, conscious maladministration of the assessment process may be said also not to produce an “assessment” to which s 175 applies. Whether this be so is an important issue for the present appeal.

In effect the Court confined judicial review to two circumstances: first, where what is said to be an assessment is not in truth an assessment; and secondly, where there has been conscious maladministration. These two concepts were, to

³⁴ See for instance *Muir v Commissioner of Inland Revenue* (2004) 21 NZTC 18,894 (CA).

³⁵ *Commissioner of Inland Revenue v Canterbury Frozen Meat Co Ltd* [1994] 2 NZLR 681 (CA).

³⁶ *Commissioner of Inland Revenue v Lemmington Holdings Ltd* [1982] 1 NZLR 517 (CA) and *Miller v Commissioner of Inland Revenue* [1995] 3 NZLR 664 (CA).

³⁷ *Miller v Commissioner of Inland Revenue* [2001] 3 NZLR 316 at [18] (PC).

³⁸ *Commissioner of Taxation v Futuris Corporation Ltd* (2008) 247 ALR 605 (HCA).

some extent, run together, with both seen as not producing an assessment that is immune from judicial review.

In the past, taxpayers going down the judicial review route have often sought to delay the statutory processes (whether prior to or after assessment) until the judicial review proceedings are completed; this on the ostensibly sensible ground that before this point it would be premature to proceed with the statutory process. The potential for delay is obvious. As well, collateral challenge diverts effort and resources from what might be thought to be the more important task of determining the correct tax position of the taxpayer.

V OTHER CONTEXTUAL FACTORS

Contextual but nonetheless very important practical features of the tax disputes process are use of money charges and penalties. These make unsuccessful tax litigation an expensive exercise for a taxpayer, and this necessarily provides incentives which encourage settlement.

This is illustrated by what happened in the *Trinity* litigation.³⁹ The settlement terms reached by the investors who settled with the Commissioner on the eve of trial⁴⁰ produced a result for them which is in marked contrast to the consequences for the investors who litigated the case as far as the Supreme Court. Another relevant contextual factor is the 1996 establishment by the Inland Revenue Department of a litigation management unit. I suspect that this has resulted in a more structured and systematic approach by the Department to the management of complex tax disputes.

VI JUDICIAL INVOLVEMENT IN TAX DISPUTES – MORE ABOUT PROCESS THAN SUBSTANCE

A The mix of cases

Tax litigation is frequently about process. Mark Keating's recent review of the number and type of reported tax cases over the past three years yielded the following findings:⁴¹

From 2005 to the present, there was a total of 121 reported cases on procedural issues in the High Court, Court of Appeal and Supreme Court, while over that period there were only 27 purely substantive cases. Over that same period, the Taxation Review Authority (TRA) has determined 23 procedural cases compared with 29 substantive cases.

The distinction between process and substance can be slippery, because often enough determination of a procedural issue effectively resolves the case.⁴² That said, Mr Keating's observations accord with my own experience. In the five years during which I have been a member of the Court of Appeal, most of the tax cases I have sat on have been procedural in nature.

³⁹ This litigation recently culminated in *Ben Nevis Forestry Ventures Ltd v Commissioner of Inland Revenue* [2008] NZSC 115.

⁴⁰ These are set out in *Accent Management Ltd v Commissioner of Inland Revenue* (2007) 23 NZTC 21,366 at [7] (CA).

⁴¹ See n 23 at 428.

⁴² As in *Allen v Commissioner of Inland Revenue* [2006] 2 NZLR 1 (SC).

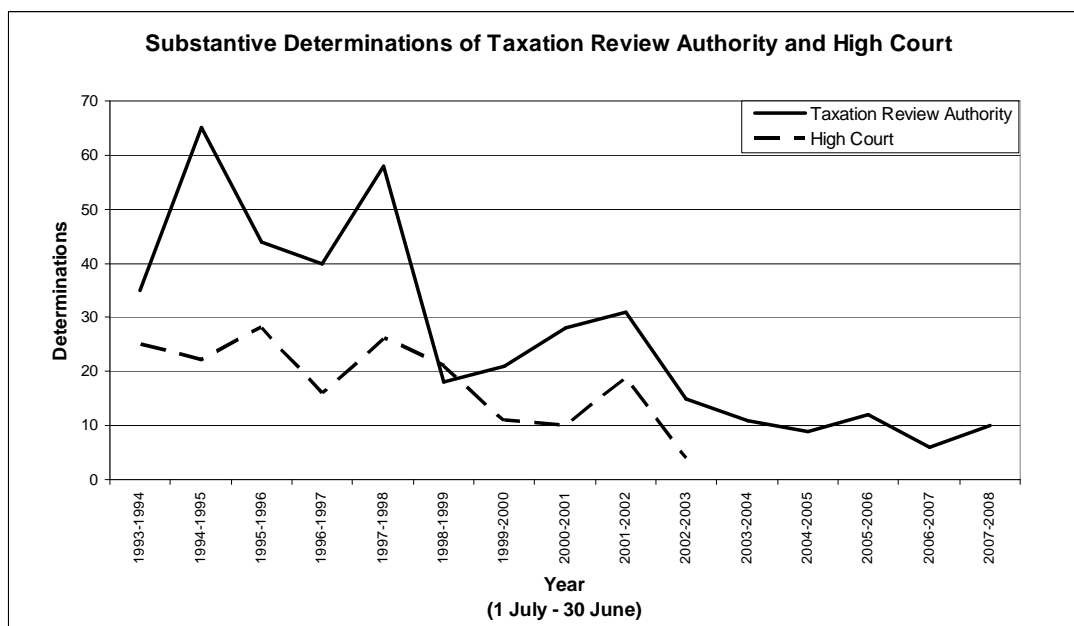
It is not entirely easy to assemble statistics as to the numbers of tax disputes that are resolved substantively by judicial determination. These figures, which once appeared in Inland Revenue Department annual reports, are apparently no longer collected. The best that I can offer is the following information which my clerk Peter Marshall was able to compile from various sources:⁴³

