NEW ZEALAND LAW SOCIETY
NZLS EST 1869

Level 4, 17-21 Whitmore Street, Wellington
DX SP20202, Wellington
PO Box 5041, Wellington 6140, New Zealand

TEL 04 472 7837 · E inquiries@lawsociety.org.nz
www.lawsociety.org.nz

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Graeme Smaill
By email: Graeme@greenwoodroche.com

Dear Graeme

Taxation legislation drafting review – NZLS Tax Law Committee input

Thank you for your invitation for the New Zealand Law Society | Te Kāhui Ture o Aotearoa (Law Society) Tax Law Committee (committee) to engage in relation to the review of the drafting of taxation legislation.

We understand Inland Revenue (IR) has decided it is timely to have a review, having regard to the time that has elapsed since the initial steps were taken in the project for rewriting the Income Tax Act 1976 (the rewrite project). The committee welcomes the review and is grateful for the discussion with you on 10 August. We thought it would be helpful to briefly record below the key issues discussed, to assist with progressing the review.

Executive summary

As you are aware, part of the Law Society's remit is to uphold the rule of law and support clear, workable and accessible legislation.[1] Accordingly, we are very keen to be involved at every stage of the development of tax law.

We have provided preliminary comments below, identified some emerging problems and have recommended some improvements in relation to:

- the locus of tax legislation drafting (IR or Parliamentary Counsel Office)
- inappropriate use of Supplementary Order Papers (SOPs)
- remedials
- constitutional concerns regarding tax policy, drafting, official advisers – lack of separation and independence
- the New Zealand approach – a comparative analysis

We emphasise that our comments are not intended as a criticism of IR officials, who do commendable work responding to fast-paced and complex demands.

Preliminary comments

Many of the issues discussed on 10 August, and summarised below, are inter-linked. The broad thematic concern relates to the tax policy development process and subsequent legislative drafting.

The committee has written recently to IR emphasising the importance of the Generic Tax Policy Process (GTPP) and raising general concerns about the development of tax policy (**annexed** to this letter, for context). The GTPP is designed to provide increased opportunity for public consultation to

[1] Section 65(e), Lawyers and Conveyancers Act 2006.

ensure that tax initiatives and tax law developments are subject to public scrutiny at all stages of development.

Broadly speaking, the committee is concerned that tax legislation is being drafted at pace and with IR Policy working very closely with IR drafters, and a reduced quality of legislation. Currently we see a vast amount of legislation produced each year by a very small team which gets insufficient scrutiny, so there is a lack of opportunity for considered review and comment. We acknowledge the need for a reasonably speedy legislative process, but the appropriate quality checks and independent scrutiny need to be built into the system.

NZLS used to get draft legislation to look at as part of the consultation process, however now it seems standard that select provisions are provided to a limited group on a confidential basis for review by a few people. The wider consultative process seems not to be happening. There are a few examples where tax legislation has been enacted and then found wanting (Kiwisaver legislation in particular has proven not to be fit for purpose). The underlying problem is that IR is a 'one stop shop', catching things on the go.

This leads onto the next point, about the need for greater separation and independence of the tax legislation drafters.

Locus of tax legislation drafting: IR or Parliamentary Counsel

We acknowledge there are some very experienced and informed people at IR. However, the small group of IR officials with relevant tax drafting expertise and experience is an issue.

The Law Society's view, supported by its Tax Law and Rule of Law committees, is that all tax legislation drafting should be done by PCO. The Law Society's recommendation to the Justice select committee in 2018 was that:[2]

> "It also follows … that drafting of primary tax legislation, at least, should be moved back to PCO, as was recommended by the Law Commission.[1] The PCO is a custodian of constitutional standards and uniform drafting practices. It is undesirable in principle for officers of a department to draft legislation under the instructions of the same department, without the important influences of the wider stewardship role that PCO provides.[2]"

That recommendation was not adopted, but it remains relevant and the benefits of such a change should be reconsidered.

Regardless of the locus of tax legislation drafting, a more disciplined and principled process is needed. Best practice should be adopted – options include, for example:

- Internal peer review of drafting (which we understand is standard practice at PCO).
- Independent review, possibly by LDAC – LDAC has previously been involved in looking at sections (it would be useful to have someone looking at tax legislation independently full-time and gathering examples where it isn't working).
- The rewrite advisory panel (or similar mechanism), which the committee has advocated for in the past, could be an extremely useful means of ensuring review by internal IR and external people, mandated with putting out a scorecard on how good the drafting team has been at writing law. The original iteration of the rewrite advisory panel was formed for a different

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2 NZLS submission 23.2.18 on the Legislation Bill, at [5.3]. (Footnotes: [1] NZLC R107, Review of the Statutes Drafting and Compilation Act 1920, at 18-20; [2] As is recognised in clause 127.)

purpose, the way it operated was by triaging issues and putting them out publicly as identified issues – people could comment. The panel was independent, this facilitated early resolution of issues, utilised private sector resources, and identified issues in a non-partisan way.

