Inland Revenue Department: Managing tax debt

This is an independent assurance report about a performance audit carried out under section 16 of the Public Audit Act 2001.

June 2009

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Although most taxpayers pay their tax on time, the Inland Revenue Department (Inland Revenue) acknowledges that tax debt is growing at a rate that is outpacing Inland Revenue’s capacity to deal with it. As at 30 June 2008, there were 202,000 cases of tax debt, totalling $4.036 billion.

Inland Revenue has estimated that total tax debt could more than double within five years unless it takes a different approach to managing the debt.

Inland Revenue is aware of the challenges it faces, and is updating its tax debt strategy to respond to these challenges. It is proposing to better understand taxpayers, provide taxpayers with improved online tools, and pilot new approaches designed to enhance its processes for collecting tax debt.

My staff looked at how Inland Revenue manages its tax debt collection role. They examined whether Inland Revenue was taking a strategic approach to debt management, effectively identifying and recovering debt, and adequately monitoring and reporting its performance in managing tax debt. Although Inland Revenue’s management of tax debt was satisfactory once debt cases were assigned to its debt officers, I agree with Inland Revenue that its overall approach to tax debt management is insufficient to control the growth in tax debt.

Inland Revenue has a responsibility to maximise the amount of revenue collected while having regard to the resources available, maintaining the integrity of the tax system (promotion of tax compliance), and the costs to taxpayers. By integrity of the tax system, I mean that taxpayers are all treated – and are seen to be treated – in the same way, consistently and fairly. Maintaining confidence in the integrity of the system is essential for any area of regulation that depends on voluntary compliance.

Because Inland Revenue prioritises what its debt officers work on, some tax debt cases regarded by Inland Revenue as lower risk are unlikely to be assigned to a debt officer. Although these may be subject to ongoing automated actions, not assigning certain types of cases to a debt officer may pose a risk to the integrity of the tax system. In my view, Inland Revenue needs to review how it assesses risk when selecting tax debt cases for further enforcement action. This is in order to enforce all kinds of tax obligations and to maintain public confidence that non-compliance is effectively deterred for all types of taxpayer.

Inland Revenue has limited information to monitor the effectiveness and efficiency of its tax debt collection work. Inland Revenue was aware of how many tax debt cases it needs to manage, but it was not able to tell my staff how many tax debt cases it was actively managing. In my view, such information is fundamental to Inland Revenue effectively and efficiently deploying its debt.
collection resources, demonstrating its performance in collecting tax debt, and having informed discussions with the Government about options for collecting tax debt.

For Inland Revenue to produce a new strategy, to manage the growth of tax debt in a timely, effective, and efficient way, it will need better information about the effectiveness and efficiency of its debt collection techniques. The five recommendations I have made involve Inland Revenue improving the information that it collects, uses, and reports.

Inland Revenue has told me that the capabilities of its debt management information system limit the extent to which it can achieve two of my recommendations. My staff have not carried out a detailed assessment of this issue because they did not perform a detailed information systems audit. I am of the view that the information referred to in my recommendations is fundamental to the effective and efficient management of tax debt.

It is important that Inland Revenue is effectively and efficiently managing tax debt at any time – but even more so given the current economic climate and the pressure that the Crown faces with forecast deficits. It is also important that Inland Revenue moves quickly to implement its proposed new tax debt strategy to make best use of its available resources.

I thank the staff of Inland Revenue and others for providing my Office with a high level of assistance and co-operation during the performance audit.

K B Brady
Controller and Auditor-General

16 June 2009
Our recommendations

To control the growth of tax debt, Inland Revenue will need better information about the effectiveness and efficiency of its debt collection techniques. For this reason, these five recommendations involve Inland Revenue improving the information that it collects, uses, and reports.

We recommend that the Inland Revenue Department:

1. collect and analyse information about how many cases debt officers are managing, and how much of their work is inbound contact (where first contact is from a taxpayer contacting Inland Revenue) and how much is outbound (where Inland Revenue debt officers make first contact);

2. review how it selects the types of cases it does – and does not – allocate to debt officers, to ensure that it is:
   • taking reasonable steps to enforce taxpayers’ obligations; and
   • considering the potential effect on voluntary compliance if some types of cases are unlikely to be assigned to a debt officer;

3. include in its external reporting the total number of outstanding tax debt cases (by the age of tax debt) and the methods used to resolve tax debt cases;

4. improve the information used to monitor the effectiveness and efficiency of its tax debt collection work and to prepare its tax debt strategy; and

5. closely align its internal and external tax debt reporting.
Part 1
Introduction

1.1 For most New Zealanders, paying tax is a part of life. In 2007/08, there were about 6.5 million taxpayers (individuals, companies, trusts, and other entities), who paid the Inland Revenue Department (Inland Revenue) a total of $51.2 billion.