Table 1: Number of Tax Disputes: TRA and High Court

	Taxation Review Authority	High Court
1993-1994	35	25
1994-1995	65	22
1995-1996	44	28
1996-1997	40	16
1997-1998	58	26
1998-1999	18	21
1999-2000	21	11
2000-2001	28	10
2001-2002	31	19
2002-2003	15	4
2003-2004	11	
2004-2005	9	
2005-2006	12	
2006-2007	6	
2007-2008	10	

As far as I can tell, between 1996 and 2006 only 6 cases were determined by the Taxation Review Authority in its small claims jurisdiction. It appears that subsequently one more case has been determined in this way. The sharp decline in substantive determinations is perhaps best portrayed graphically:

⁴³ Up to 2002-2003 the data was sourced either directly from the Department or from its annual reports. After this, the data was compiled manually from the archives of the Ministry of Justice's Tribunals Unit: a substantive determination was defined to exclude interlocutory rulings (except successful strike out applications that substantively disposed of the case) and interim decisions. Figures for the High Court after 2002-2003 were not available.



B Why so many procedural cases?

I think it unsurprising that there have been, and continue to be, so many procedural disputes. The new procedures as introduced in 1996 differed significantly from what had gone before. Some teething difficulties were thus inevitable. More importantly, however, there are some design features and flaws of the scheme that encourage dispute.

To my way of thinking, one significant flaw is that the new provisions did not fit altogether easily with other, unamended, provisions of the Tax Administration Act. For instance, prior to the 2004 amendments, s 113 provided simply:

113 Commissioner may at any time amend assessments

(1) The Commissioner may from time to time, and at any time, make all such alterations in or additions to an assessment as the Commissioner thinks necessary in order to ensure its correctness, notwithstanding that tax already assessed may have been paid.

(2) If any such alteration or addition has the effect of imposing any fresh liability or increasing any existing liability, notice of it shall be given by the Commissioner to the taxpayer affected.

Although some attempts have been made to tidy up the incongruities (for instance s 89N has been introduced and s 113 is now expressed to be subject to it), there remain loose ends as to the consequences, if any, of deviations by the Commissioner from the scheme of Part 4A and also as to the impact of the evidence exclusion rule.

Importantly, s 114(a) prevents any assessment being challenged on grounds of non-compliance with procedural requirements. This section has not been amended and it remains to be seen whether it will provide a safe long stop for the Commissioner in the event of established non-compliance with Part 4A. It probably will do so with breaches of s 89C as the legislation contemplates that an

assessment issued in breach of s 89C is nonetheless valid.⁴⁴ Reliance on s 114, however, arguably will not save an assessment issued in breach of s 89N given the peremptory language used and the amendment to s 113. If so, this may prove a little awkward as some of the exceptions listed in s 89N(1)(c) involve questions of degree⁴⁵ and there may be legitimate scope for disagreement as to whether they have been properly invoked. The possibility that truncating the process may result in the invalidity of an assessment could deter the Commissioner from invoking these exceptions. And where such an exception is invoked by the Commissioner, the possibility of securing a technical knock out will encourage the taxpayer to challenge the process.

So, to some (but an uncertain) extent, the legislative provisions in Part 4A are directory⁴⁶ in character and the incoherent structure of the legislation invites litigation.