- IR improved responsiveness to issues identified by externals: a related issue is that as things stand, manifestly reasonable suggestions are being ignored. This is problematic because officials should respond promptly to concerns about legislative inconsistencies.
- Mandatory post-enactment review should be considered. Post-implementation review does not signal a 'failure'; rather it is to be expected that with the pace of reform there are going to have to be tweaks.

Inappropriate use of SOPs

Relatedly, there seems to be an increasing trend toward the use of SOPs late in the tax development process and often without any adequate external scrutiny. The sheer volume and complexity of legislation means there is an over-reliance on supplementary amendments and secondary legislation.

There used to be a presumption against the frequent use of SOPs, whereas now SOPs are used commonly to 'mop up' issues and tack reforms onto bills that are already in front of select committee or in their late stages in the House.

This approach results in law being developed in a piecemeal way, which is problematic. By contrast, PCO develops legislation in a more disciplined and predictable way, requires clear drafting instructions and develops draft legislation at arm's length.

Remedials

There is a burgeoning list of remedials. Martin Smith has spoken at TICAL about the place of remedials, and the importance of getting remedials right. There seem to be 10 really important remedials that are required at any one time, but there are probably 30 or so remedials sitting in the queue; what happens is the 11th or 12th never get seen to – so this is a real problem.

It also appears that 'revenue-friendly' remedials get advanced whereas taxpayer-friendly remedials typically languish. This clearly is undesirable from several perspectives: it creates enduring uncertainty for tax advisers and their clients, and potentially brings the system into disrepute.

We need to move towards a much better use of both public and private sector resources in order to break the logjam of remedials. (The Law Society would not advocate for Henry 8th style clauses to fix the problem.)

The committee considers that the rewrite advisory panel would be a good solution – as noted earlier, the panel (or similar mechanism) would be able to identify and assess issues in a non-partisan way, provide transparency in terms of what remedials are being considered, and be an effective use of private sector resources.

Constitutional concerns: tax policy, drafting, official advisers – lack of separation and independence

There is significant unease about the potential scope for conflicts of interest in current settings.

This was most obvious in the context of the *Roberts* litigation and the advice provided at the time by tax officials to the Finance & Expenditure select committee (FEC),[3] which in the Law Society's view was problematic. The officials' recommendation to FEC to amend section LD 3 raised a number of concerns:

- It is problematic for officials to introduce and recommend amendment at the select committee stage of the legislative process on the basis of "policy intent" without providing evidence of such policy intent, and in the face of a contrary finding by the High Court that at the time stood as authority for the intent behind the provision's enactment.
- The concern was compounded because at the time *Roberts*[4] was on appeal. (Officials should exercise caution in making explicit statements as to original policy intent in circumstances where intent is, or is likely to be, an issue in a live dispute.)
- It was compounded further because officials' description of the policy intent was being used to justify the proposed retrospective application of the proposed amendment.
- If such statements are made, they should be made at the drafting/commentary stage of proposed legislation, so that public submissions can be considered by the select committee.

In short, it is the role of officials advising select committees to provide impartial advice, and not to defend or advance departmental agendas.

The New Zealand approach – a comparative analysis?

In terms of 'NZ Inc.', the opportunity cost of the current system – an inefficient law reform process for tax, and the resulting drag on economic activity – is largely invisible to IR officials.

In this context, it would be interesting for IR to consider how the New Zealand system of making tax law compares to overseas jurisdictions.

We hope these comments are helpful and please get in touch if further discussion would assist. We look forward to an update in due course on the outcome of the review; contact can be made in the first instance through the Law Society's Law Reform Adviser Emily Sutton (emily.sutton@lawsociety.org.nz).

Yours sincerely

Neil Russ
Convenor, NZLS Tax Law Committee

Cc: Susan Price, Group Leader, Tax Counsel Office, Inland Revenue
Emma Grigg, Tax Policy Director, Policy and Strategy, Inland Revenue

Encl (1)

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3 *Officials' Report to the Finance and Expenditure Committee on Submissions on Taxation (Annual Rates for 2018–19, Modernising Tax Administration, and Remedial Matters) Bill*, November 2018, at 279-280.

4 *Roberts v Commissioner of Inland Revenue* [2018] NZHC 2153.