1.2 The tax system is based largely on voluntary compliance, and most taxpayers (86% in 2007) pay their taxes on time. However, some taxpayers do not meet their tax obligations. As at 30 June 2008, there were 202,000 cases of outstanding tax debt,\(^1\) totalling $4.036 billion. Of this, $2.216 billion was considered to be collectable debt\(^2\) and $1.820 billion was considered to be non-collectable debt.\(^3\)

1.3 In the context of this report, “tax debt” refers to amounts owing for income tax in its various forms (mainly that payable by individuals and companies) and goods and services tax.

1.4 About $1.606 billion (40%) of the total tax debt (as at 30 June 2008) is made up of penalties and interest. Legislation requires Inland Revenue to charge interest on a taxpayer’s outstanding debt, but under certain circumstances Inland Revenue can remit interest and penalties. These circumstances include serious hardship, if the maximum amount of debt has been recovered, or it is inefficient for Inland Revenue to continue chasing the debt.

1.5 Between 2004 and 2008, the total tax base grew by 35%, but total tax debt increased by 91% ($1.92 billion). This indicates that Inland Revenue’s collection practices are not keeping pace with tax debt. For the 2007/08 year, Inland Revenue had 428 staff doing tax debt work (and similar numbers for the two years before that).

1.6 Inland Revenue acknowledges that the growth in tax debt is outpacing its capacity for dealing with the debt, and is putting pressure on organisational resources. Inland Revenue has told us that it believes society’s attitude towards debt has led to a growth of both household debt and personal debt in New Zealand. It believes that this has also contributed to the growth in tax debt. Inland Revenue told us that its active targeting of large-value non-compliant taxpayers for auditing has also contributed to the rising debt trend by identifying more tax due.

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1 “Outstanding tax debt” is tax debt that has not been paid by its due date.

2 “Collectable debt” is tax debt that Inland Revenue reasonably expects to collect. It includes debt being repaid in instalments, and cases where collection action is pending.

3 “Non-collectable debt” is tax debt that cannot currently be collected. It includes Inland Revenue’s assessment of debt when a taxpayer fails to file a return (default assessments), and debt owing that is under investigation or dispute (deferred debt). It also includes debt owing that is subject to bankruptcy, liquidation, or receivership action, and debt to be written off. Some non-collectable debt can become collectable after disputes or returns are finalised.
1.7 Inland Revenue has predicted that tax debt could more than double within five years, unless it “takes a fresh approach” to managing debt (see Figure 1).

**Figure 1**

*Actual and projected increases in tax debt, 2004-2012*

![Graph showing the increase in tax debt from 2004 to 2012.](Source: Inland Revenue)

**Why and how we carried out our audit**

1.8 Because the amount of outstanding tax debt is significant and growing, we carried out a performance audit to provide assurance to Parliament that Inland Revenue was effectively and efficiently managing tax debt. Our audit examined whether Inland Revenue is:

- taking a strategic approach to tax debt management (Part 2);
- effectively identifying and recovering debt through its automated actions and debt officers (Part 3); and
- adequately monitoring and reporting its performance (Part 4).

1.9 We expected Inland Revenue, in taking a strategic approach, to:

- have strategies to manage the effects of the growth in tax debt (to the extent that these are within Inland Revenue’s influence); and
- manage tax debt cases consistently throughout the country.

1.10 We expected Inland Revenue, in effectively identifying and recovering tax debt, to:

- have processes to ensure that older tax debt cases are actively managed so that the debt is recovered; and
have debt staff who are well trained and well supported in their decision-making.

1.11 In terms of adequately monitoring and reporting its performance, we expected Inland Revenue to:

- analyse the success of each of its methods used to recover tax debt and enforce compliance;
- regularly monitor and report trends in tax debt; and
- have all information required for monitoring and reporting readily available.