The evidence exclusion rule applies not only to “evidence” but also to legal propositions. What is not clear from the statute as it now stands is the impact of the evidence exclusion rule on the s 138P entitlement of a hearing authority (whether Taxation Review Authority or High Court) to exercise the powers of the Commissioner. Is it possible for a hearing authority to decide a case on the basis of a legal proposition not advanced in the SOPs? If the disclosure notice/SOP procedure had been invoked in the Trinity case, it is almost inconceivable that the Commissioner would have been bold enough to advance the legal proposition that s BG 1 of the Income Tax Act 1994 means what it says. Yet, on perhaps a simplistic analysis, this is pretty much what a majority in the Supreme Court concluded.⁴⁷ Would the majority have been debarred from deciding the case on that basis if the evidence exclusion rule applied?

A related problem is the new disputes resolution process has always only been partially implemented by legislation. The Organisational Review Committee envisaged that:⁴⁸

The audit investigation and final quantification of liability should, as far as practicable, be clearly separated.

This, however, is only currently provided for at the adjudication step in the process, which is not legislatively required. While the courts do not hold the Commissioner to administrative procedures laid down in the relevant policy statements, inconsistency between policy statements and the Commissioner’s actions has proved to be a common trigger for litigation.

This last point raises an issue as to the design of the legislation. Pre-assessment procedures involving more elaborate debate between Commissioner and taxpayer (including provision for NOPAs, NORs, conferences and reference to the Adjudication Unit) could have been introduced administratively. If that approach had been adopted, the need for legislative amendment would have been limited – confined probably to the establishment of an evidence exclusion rule (if thought appropriate) and a small claims procedure.

⁴⁴ See s 89D(b) and *Spencer v Commissioner of Inland Revenue* (2004) 21 NZTC 18,818 (HC) at [50].

⁴⁵ See for example s 89N(1)(c)(ii) and (iii).

⁴⁶ Not a very good word, I know, but it captures the idea that non-compliance might not matter.

⁴⁷ *Ben Nevis Forestry Ventures Ltd v Commissioner of Inland Revenue* [2008] NZSC 115.

⁴⁸ Organisational Review Committee *Organisational Review of the Inland Revenue Department*, (Wellington, April 1994) at 67.

Alternatively, the dispute resolution process could have been legislated for comprehensively. What has happened, however, is that a system of dispute resolution which was presumably originally designed as a single comprehensive system, is now implemented partly by statute and partly as a matter of administrative practice. I suspect that whoever drafted s 89N (and in particular came up with the heading “completing the disputes process”) had in mind the disputes process as a whole (including the administrative steps of conference and adjudication). As it is, however, the section ends up, rather lamely to my way of thinking, with simply requiring the Commissioner to “consider” the taxpayer’s statement of position. Incoherence of this nature breeds disputes.

C Why so few substantive judicial determinations?

In the five years from 1993 to 1998, the Taxation Review Authority issued an average of 48.4 substantive determinations per year, whereas in the last five completed years this figure has plummeted to 9.6, a drop of over 80 percent. Equivalent figures are not available for substantive High Court determinations over the past five years. Despite this, given the way the annual number of High Court determinations has closely mirrored those of the Taxation Review Authority,⁴⁹ it is reasonable to assume that a corresponding decline has occurred in relation to High Court determinations.⁵⁰

The Inland Revenue Department’s 2003 discussion paper noted a sharp reduction in the number of litigated tax cases and commented:⁵¹

The current process would appear to a significant extent to be meeting its objectives because the number of audited cases that are disputed is decreasing and the cases that are being litigated are also decreasing.

The same paper noted that it is generally the higher value cases which are being litigated and that the Commissioner is becoming increasingly more successful in cases which are litigated.

The pre-assessment dispute process has presumably improved the accuracy of the assessment process. If so, this could be expected to have reduced the number of assessments that are properly open to dispute and correspondingly the number of disputes resulting in judicial determination. In particular, the adjudication process has involved administrative and pre-assessment determination of what would otherwise have been litigated disputes. It is also plausible to assume that the more robust the pre-assessment process, the more successful the Commissioner will be in the cases which do go to trial. So to some extent the comment in the discussion paper is probably right. I nonetheless see it as probably an incomplete explanation for what has happened. Other relevant factors presumably are:

Litigation risks associated with use of money charges and penalties that may serve to deter challenge proceedings.

The Commissioner’s ability to settle cases on a commercial basis.

⁴⁹ See the graph at p 9, above.

⁵⁰ This also accords with Keating’s figures, quoted above at p 8, in which he identified only 27 reported substantive tax determinations in the High Court over the period 2005-2008.

⁵¹ Inland Revenue Department *Resolving Tax Disputes: A Legislative Review* (Wellington, July 2003) at [1.7].

I see grounds for concern in the limited number of cases that are determined substantively by the courts. It means that taxation disputes are being largely resolved within the Inland Revenue Department. Because internal departmental opinions are necessarily backwards looking and controlled by the existing patterns of judicial decisions, there is little scope for judicial development of the law – the sort of fresh look exemplified by the Supreme Court judgment in the Trinity case. Associated with all of this is the possibility that some (and perhaps many) taxpayers are burnt off by the costs of the process and by the risks of litigation. The resulting practical unavailability of departmental opinions may be unhealthy in a society that subscribes to the rule of law.

