

Annual Report 2014



Inland Revenue
Te Tari Taake

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From the Commissioner

Welcome



Inland Revenue is making tax simpler, more open and more certain. We've made great strides towards that in the past year.

The next time you file a tax return, claim a refund, pay GST or look for information online, you will find it easier.

Businesses and customers across New Zealand have been telling us what they expect from Inland Revenue: what would save most time and cut costs, what would remove barriers, what would make it easier for people to get on with their lives while still paying their fair share of tax and claiming the right entitlements.

We have been listening and making changes that make a real difference for taxpayers. Coming years will see even more improvement as our business transformation begins to roll out.

Delivering today's services better

Our continuous improvement approach is already bringing new opportunities for New Zealanders as we prepare for major business transformation.

We are talking with software developers about building tax reporting into everyday business transactions, and with small, medium and corporate businesses about future needs. We are talking with tax agents about new relationships and support for clients as Inland Revenue simplifies tax requirements.

To deliver more seamless services for New Zealanders we're working jointly with many other agencies across government. The Better Public Services programme and Government ICT Strategy are supporting increased information-sharing that benefits customers and reduces costs.

Much has changed for the better for our customers over the past year—we celebrate these and further highlights on the next page:

- 1.8 million customers are signed up to manage their tax, file GST and make payments online through myIR secure digital services
- businesses can now register for PAYE when they incorporate online via the Companies Office: more than 2,000 companies using this service have saved \$1.2 million through time saved on compliance
- joint delivery of many government services to shared customers cuts out duplication and makes life easier
- using crowd-sourcing to identify and start work on a mobile app with great benefits for business
- public consultation on tax legislation to simplify tax laws, ensure fairness and support growth
- major court decisions which upheld Inland Revenue's position in favour of taxpayers on the long-running Sovereign case

- continuing support for the Christchurch Rebuild.

Altogether, Inland Revenue reached 85% of our performance targets—an important indication of our continuous improvements in service.

Keeping the tax field level

Our involvement in international tax matters affecting New Zealand continues to grow. We took a leading role in developing OECD responses to the global problem of “base erosion and profit shifting” (BEPS) by multinationals, and supported proposed solutions with our own legislation.

We consulted on and shepherded through legislation to ensure fairness across sectors, to simplify laws so they’re easier to understand, to remove tax loopholes, and to support growth and innovation.

While Child Support Reforms were delayed for a year, we are on track to deliver these in April 2015.

We continued to refresh our approach to debt management and encouraging compliance with tax laws. We now intervene earlier and with a range of options to prevent people and businesses falling into debt and we are examining the current penalties regime. We use sophisticated intelligence systems to tailor compliance approaches to different customer groups, and to tackle ongoing issues like the hidden economy where no tax is paid, deliberate fraud, and tax avoidance.

We over-delivered against our targets in these areas. We continue to investigate fresh ways to encourage behaviour change and make it easier for people to pay.

Together these measures are showing success. New debt has declined by more than 20% and outstanding tax returns continue to decrease. Our investigations work uncovered \$1.24 billion in tax owed.

Building a tax system for the future

We have started work on one of New Zealand’s biggest business transformations that will completely change how Inland Revenue provides service.

There will be real value for New Zealanders as we simplify and streamline the tax system, transform tax policies, business processes and customer services, and make full use of new technology to modernise the tax system.

In future, businesses will be able to manage their tax easily as part of their normal online business processes—not a separate compliance requirement. PAYE, employer monthly schedule and complicated taxes will be simplified. Relevant statistics that Inland Revenue gathers can be shared with other agencies to cut endless duplication—while privacy is still protected.

Individual customers will be able to manage their own tax and entitlements easily online at any time—and be certain they’ve got it right with rapid confirmation. Payments will be lined up with real life and coordinated across agencies.

To provide benefits as early as possible our programme will be delivered in a series of stages. We are talking with customers, businesses and providers as we design our changes so we understand and meet their needs.

Conclusion

This is an exciting time to be leading Inland Revenue. I’m proud of the differences we’re making in people’s lives. I want to acknowledge our staff who are deeply committed to excellent customer service and finding innovative ways to meet ever-changing needs.

We still have many challenges ahead but I am confident Inland Revenue has the people, the skills and the foresight to overcome them.



Naomi Ferguson

Chief Executive and Commissioner of Inland Revenue

Highlights

**\$56.2
Billion**

Tax revenue collected

**\$1.1
Billion**

other revenue
collected

Over one million customers
have registered for our
Voice ID service.



www.ird.govt.nz – 2013

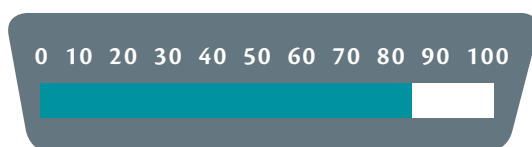
NetGuide Award's best
government website for the
seventh time in eight years.