How we carried out our audit

1.12 We requested and reviewed a wide range of documents and reports, both public and internal. We watched demonstrations of computer systems, and reviewed 40 randomly selected tax debt cases from a range of taxpayers. We interviewed 30 Inland Revenue staff in four different cities. We also met with relevant external organisations to get their views on how Inland Revenue is managing tax debt.

Outside the scope of our audit

1.13 We did not assess:

- the efficiency of debt information systems;
- the accuracy of data in the debt information systems; or
- Inland Revenue’s management of debt that was not tax debt.4

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4 The non-tax debt comprises Child Support debt, Working for Families Tax Credit debt, and overdue student loan repayments.
2.1 In this Part, we set out our findings about Inland Revenue’s:
   • national tax compliance strategy;
   • encouragement of prompt payment of taxes;
   • devising of new tax debt collection techniques; and
   • updating of its tax debt strategy.

2.2 Overall, Inland Revenue has a sensible tax compliance strategy in place, and its compliance model clearly drives that strategy. Inland Revenue is well aware of the challenges it faces, and is addressing those challenges by updating its tax debt strategy.

National tax compliance strategy

Inland Revenue has a comprehensive national compliance strategy guiding its approach to managing tax debt.

2.3 Inland Revenue’s compliance strategy is based on voluntary compliance. Inland Revenue begins by trying to make it easy for people to comply, by informing taxpayers of their obligations, and providing a mix of services to support payment. When a taxpayer does not meet their tax obligations, Inland Revenue can encourage and enforce compliance by a range of measures.

2.4 Inland Revenue’s compliance model shows how taxpayer attitudes about compliance relate to the actions Inland Revenue uses to encourage or enforce compliance (see Figure 2). Figure 2 shows, for example, that Inland Revenue tries to make it easy for taxpayers who are “Willing to do the right thing”.

2.5 The actions taken by Inland Revenue to collect tax debt clearly align with its compliance model. It uses both automated and manual methods to encourage compliance. Automated actions begin with a warning letter. All types of taxpayers receive these letters. If there is no response, and the tax owed is below a predetermined threshold, a deduction order is issued to the employer. If ongoing automated actions fail to secure payment, the case needs to be assigned to a debt officer for further action.

2.6 Inland Revenue takes a nationwide approach, allocating tax debt cases to debt officers based on the type of debt or the risk of the debt (not the geographic location of the debtor). The exception to this is when legal action is likely to require a court appearance; these cases are allocated to an Inland Revenue office close to the Court.
2.7 Inland Revenue’s organisational structure (see the Appendix) aligns broadly with the compliance model:

- At the “Make it easy” stage (see Figure 2), a group within Inland Revenue assists with the design of systems to encourage taxpayer compliance.

- The “Assist to comply” stage of the model relates to the automated actions of Inland Revenue’s computer systems, and handling of incoming calls when a taxpayer needs assistance.

- Of those taxpayers in the “Don’t want to comply” and “Have decided not to comply” stages, some cases are assigned to a debt officer in either the Receivables group or the National Collections Enforcement (NCE) group for further action. (Further information about these two groups, including how they fit into Inland Revenue’s organisation structure, is in the Appendix).

**Figure 2**
Inland Revenue’s compliance model for collecting tax

Encouraging prompt payment of taxes

Encouraging taxpayers to comply voluntarily is an important part of Inland Revenue’s compliance model. In 2007, 86% of taxpayers met their obligations on time. The proportion of taxpayers paying on time has remained largely the same during the past five years. Promoting and supporting compliance is seen as an increasingly important part of Inland Revenue’s tax compliance strategy.

Some staff and external organisations consulted have pointed out that the compounding nature of penalties and interest can act as a disincentive to pay current or future taxes if the tax debtor believes that they cannot ever catch up. Inland Revenue is aware of this issue and is planning to better understand the point at which penalties and interest influence compliance.

We encourage Inland Revenue to continue refining its systems for encouraging taxpayers to promptly pay taxes, and to better understand the effect that penalties and interest may have on compliance. Inland Revenue has told us that it agrees this is an activity that should be encouraged.

Devising new tax debt collection techniques

Inland Revenue is devising new tax debt collection techniques to encourage compliance and improve its effectiveness at collecting debt.

Inland Revenue is devising new ways to detect taxpayers who are not complying with their obligations. Inland Revenue is also looking at best practice from overseas agencies, as a way of refining its own debt collection techniques.