VII POSSIBLE OUTCOMES

A number of possible reforms to the pre-assessment process have been promoted. The August 2008 Joint Submission made by the taxation committee of the New Zealand Law Society and the national tax committee of the New Zealand Institute of Chartered Accountants addressing Parts 4A and 8A of the Tax Administration Act suggested:

- More focused, coherent and clear NOPAs;
- Independent review of NOPAs and NORs within the Inland Revenue Department prior to the adjudication phase;
- A compulsory conference system;
- A softening of the use of money interest regime;
- A limiting of the evidence exclusion rule so that it applies only to propositions of law not advanced in the relevant statements of position;
- More symmetry in terms of time frames and sanctions as between Commissioner and taxpayer;
- Permitting the Adjudication Unit to make factual determinations; and
- A more coherent approach within the Department to the settlement of tax disputes.

Reforms suggested by commentators include compulsory mediation,⁵² entitlement for taxpayers to go straight to challenge proceedings after the exchange of NOPAs and NORs⁵³ and complete abolition of the evidence exclusion rule.⁵⁴

As a Judge, I perhaps have a bias towards judicial – over administrative – determination. And I have a very particular perspective which is necessarily associated with the sort of tax cases which reach the Court of Appeal – cases where it was reasonably clear from the outset that there would be litigation. For cases of that type (ie where litigation is practically inevitable) I think it clear the pre-assessment disputes procedures are unnecessarily complex, repetitive and time consuming (not to mention expensive for participants). Judges are well used to disclosure (in the context of discovery rules), pleading requirements and the circumstances in which amendment of pleadings is appropriate. Building functionally similar procedures into the pre-assessment stage of a tax dispute necessarily involves duplication of what is to follow if there is litigation.

⁵² See n 23 at 454.

⁵³ See J Coleman “Tax Update” [2007] *New Zealand Law Journal* 407 at 407 and see n 1 at 438.

⁵⁴ See n 53, at 408 and see n 1 at 438 and 439.

Importantly, the Commissioner, as a player/referee, is not well placed to manage such processes. The recommendations of the Organisational Review Committee came at a time when case management in the High Court was a comparatively recent innovation. My reading of the report suggests that the Committee saw the timetabling of litigation as the primary benefit of “judicial management” and in this respect may have underestimated the ability of the Court system to manage disputes in an effective and fair manner.⁵⁵

As an appellate Judge I also have a preference for accurate factual and legal determinations unstructured by artificial constraints. Although I have not yet been required to deal with cases in which the evidence exclusion rule has had a role to play, I suspect that it will become extremely cumbersome in practice, with arguments of a “how long is piece of string character” as to its application and perhaps forced resort to either the exceptions (which are not well addressed to the exigencies of the resolution of complex disputes) or perhaps s 138P. Fear of falling foul of the evidence exclusion rule encourages prolixity in SOPs. Because the evidence exclusion rule promotes reference to every conceivable argument that might be deployed, it has the perverse tendency to obscure rather than to elucidate what is truly in issue.

Further, I have a distinct preference for procedures that facilitate the resolution of substantive disputes rather than proliferate process disputes. As I have endeavoured to explain, the design of the dispute resolution process made procedural disputes inevitable.

I do not think that the answer lies in more add-ons to a process, which is already sufficiently complex. Indeed, it might be simpler and more effective to strip the required statutory process back to the bare essentials of assessment and challenge, and leave everything else to departmental practice, with the Commissioner and taxpayer free to engage in elaborate pre-assessment exchanges if they choose. This would reduce the expense and time associated with tax disputes although it would presumably also result in less accuracy in the assessment process.

I have been at pains to recognise the limitations of my perspective and I accept that the tax system cannot be designed around the comparatively few tax disputes that go to court. That said, the issue whether the whole process has become too hard and too expensive for taxpayers warrants consideration as part of a fresh look at the system, incorporating not only the process perspective of the Inland Revenue Department and the practical requirements of tax advisers and taxpayers but also rule of law principles.

⁵⁵ See g Blanchard “The Case For A Simplified Tax Disputes Process”, (2005) 11 *New Zealand Journal of Taxation Law and Policy* 417 at 437.

APPENDIX

Relevant Sections of the Tax Administration Act 1994

6 Responsibility on Ministers and officials to protect integrity of tax system

- (1) Every Minister and every officer of any government agency having responsibilities under this Act or any other Act in relation to the collection of taxes and other functions under the Inland Revenue Acts are at all times to use their best endeavours to protect the integrity of the tax system.
- (2) Without limiting its meaning, **the integrity of the tax system** includes—
 - (a) Taxpayer perceptions of that integrity; and
 - (b) The rights of taxpayers to have their liability determined fairly, impartially, and according to law; and
 - (c) The rights of taxpayers to have their individual affairs kept confidential and treated with no greater or lesser favour than the tax affairs of other taxpayers; and
 - (d) The responsibilities of taxpayers to comply with the law; and
 - (e) The responsibilities of those administering the law to maintain the confidentiality of the affairs of taxpayers; and
 - (f) The responsibilities of those administering the law to do so fairly, impartially, and according to law.