Nearly 95% of new parents
chose to apply for an IRD
number for their baby when
they registered the birth with
Department of Internal Affairs.



We achieved 85% of our performance
targets, compared with 76% last year.



**85% of our voice and
correspondence customers
are satisfied with our service.**

TransTasman Department-of-the-year: Inland Revenue was chosen as the top-performing government department “based on [our] clear improvement in customer engagement” during the previous 12 months.



We collected total cash in relation to overdue debt of \$4.1 billion, an increase of \$752 million compared to last year.



Cabinet approved the Business Case for our change programme.



Alesco and 11 other companies agreed to an out-of-court settlement \$355.8 million in discrepancies over the use of optional convertible notes. The High Court ruled this to be tax avoidance.

Our specific debt initiative funded through Budget 2010 collected \$293.8 million, 54.6% more than the target of \$190 million. The return on investment was \$13.79:\$1 (target \$8.70).

Through our Budget 2012 debt initiative, we collected \$99 million of aged debt, 164% above our target of \$37.5 million. The return on investment was \$11.45:\$1 (target \$5.50).

PART 01

About Inland Revenue

About us

Inland Revenue contributes to the economic and social wellbeing of New Zealand by collecting and distributing money. Our success is reflected in two outcomes:

- Revenue is available to fund government programmes through people meeting payment obligations of their own accord.
- People receive payments they are entitled to, enabling them to participate in society.

At 30 June 2014 we had 5,641¹ full-time equivalent employees.

Our scope

In the tax year ending March 2013²:

- **Individuals**—about 1.15 million filed annual tax returns
- **Employers**—about 195,000 employers filed over 2.0 million employer monthly schedules with PAYE deductions for employees
- **Companies**—over 380,000 company returns were filed
- **GST filers**—630,000 registered customers filed 3.0 million GST returns.

We manage or share the administration of:

- **Working for Families Tax Credits**—we distributed, with the Ministry of Social Development, \$2.5 billion in entitlements to support working families.
- **Child support**—we collected \$449 million from 175,183 paying parents and distributed \$242 million to custodial parents.
- **KiwiSaver**—we administer the scheme by collecting contributions and transferring them to scheme providers for investment. At 30 June 2014 2.35 million people were

enrolled in KiwiSaver. We distributed \$4.1 billion to scheme providers.

- **Student loans**—we jointly administer this programme with the Ministries of Education and Social Development (StudyLink). We had 721,437 student loan borrowers and collected \$1.0 billion in repayments.
- **Paid parental leave**—we make payments, for the Ministry of Business, Innovation and Employment, to parents who take leave from their job or business to care for a baby. We made \$165 million in payments to 25,836 parents.

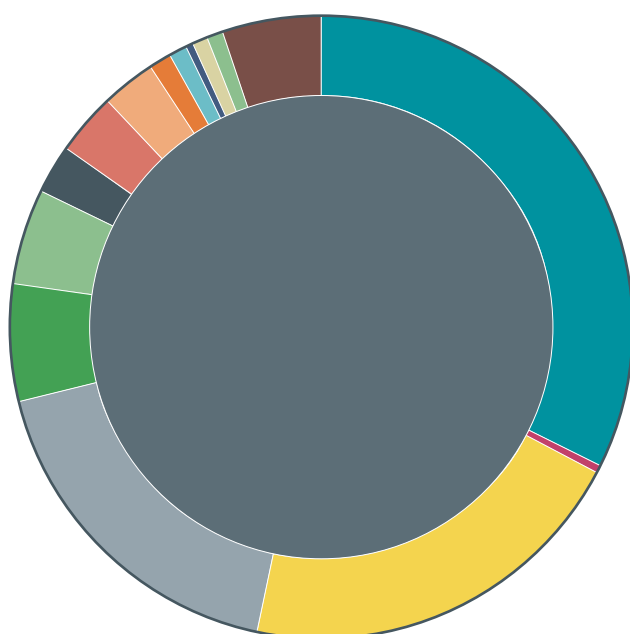
¹ Excludes vacancies.

² 2014 data not available.

Why paying tax matters

In 2013–14, Inland Revenue collected \$56.2 billion in tax revenue, which is more than 80% of the money government uses to pay for services that all New Zealanders benefit from, including healthcare, education, and law and order.

Figure 1 – Breakdown of core Crown expenses by functional classification



Actual 30 June 2013	
GSF pension expenses	\$278 million
Housing and community development	\$283 million
Environmental protection	\$530 million
Other	\$603 million
Primary services	\$659 million
Heritage, culture and recreation	\$804 million
Defence	\$1,804 million
Economic and industrial services	\$1,978 million
Transport and communications	\$2,255 million
Law and order	\$3,456 million
Finance costs	\$3,619 million
Core government services	\$4,294 million
Education	\$12,504 million
Health	\$14,498 million
Social security and welfare	\$22,741 million
Total core Crown expenses (excluding losses)	\$70,306 million

Figures from the Treasury's financial statements.