Inland Revenue has teams of experienced staff who manage complex debt (complex debt teams). One of their roles is to devise new recovery techniques. If these techniques prove to be effective in collecting tax debt or promoting compliance, they are adopted by the wider organisation. Complex debt teams also deal with the more difficult debt cases, often involving taxpayers who have decided not to comply.

Introducing any new debt collection techniques requires a balancing of costs and benefits, including protection of the integrity of the tax system. Inland Revenue is aware that, for some new techniques, the costs (such as legal costs) may exceed the tax collected, at least initially. Inland Revenue considers costs, benefits, and protecting the integrity of the tax system when deciding whether to proceed with an action. If Inland Revenue does go ahead with an action that costs more than
the amount recovered, it will have determined that the cost is offset by the new knowledge that can lead to new collection approaches. Or it will have determined that the cost is outweighed by the need to protect the integrity of the tax system.

2.14 Inland Revenue is aware that overseas best practice could be useful in New Zealand. For example, Inland Revenue staff and documents note a need to have more sophisticated tools to assess the risk associated with individual taxpayers, and to increase the number of calls made to tax debtors to discuss their debt (outbound calling). These proposals align with best practice material produced by the Organisation for Economic Co-operation and Development (OECD), which emphasises early intervention and outbound calling.²

2.15 In our view, outbound calling and improved risk assessment can potentially generate a good return on investment, and we encourage Inland Revenue to acquire a good understanding of the likely costs and benefits of adopting these changes. Inland Revenue has told us that it agrees with this comment.

## Updating tax debt strategy

Inland Revenue is responding to debt growth by updating its national approach to tax debt collection.

2.16 Inland Revenue is updating its national approach to debt collection, as a part of preparing a new tax debt strategy.

2.17 Inland Revenue’s new tax debt strategy identifies challenges posed by an increasing number of tax debtors, systems that do not support the type of work it wants to do, and taxpayers who are less concerned about being in debt.

2.18 To address these challenges, Inland Revenue is proposing to better understand taxpayers, provide taxpayers with improved online tools, and pilot new tools designed to enhance tax debt collection processes.

2.19 The approach Inland Revenue is taking with its new tax debt strategy aligns well with many of our observations and findings. We encourage Inland Revenue to continue refining its new tax debt strategy and pilot the new debt collection approaches mentioned in that strategy.

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Part 3
Identifying and recovering tax debt

3.1 In this Part, we set out our findings about how Inland Revenue:
• uses information systems to identify tax debt;
• uses automated actions to collect tax debt;
• allocates cases to debt officers;
• trains debt officers;
• uses a range of collection techniques; and
• uses information systems to support its debt officers.

3.2 Overall, Inland Revenue successfully collects about half of the total tax debt through automated actions such as reminder letters. When these actions do not achieve payment of tax debt, the next stage is to assign a case to a debt officer. In our view, once debt cases are assigned to a debt officer, Inland Revenue’s management of tax debt is satisfactory. However, Inland Revenue has more tax debt cases than its staff can actively manage using its current approach. As a consequence, some lower-risk cases are unlikely to be assigned to a debt officer.

3.3 In our view, Inland Revenue needs to review how it assesses risk when selecting tax debt cases for further enforcement action, to ensure that all types of cases are treated fairly and consistently.

3.4 Inland Revenue can also improve the management information it collects to monitor the cost-effectiveness of the various techniques it uses to collect tax debt.

3.5 Inland Revenue wants to improve its tax debt system but does not know, with any certainty, what savings it might make or the additional revenue that it might collect by doing so. In our view, this information is important in any business case for a new computer system that Inland Revenue puts to the Government.

Debt identification

Inland Revenue’s debt management system identifies debt appropriately.

3.6 Inland Revenue’s debt management system recognises a debt:
• when a return is filed but the payment was not made on time;
• when an expected return is not filed (this can result in a default assessment being made, creating a tax debt); and
• when a tax debt has been identified by an audit.

3.7 Sometimes, Inland Revenue may not be aware of a taxpayer’s obligations because the taxpayer has not filed a return before. In this situation, the debt would have to
be identified through an audit or an investigation, or by the taxpayer filing a tax return.