Compare: 1974 No 133 s 4(1)

6A Commissioner of Inland Revenue

- (1) The person appointed as chief executive of the Department under the State Sector Act 1988 is designated the Commissioner of Inland Revenue.
- (2) The Commissioner is charged with the care and management of the taxes covered by the Inland Revenue Acts and with such other functions as may be conferred on the Commissioner.
- (3) In collecting the taxes committed to the Commissioner's charge, and notwithstanding anything in the Inland Revenue Acts, it is the duty of the Commissioner to collect over time the highest net revenue that is practicable within the law having regard to—
 - (a) The resources available to the Commissioner; and
 - (b) The importance of promoting compliance, especially voluntary compliance, by all taxpayers with the Inland Revenue Acts; and
 - (c) The compliance costs incurred by taxpayers.

89A Purpose of this Part

- (1) The purpose of this Part is to establish procedures that will—
 - (a) Improve the accuracy of disputable decisions made by the Commissioner under certain of the Inland Revenue Acts; and
 - (b) Reduce the likelihood of disputes arising between the Commissioner and taxpayers by encouraging open and full communication—
 - (i) To the Commissioner, of all information necessary for making accurate disputable decisions; and
 - (ii) To the taxpayers, of the basis for disputable decisions to be made by the Commissioner; and
 - (c) Promote the early identification of the basis for any dispute concerning a disputable decision; and
 - (d) Promote the prompt and efficient resolution of any dispute concerning a disputable decision by requiring the issues and evidence to be considered by the Commissioner and a disputant before the disputant commences proceedings.
- (2) This Part does not apply with respect to any tax returns or notices of assessments that are, or become, subject to objection proceedings under Part 8.
- (3) Despite section 1(2), this Part applies to disputable decisions made by the Commissioner for tax years before the 1994-95 tax year.

89C Notices of proposed adjustment required to be issued by Commissioner

The Commissioner must issue a notice of proposed adjustment before the Commissioner makes an assessment, unless—

- (a) The assessment corresponds with a tax return that has been provided by the taxpayer; or
- (b) The taxpayer has provided a tax return which, in the Commissioner's opinion, appears to contain a simple or obvious mistake or oversight, and the assessment merely corrects the mistake or oversight; or
- (c) The assessment corrects a tax position previously taken by the taxpayer in a way or manner agreed by the Commissioner and the taxpayer; or
- (d) The assessment reflects an agreement reached between the Commissioner and the taxpayer; or
- (db) the assessment is made in relation to a matter for which the material facts and relevant law are identical to those for an assessment of the taxpayer for another period that is at the time the subject of court proceedings; or
- (e) The Commissioner has reasonable grounds to believe a notice may cause the taxpayer or an associated person—

- (i) To leave New Zealand; or
 - (ii) To take steps, in relation to the existence or location of the taxpayer's assets, making it harder for the Commissioner to collect the tax from the taxpayer; or
- (eb) the Commissioner has reasonable grounds to believe that the taxpayer has ... been involved in fraudulent activity; or
- (f) The assessment corrects a tax position previously taken by a taxpayer that, in the opinion of the Commissioner is, or is the result of, a vexatious or frivolous act of, or vexatious or frivolous failure to act by, the taxpayer; or
- (g) The assessment is made as a result of a direction or determination of a court or the Taxation Review Authority; or
- (h) The taxpayer has not provided a tax return when and as required by a tax law; or
- (i) the assessment is made following the failure by a taxpayer to withhold or deduct an amount required to be withheld or deducted by a tax law or to account for an amount withheld or deducted in the manner required by a tax law; or
- (j) The taxpayer is entitled to issue a notice of proposed adjustment in respect of a tax return provided by the taxpayer, and has done so; or
- (k) The assessment corrects a tax position taken by the taxpayer or an associated person as a consequence or result of an incorrect tax position taken by another taxpayer, and, at the time the Commissioner makes the assessment, the Commissioner has made, or is able to make, an assessment for that other taxpayer for the correct amount of tax payable by that other taxpayer; or
- (l) The assessment results from an income statement under Part 3A; or
- (m) the assessment includes a calculation by the Commissioner of a tax credit identified in subparts MA to MF and MZ of the Income Tax Act 2007.