3.8 Although Inland Revenue’s debt management system may identify that a tax debt exists, the amount identified may not be accurate. Additional information provided by a taxpayer or debt officer can change the amount of outstanding tax debt. During our audit, we saw how Inland Revenue updates its records when additional information becomes available.

Automated actions to collect debt

Automated actions account for about half of the tax debt collected by Inland Revenue.

3.9 Once a tax debt is identified, automated actions account for about half of the debt collected by Inland Revenue. These actions usually happen during the first 90 days after the debt becomes outstanding.

3.10 For all types of taxpayers, automated actions begin with a warning letter being sent.

3.11 There are additional actions that apply to salary and wage earners. For these taxpayers, if there is no response and the tax owed is below a predetermined threshold, a deduction order is issued to the employer.

3.12 After those actions and if the debt remains unpaid, tax debtors receive a regular statement of their account that shows their total debt (including any penalties and interest that have accrued). Further action occurs only if the case is assigned to a debt officer or if the taxpayer contacts Inland Revenue.

3.13 Inland Revenue’s automated systems do not differentiate between taxpayers based on their payment history, current behaviour, or compliance risk. Inland Revenue has told us that a more flexible range of automated actions, based on a wider range of information about taxpayers, would help it better collect tax debt. Inland Revenue expects that a wider range of automated actions will be part of the functionality required from future information systems.

3.14 These views about automated recovery action as are in keeping with those of the OECD Forum on Tax Administration, which notes that some countries are creating and using automated risk-profiling techniques. Further, an OECD Forum paper\(^1\) says that predicative modelling (which is more widely used in the private sector) is helpful in establishing the best way to collect certain types of debt. Inland Revenue considers this modelling to have a potentially significant role in tax collection.

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3.15 As automated risk-profiling by overseas tax agencies continues to be established and used, we encourage Inland Revenue to closely monitor whether such risk-profiling does lead to improved compliance with tax payment obligations.

**Allocating cases to debt officers**

Inland Revenue has more debt cases than its staff can actively manage, so it must prioritise which tax debts to pursue. It can improve the information it collects about the types of cases its debt officers are managing and how many cases are being actively pursued.

3.16 Inland Revenue does not have enough debt officers to actively manage all the debt cases it has. As at June 2008, of the 202,000 outstanding tax debt cases, about 70,000 were more that six months old and about 49,000 were more than one year old.

3.17 For the 2007/08 year, Inland Revenue had 428 staff doing tax debt work (and similar numbers for the two years before that). Debt officers are involved in both outbound work (when they are actively seeking to recover a debt) and inbound work (when they are responding to a taxpayer-initiated contact). Their role also includes pursuing taxpayers to file a return if the taxpayers have not yet done so.

3.18 Tax debtors paying debts on their own initiative will resolve some of the outstanding cases. Other tax debtors will contact Inland Revenue to resolve their debts. Unresolved cases need to be assigned to a debt officer. Because Inland Revenue can assign only a portion of its debt cases to officers at any one time, some debt cases will effectively be set aside (although penalties and interest continue to be incurred), until a taxpayer settles the debt or Inland Revenue is able to assign the case to a debt officer.

3.19 Inland Revenue was unable to provide us with information about how many debt cases were actively managed by debt officers and what proportion of debt officers’ work was inbound or outbound. We expected Inland Revenue to have this information. This is because we consider it to be an important part of any informed discussions about staffing levels, and in helping Inland Revenue to allocate resources effectively and efficiently.

**Recommendation 1**

We recommend that the Inland Revenue Department collect and analyse information about how many cases debt officers are managing, and how much of their work is inbound contact (where first contact is from a taxpayer contacting Inland Revenue) and how much is outbound (where Inland Revenue debt officers make first contact).
3.20 Inland Revenue has told us that it understands the opportunity costs and benefits that it would gain from the type of information referred to in this recommendation. It has also told us that its current debt management system limits its ability to distinguish this information, and that manually assembling the information would not be the best use of the limited resources available to it.

Debt cases assigned to officers using a model based on risk

3.21 Depending on the nature and type of the tax debt, Inland Revenue has several processes for allocating to debt officers the cases that require manual intervention. Some cases are immediately assigned to debt officers, such as Audit Assessed Debt, which is debt identified by an investigation or audit. Cases involving large amounts of tax debt are usually allocated to the NCE group.

3.22 Apart from some minor exceptions, the rest of Inland Revenue's case allocation processes rely on a risk-modelling system. The risk model uses a range of information about a taxpayer. The information is used to assign a score to the debt case. The greater the score, the more likely it is that a case will be assigned to a debt officer. Cases with lower-risk scores are less likely to be assigned to debt officers.

3.23 However, Inland Revenue does not ignore cases with low scores. All taxpayers are subject to the automated actions discussed in paragraphs 3.9-3.11. A taxpayer will continue to receive statements showing the total debt including any penalties and interest. This alone can be enough to encourage some taxpayers to resolve the debt. Also, because the risk score grows as the debt grows, the probability of a case being assigned to a debt officer increases with time.

3.24 Although Inland Revenue has a risk-based system for allocating cases to debt officers, it keeps limited records of the cases it allocates. This makes it difficult to review the overall characteristics of the types of cases that Inland Revenue is pursuing, and those that it is not.

3.25 Government agencies have a responsibility to enforce the whole of the area of law they are administering, although they can prioritise their efforts. In our view, collecting and analysing information on the types of cases that Inland Revenue is pursuing (and those it is choosing not to actively pursue) would help it ensure that it is not leaving some types of tax debt unenforced.

3.26 As we discuss later, better information about the cases that are being actively pursued – and those that are not – would also help Inland Revenue to assess the likely costs and benefits of any proposed changes to its tax debt strategy and processes. Inland Revenue has told us that its debt management system limits its ability to obtain the information that we have identified as being important.
3.27 Inland Revenue needs to balance maintaining the integrity of the tax system against the collection of revenue. Inland Revenue needs to ensure that the public remains confident that taxpayers are treated consistently and that all types of debt may be assigned to a debt officer.

3.28 In our view, Inland Revenue’s approach raises a risk that certain types of tax debt cases are unlikely to be assigned to a debt officer for further action. Not actively targeting certain types of tax debt can lead to a perception of unequal treatment and jeopardise public confidence in, and compliance with, the tax system.

Recommendation 2
We recommend that the Inland Revenue Department review how it selects the types of cases it does – and does not – allocate to debt officers, to ensure that it is:

- taking reasonable steps to enforce taxpayers’ obligations; and
- considering the potential effect on voluntary compliance if some types of cases are unlikely to be assigned to a debt officer.

3.29 Inland Revenue has told us that it supports this recommendation. It has noted that it has activities under way as part of its ongoing debt management improvement work that will enable it to act on the recommendation.

Debt officer training and development
Debt officer training and development is well structured and supports the work of debt officers.

3.30 Debt case management requires the debt officer to exercise considerable judgement. In particular, applying the financial relief and hardship provisions in The Taxation (Relief, Refunds and Miscellaneous Provisions) Act 2002 requires debt officers to exercise discretion but do so in a consistent way.

3.31 Inland Revenue uses a mix of formal training and mentoring to ensure that its debt officers are supported in their work. Inland Revenue has a framework setting out the nature and timing of training needed by all debt officers. A debt officer’s training starts at induction, and continues throughout their time at Inland Revenue. For some, this may lead to specialising in complex debt work.

3.32 The framework links the completion of formal Acquisition of Skills Programme for Inland Revenue Employees (ASPIRE) training packages to increasing levels of competency. Completing ASPIRE packages requires the debt officer to demonstrate their knowledge and understanding of the training, and for this to be confirmed by their team leader.
3.33 The NCE group is expanding its formal training through its Advancing the Collection of Returns and Debt (ACORD) programme. This includes training in advanced debt management techniques.

3.34 Debt officers we spoke to were aware of, and spoke positively about, training and development opportunities. As well as training packages requiring staff to carry out formal training and then demonstrate those skills, Inland Revenue has online reference materials to guide debt officers through a range of debt collection actions. Inland Revenue uses project work as opportunities for staff to diversify their skills.

3.35 We consider that Inland Revenue’s framework for staff training and development is appropriate and adequate.

### Collection techniques supporting debt officers

**Debt officers have access to an escalating range of collection techniques.**

3.36 Inland Revenue’s debt manual offers an escalating range of collection techniques that debt officers can use to collect a debt. Techniques include, but are not limited to:

- issuing a deduction notice against a taxpayer’s bank accounts;
- calling the taxpayer to establish an arrangement;
- writing off the debt in part or in full; and
- legal remedies, such as liquidation.