89D Taxpayers and others with standing may issue notices of proposed adjustment

- (1) If the Commissioner—
- (a) Issues a notice of assessment to a taxpayer; and
 - (b) Has not previously issued a notice of proposed adjustment to the taxpayer in respect of the assessment, whether or not in breach of section 89C,—

the taxpayer may, subject to subsection (2), issue a notice of proposed adjustment in respect of the assessment.

- (2) A taxpayer who has not furnished a return of income for an assessment period may dispute the assessment made by the Commissioner only by furnishing a return of income for the assessment period.
- (2A) For the purpose of subsection (2), section 33(2) does not apply.

- (2B) A taxpayer to whom section 80F applies who has not furnished an amended income statement for an assessment period may dispute a deemed assessment under section 80H only by furnishing an amended income statement for the assessment period.
- (2C) A taxpayer who has not provided a GST tax return for a GST return period may not dispute the assessment made by the Commissioner other than by providing a GST return for the GST return period.
- (2D) For the purpose of subsection (2C), [section 16(6)] of the Goods and Services Tax Act 1985 does not apply.
- (3) If the Commissioner—
- (a) Issues a notice of disputable decision that is not a notice of assessment; and
 - (b) The notice of disputable decision affects the taxpayer,—

the taxpayer, or any other person who has the standing under a tax law to do so on behalf of the taxpayer, may issue a notice of proposed adjustment in respect of the disputable decision.

(4) *Repealed.*

- (5) For a notice of proposed adjustment issued under this section to have effect, the notice must be issued within the applicable response period.

89E Election of small claims jurisdiction of Taxation Review Authority

- (1) Where a disputant—
- (a) Issues a notice of proposed adjustment under section 89D or 89DA and the amount in dispute is \$30,000 or less; or
 - (b) Rejects a notice of proposed adjustment issued by the Commissioner under section 89B and the amount in dispute is \$30,000 or less,—

the disputant may elect, in the disputant's notice of proposed adjustment or notice of rejection, that any unresolved dispute arising from the notice of proposed adjustment is to be heard by a Taxation Review Authority acting in its small claims jurisdiction.

- (2) If a disputant elects under subsection (1) to challenge a disputable decision or tax liability in a Taxation Review Authority acting in its small claims jurisdiction, the decision is irrevocable and binds the disputant.

89G Issue of response notice

- (1) To reject a proposed adjustment, the recipient of the notice of proposed adjustment must, within the response period for the notice, notify the issuer that the adjustment is rejected by issuing a response notice.
- (2) A notice of response must state concisely—
- (a) the facts or legal arguments in the notice of proposed adjustment that the issuer of the notice of response considers are wrong; and

- (b) why the issuer of the notice of response considers those facts or legal arguments to be wrong; and
- (c) any facts and legal arguments relied on by the issuer of the notice of response; and
- (d) how the legal arguments apply to the facts; and
- (e) the quantitative adjustments to any figure referred to in the notice of proposed adjustment that result from the facts and legal arguments relied on by the issuer of the notice of response.

89H Deemed acceptance

- (1) If a disputant does not, within the response period for a notice of proposed adjustment issued by the Commissioner, reject an adjustment contained in the notice, the disputant is deemed to accept the proposed adjustment and section 89I applies.
- (2) If the Commissioner does not, within the response period for a notice of proposed adjustment issued by a disputant, reject an adjustment contained in the notice, the Commissioner is deemed to accept the proposed adjustment and section 89J applies.
- (3) Where—
 - (a) A disputant does not, within the response period for replying to a notice from the Commissioner rejecting an adjustment proposed by the disputant, reject in writing all or part of the Commissioner's notice, the disputant is deemed to accept the matters specified in the Commissioner's notice; or
 - (b) The disputant accepts all or part of the Commissioner's notice in writing,—

then, in those circumstances,—

- (c) Section 89I applies as if the matters contained in the Commissioner's notice were an adjustment or adjustments proposed by the Commissioner; and
- (d) The Commissioner's notice is deemed, for the purposes of section 89K, to be a notice of proposed adjustment.

89M Disclosure notices

- (1) Unless subsection (2) applies, and subject to section 89N, the Commissioner must issue a disclosure notice in respect of a notice of proposed adjustment to a disputant at the time or after the Commissioner or the taxpayer, as the case may be, issues the notice of proposed adjustment.
- (2) The Commissioner may not issue a disclosure notice in respect of a notice of proposed adjustment if the Commissioner has already issued a notice of disputable decision that includes, or takes account of, the adjustment proposed in the notice of proposed adjustment.
- (3) Unless the disputant has issued a notice of proposed adjustment, the Commissioner must, when issuing a disclosure notice,—