3.37 None of the debt cases we examined during our review had stalled because existing collection techniques were in some way inadequate. Debt officers we spoke with did not raise any shortcomings with the collection techniques they have available to them.

3.38 Overall, we are of the view that the collection techniques available are able to support debt officers’ work, and escalate in line with Inland Revenue’s compliance model.
Information systems supporting debt officers

Debt officers have a debt management system to help them manage cases. However, the system could better support staff.

3.39 Inland Revenue has a debt management system that allows debt officers to access account details, contact information, and a history of actions taken for individual taxpayers. Debt officers and team leaders use a separate tool to monitor the timeliness of their casework.

3.40 We observed demonstrations of Inland Revenue’s debt management system that showed the range of a taxpayer’s information that is available to debt officers. We also saw parts of Inland Revenue’s debt management system that could be improved to provide staff with better support.

3.41 Two examples where improved system capabilities could better support staff are:
   - monitoring of instalment arrangements to ensure that prompt follow-up occurs if these arrangements are defaulted on (currently, a debt officer has to do this manually); and
   - electronically storing and managing correspondence (currently, debt officers must manually enter correspondence into the debt management system).

3.42 Also, Inland Revenue told us that significant transaction costs can arise from using the existing systems to carry out collection actions, such as calculating and sending a statement to a taxpayer. We have not audited these transaction costs, and Inland Revenue has not quantified them.

3.43 Inland Revenue has begun putting together a business case for a new computer system. As part of this business case, Inland Revenue will need to accurately assess any efficiency and capability gains of a new system against its purchase and set-up costs. We consider this assessment to be an important part of any sound business case presented to the Government.
Part 4
Performance reporting

4.1 In this Part, we set out our findings about Inland Revenue’s:
- external tax debt reporting;
- internal tax debt reporting; and
- consistency of external and internal reporting.

4.2 In 2008, the Auditor-General observed that:

A core purpose of performance reporting is to provide for public accountability for the responsible use of public resources and regulatory powers, including demonstrating that public services are being delivered effectively and efficiently. Entities can be truly accountable only if they are transparent about both their financial and non-financial performance and the relationship between the two.¹

4.3 We examined Inland Revenue’s reporting of its performance in managing tax debt, and found that its external and internal reporting could be improved. We consider these improvements would provide for better transparency, as well as help Inland Revenue better understand how to improve its tax debt performance.

External reporting of tax debt
Inland Revenue’s external performance reporting provides only a partial view of its performance in managing overall tax debt.

4.4 For the 2007/08 financial year, Inland Revenue’s external performance standards were to:
- ensure that the number of new debt cases was less than 575,000;
- ensure that at least 95% of all work was completed in a correct, complete, clear, timely, and appropriately referenced manner that also showed an understanding of the environment;
- resolve 500,000 to 550,000 debt cases by the end of the financial year; and
- resolve at least 85% of all new debt cases within 12 months of the due date for payment.

4.5 Inland Revenue’s external performance standards focus on the number of new debt cases and the resolution of tax debt cases. Inland Revenue’s 2008 annual report includes this information as well as information on the amount of outstanding tax debt and outstanding tax debt analysed by tax type. Inland Revenue’s annual reports state the total amount of outstanding tax debt.

4.6 Inland Revenue’s 2008 annual report does not contain information about the total number or age of debt cases that Inland Revenue has to manage. Highlighting trends in the number of unresolved cases would indicate whether Inland Revenue...

¹ The Auditor-General’s observations on the quality of performance reporting, page 4.
is keeping the overall number of debt cases under control. Highlighting trends in the age of tax debt cases would also indicate whether Inland Revenue is keeping debt growth under control.

4.7 We note that Inland Revenue’s internal reporting does record the age of debt and the total number of debt cases it is managing. In our view, this is useful information for Parliament and the public that Inland Revenue should report externally.

4.8 Inland Revenue reports on how many debt cases it resolves in a year, but does not note how those cases are resolved. Tax debts may be resolved by a variety of methods, some of which include:

- taxpayers contacting Inland Revenue to work out a debt;
- taxpayers paying in response to automated actions;
- Inland Revenue taking manual measures to actively collect a debt; and
- Inland Revenue resolving debts by account maintenance (that is, correcting inaccurate information in Inland Revenue’s system that has given rise to debt that does not actually exist).