- (a) Provide the disputant with the Commissioner's statement of position; and
- (b) Include in the disclosure notice—
 - (i) A reference to section 138G; and
 - (ii) A statement as to the effect of the evidence exclusion rule.
- (4) The Commissioner's statement of position in the prescribed form must, with sufficient detail to fairly inform the disputant,—
 - (a) Give an outline of the facts on which the Commissioner intends to rely; and
 - (b) Give an outline of the evidence on which the Commissioner intends to rely; and
 - (c) Give an outline of the issues that the Commissioner considers will arise; and
 - (d) Specify the propositions of law on which the Commissioner intends to rely.
- (5) If the Commissioner issues a disclosure notice to a disputant, the disputant must issue the Commissioner with the disputant's statement of position within the response period for the disclosure notice.
- (6) A disputant's statement of position in the prescribed form must, with sufficient detail to fairly inform the Commissioner,—
 - (a) Give an outline of the facts on which the disputant intends to rely; and
 - (b) Give an outline of the evidence on which the disputant intends to rely; and
 - (c) Give an outline of the issues that the disputant considers will arise; and
 - (d) Specify the propositions of law on which the disputant intends to rely.
- (6B) In subsections (4)(b) and (6)(b), **evidence** refers to the available documentary evidence on which the person intends to rely, but does not include a list of potential witnesses, whether or not identified by name.
- (7) A disputant who does not issue a statement of position in the prescribed form within the response period for the statement of position, is treated as follows:
 - (a) if the Commissioner has proposed the adjustment to the assessment, the disputant is treated as having accepted the Commissioner's notice of proposed adjustment or statement of position:
 - (b) if the disputant has proposed the adjustment to the assessment, the disputant is treated as not having issued a notice of proposed adjustment.
- (8) The Commissioner—
 - (a) May, within the response period for a disputant's statement of position, provide the disputant with additional information in response to the disputant's statement of position; and

- (b) Must provide the additional information as far as possible in the manner required by subsection (4).
- (9) The additional information provided by the Commissioner under subsection (8) is deemed to form part of the Commissioner's statement of position.
- (10) The Commissioner may apply to the High Court for more time to reply to a disputant's statement of position if—
 - (a) The Commissioner applies before the expiry of the response period for the disputant's statement of position; and
 - (b) The Commissioner considers it is unreasonable to reply to the disputant's statement of position within the response period, because of the number or complexity or novelty of matters raised in the disputant's statement of position.
- (11) The disputant may apply to the High Court for more time within which to reply to the Commissioner's statement of position if—
 - (a) The disputant applies before the expiry of the response period for the Commissioner's statement of position; and
 - (b) The disputant considers it unreasonable to reply to the Commissioner's statement of position within the response period, because the issues in dispute had not previously been discussed between the Commissioner and the disputant.
- (12) The High Court shall, in considering an application under subsection (11), have regard to the provisions of section 89A and the conduct of the parties to the dispute.
- (13) The Commissioner and a disputant may agree to additional information being added, at any time, to either of their statements of position.
- (14) The additional information provided by the Commissioner or a disputant under subsection (13) is deemed to form part of the provider's statement of position.

89N Completing the disputes process

- (1) This section applies if—
 - (a) a notice of proposed adjustment has been issued; and
 - (b) the dispute has not been resolved by agreement between the Commissioner and the disputant; and
 - (c) none of the following applies:
 - (i) the Commissioner notifies the disputant that, in the Commissioner's opinion, the disputant in the course of the dispute has committed an offence under an Inland Revenue Act that has had an effect of delaying the completion of the disputes process:
 - (ii) the Commissioner has reasonable grounds to believe that the disputant

may take steps in relation to the existence or location of the disputant's assets to avoid or delay the collection of tax from the disputant:

- (iii) the Commissioner has reasonable grounds to believe that a person who is, under the 1988 version provisions in subpart YB of the Income Tax Act 2007, an associated person of the disputant may take steps in relation to the existence or location of the disputant's assets to avoid or delay the collection of tax from the disputant:
 - (iv) the disputant has begun judicial review proceedings in relation to the dispute:
 - (v) a person who is, under the 1988 version provisions in subpart YB of the Income Tax Act 2007, an associated person of the disputant and is involved in another dispute with the Commissioner involving similar issues has begun judicial review proceedings in relation to the other dispute:
 - (vi) during the disputes process, the disputant receives from the Commissioner a requirement under a statute to produce information relating to the dispute and fails to comply with the requirement within a period that is specified in the requirement:
 - (vii) the disputant elects under section 89E to have the dispute heard by a Taxation Review Authority acting in its small claims jurisdiction:
 - (viii) the disputant and the Commissioner agree in writing that they have reached a position in which the dispute would be resolved more efficiently by being submitted to the court or Taxation Review Authority without completion of the disputes process:
 - (ix) the disputant and the Commissioner agree in writing to suspend proceedings in the dispute pending a decision in a test case referred to in section 89O.
- (2) If this section applies, the Commissioner may not amend an assessment under section 113 before one of the following occurs:
- (a) the Commissioner or the disputant accepts a notice of proposed adjustment, notice of response, or statement of position issued by the other:
 - (b) the Commissioner considers a statement of position issued by the disputant.
- (3) Despite subsection (2), the Commissioner may apply to the High Court for an order that allows more time for the completion of the disputes process, or for an order that completion of the disputes process is not required.
- (4) The Commissioner must make an application under subsection (3) within the period of time during which the Commissioner would otherwise be required, under the Inland Revenue Acts, to make an amended assessment.
- (5) If the Commissioner makes an application under subsection (3), the Commissioner must make an amended assessment by the last day of the period that—

- (a) begins on the day following the day by which the Commissioner, in the absence of the suspension, would be required under the Inland Revenue Acts to make the amended assessment; and
- (b) contains the total of—
 - (i) the number of days between the date on which the Commissioner files the application in the High Court and the earliest date on which the application is decided by the High Court or the application or dispute is resolved;
 - (ii) the number of days allowed by an order of a court as a result of the application.

109 Disputable decisions deemed correct except in proceedings

Except in objection proceedings under Part 8 or a challenge under Part 8A,—

- (a) No disputable decision may be disputed in a court or in any proceedings on any ground whatsoever; and
- (b) Every disputable decision and, where relevant, all of its particulars are deemed to be, and are to be taken as being, correct in all respects.

Compare: 1976 No 65 s 27

113 Commissioner may at any time amend assessments

- (1) Subject to sections 89N and 113D, the Commissioner may from time to time, and at any time, amend an assessment as the Commissioner thinks necessary in order to ensure its correctness, notwithstanding that tax already assessed may have been paid.
- (2) If any such amendment has the effect of imposing any fresh liability or increasing any existing liability, notice of it shall be given by the Commissioner to the taxpayer affected.

Compare: 1976 No 65 s 23

114 Validity of assessments

An assessment made by the Commissioner is not invalidated—

- (a) through a failure to comply with a provision of this Act or another Inland Revenue Act; or
- (b) because the assessment is made wholly or partially in compliance with—
 - (i) a direction or recommendation made by an authorised officer on matters relating to the assessment;
 - (ii) a current policy or practice approved by the Commissioner that is applicable to matters relating to the assessment.

138G Effect of disclosure notice: exclusion of evidence

(1) Unless subsection (2) applies, if the Commissioner issues a disclosure notice to a disputant, and the disputant challenges the disputable decision, the Commissioner and the disputant may raise in the challenge only—

- (a) The facts and evidence, and the issues arising from them; and
- (b) The propositions of law,—

that are disclosed in the Commissioner's statement of position and in the disputant's statement of position.

(2) A hearing authority may, on application by a party to a challenge to a disputable decision, allow the applicant to raise in the challenge new facts and evidence, and new propositions of law, and new issues, if satisfied that—

- (a) The applicant could not, at the time of delivery of the applicant's statement of position, have, with due diligence, discovered those facts or evidence; or discerned those propositions of law or issues; and
- (b) Having regard to the provisions of section 89A and the conduct of the parties, the hearing authority considers that the admission of those facts or evidence or the raising of those propositions of law or issues is necessary to avoid manifest injustice to the Commissioner or the disputant.

(3) For the purposes of subsection (1), a statement of position includes any additional information that the Commissioner and the disputant agree (under section 89M(13)) to add to the statement of position.

138P Powers of hearing authority

(1) On hearing a challenge, a hearing authority may—

- (a) Confirm or cancel or vary an assessment, or reduce the amount of an assessment, or increase the amount of an assessment to the extent to which the Commissioner was able to make an assessment of an increased amount at the time the Commissioner made the assessment to which the challenge relates; or
- (b) Make an assessment which the Commissioner was able to make at the time the Commissioner made the assessment to which the challenge relates, or direct the Commissioner to make such an assessment.

(1B) If a taxpayer brings a challenge and proves, on the balance of probabilities, that the amount of an assessment is excessive by a specific amount, a hearing authority must reduce the taxpayer's assessment by the specific amount.

(2) If the challenge relates to a disputable decision that is not an assessment, the hearing authority—

- (a) Must not make or alter the disputable decision; and
- (b) May direct the Commissioner to alter the disputable decision to the extent necessary to conform to the decision of the hearing authority with the effect the hearing authority specifies.

- (3) Subject to subsection (4), the Commissioner must make or amend an assessment or other disputable decision in such a way that it conforms to the hearing authority's determination.
- (4) The Commissioner is not required to make or amend an assessment or other disputable decision before the resolution of appeal procedures from the hearing authority.
- (5) The time bars in sections 108, 108A, and 108B do not apply with respect to—
 - (a) A determination of a hearing authority made under subsection (1)(a) or subsection (1B) of this section or an amendment made by the Commissioner to an assessment for the purpose of conforming to such a determination; or
 - (b) An assessment made by a hearing authority under subsection (1)(b) of this section or the Commissioner under subsection (3) of this section.