4.9 In our view, aggregating these as “Cases resolved by Inland Revenue” fails to give a clear view of the results of Inland Revenue’s active debt management work.

**Recommendation 3**

We recommend that the Inland Revenue Department include in its external reporting the total number of outstanding tax debt cases (by the age of tax debt) and the methods used to resolve tax debt cases.

4.10 Inland Revenue has acknowledged that this type of information would enhance its external reporting, and is already reported in its existing internal management information.

4.11 Inland Review has also told us that its debt management system limits its ability to report on the actual methods it uses to resolve debt cases. Our view is that this information is critical to selecting the most effective and efficient set of actions for managing tax debt within the available resources.
Internal reporting of tax debt

Variations in Inland Revenue's internal performance reporting make it difficult to monitor the effectiveness and efficiency of its tax debt collection activities.

4.12 Inland Revenue uses a set of internal performance standards to monitor tax debt collection. Performance standards vary between the NCE group and the Receivables group, based on the responsibilities of each group. Receivables sections are each given a particular type of debt to focus on. Reporting within the Receivables group is less detailed than within the NCE group, and this makes it difficult to compare the effectiveness and efficiency of the different sections within the Receivables group. In our view, more comprehensive performance monitoring would help Inland Revenue to monitor the performance of the Receivables group, the sections within it, and the usefulness of the different work streams.

4.13 The types of cases that the NCE group focuses on are well defined. The NCE group's regular internal performance reports align well to its responsibilities, and provide an effective view of its performance. It produces performance reports for each manager's area of responsibility that provide an overview of how a manager's staff collectively perform.

4.14 Reporting varies because the Receivables group deals with a wider range of debt cases and is involved in more reactive work, responding to inbound telephone calls from taxpayers. This makes reporting more difficult.

4.15 We consider that Inland Revenue could expand its internal reporting to better monitor the effectiveness and efficiency of its different debt teams, and the approaches they are using to resolve tax debt cases.

4.16 Expanded internal reporting would help Inland Revenue to better monitor its ongoing activities, identify where efficiencies could be made, and help it to have more specific discussions with the Government about the level and kind of resources needed to collect any given amount of tax debt. Having a good understanding of the effectiveness and efficiency of the techniques it uses to collect tax debt is also important for Inland Revenue as it prepares its new tax debt strategy.

Recommendation 4
We recommend that the Inland Revenue Department improve the information used to monitor the effectiveness and efficiency of its tax debt collection work and to prepare its tax debt strategy.
4.17 Inland Revenue has told us that it supports this recommendation. It has noted that the proposed changes to its tax debt strategy will facilitate its ability to monitor the effectiveness of its debt collection activities. We have not audited these proposed changes.

Consistency of reporting
Inland Revenue’s external and internal reports could be more consistent.

4.18 Inland Revenue’s 2008 annual report explains that debt is increasing because of external pressures and that Inland Revenue is improving its efficiency in collecting debt. No other challenges are noted in the Debt Portfolio section of the annual report.

4.19 In contrast, Inland Revenue’s internal reports cite a wider range of challenges that it is facing in managing its debt portfolio. Although we do not expect Inland Revenue to report everything externally that it reports internally, we expect Inland Revenue to more clearly note some of these challenges in external reports. For example, Inland Revenue’s internal reports note that it needs to change its approach to keep up with rising debt. We would expect to see this clearly stated in external reports.

4.20 We expect that what is reported internally and externally will vary to accommodate the needs of different audiences. However, we also expect Inland Revenue to present essentially the same high-level information in both kinds of reports.

Recommendation 5
We recommend that the Inland Revenue Department closely align its internal and external tax debt reporting.

4.21 Inland Revenue has told us that it agrees with this recommendation and that its staff involved with debt management will be working with other parts of Inland Revenue to ensure that internal and external reporting are more closely aligned.
Appendix

Inland Revenue Department's organisation structure for managing tax debt

Tax debt is managed by the Assurance and Assistance sections, which are part of the Service Delivery division.

The Assurance section includes the National Collections Enforcement (NCE) group, including the complex debt teams. The NCE group works mainly with tax debtors who are categorised as “Have decided not to comply”.

The Assistance section includes Inland Revenue’s Call Centre and the Receivables group. The Receivables group works with a range of tax debtors, but focuses its efforts on those willing or trying to pay their tax debts.