Our tax system is broad-base and low-rate

An effective tax and social policy system comprises good policy settings plus good administration. Both are needed to have an efficient, functioning system. A well-functioning tax system supports a more competitive and productive economy and helps the Government achieve its fiscal, economic and social objectives.

Most of New Zealand's tax revenue is from three tax bases (personal tax, company tax and GST). All have broad bases, allowing substantial amounts of tax to be collected at modest tax rates.

Where we're going

We set out our long-term intentions in our guiding document *IR for the future*. It describes our role, outcomes and goals for the future.

Figure 2 – *IR for the future* – What we want to be

What we want to be

A world-class revenue organisation recognised for service and excellence

We work with customers and other organisations to make compliance easy and to give New Zealanders confidence that everyone pays and receives the right amount.

To be recognised for service and excellence we aim to achieve the performance goals that define a world-class revenue organisation. These are:

> Speed > Certainty > Compliance > Value

Our strategic intentions

Our strategic priorities referenced in our 2013–16 *Statement of Intent* are:

- We retain, develop and attract high-calibre people with the skills required in the future—enabling a culture of service and excellence
- We proactively influence voluntary compliance and address the causes of compliance risk and threats through a range of interventions
- We move customers to cost-effective channels while creating an environment to make it easy for customers to self-manage
- We improve the efficiency and effectiveness of government through working with other agencies and private providers
- We use our information to make timely decisions and build an intelligence-led organisation
- Our systems meet current and future needs.

The above priorities will help us make progress in relation to our three main areas of focus:

- Implementing our transformation change agenda

- Contributing to government policy and priorities
- Delivering and improving our core business, including enhancing the customer experience.

Our financial performance

Our operating budget for the 2013–14 financial year was \$744.2 million, an increase of \$59.3 million compared to the previous financial year. Most of this increase was for Business Transformation and funding for reform of the Child Support Scheme.

Actual expenditure was \$44.7 million (6%) under budget. A significant portion of this (\$16.8 million) will be transferred to 2014–15 for work on the child support legislative initiative, Budget 2013 legislative initiatives and information technology mainframe services. These were planned to be undertaken in 2013–14 but will now occur in 2014–15.

Since the Operations Management programme started in March 2011, we have produced capacity savings equivalent to \$17.9 million (\$3.2 million above target).

Our tax and social policy settings were designed to work well within our existing revenue collection system, FIRST. We have delivered major initiatives during the past decade through modifying and developing systems, manual interventions and workarounds. By doing this, we've added layers of complexity and risk to our business processes and core technology infrastructure.

We're committed to delivering our services today and tomorrow and recognise that we need to change. So, we're transforming Inland Revenue to achieve the goals in *IR for the future*. This work will:

- make it easier for our customers to pay tax, meet their social policy obligations and receive their entitlements

- increase certainty for our customers
- increase the efficiency of our debt collection
- reduce compliance and administration costs
- support all-of-government goals
- ensure the integrity of our tax system
- allow faster implementation of government policy.

PART 02

How we help you

Making it easy to pay tax and receive entitlements

We aim to make it easy for our customers to manage their tax obligations and entitlements by providing information, assistance and tools so they can do it for themselves.

We asked our customers how we could improve our services and how tax could be simplified. We made changes to our website so customers can easily find the information they need and know how to contact us when they need to.

We provided new ways of giving customers information. We created five new “how-to” YouTube videos to help customers understand income and provisional tax, business expenses, business structures, depreciation and how to register for GST. These videos are also available in sign language and Te Reo. We made a “getting it right” video to help our customers who are closing their businesses.

We started work to enhance our eAlerts service, to notify customers when GST statements and notices appear in their myIR accounts.

You can view our videos at:
www.ird.govt.nz/help/demo/intro-bus-vids



Voice ID

We reached the goal of one million registrations for our voice ID service this year. Callers save up to a minute of time by not having to answer personal security questions to verify their identity. Voice ID complements our online services because customers can reset their online password by phone at any time.

App4IR Challenge

We held a competition to find an innovative mobile app so small businesses could interact with us more easily. The winners of the App4IR Challenge, Matt Innes and Josh Lee, are working with us to develop their idea.

Savetime campaign

In May 2014 we ran a Savetime campaign in Hawkes Bay, asking small-business owners to rank six improvements we could make to save them time. We asked for other suggestions on what else we can do to help them.

We targeted 70% of small businesses in Hawkes Bay with our advertising. The campaign was promoted through our website and other business channels. We received over 1,400 submissions and around 300 individual suggestions for ways to save time. The Taxpayers Simplification Panel and our Business Transformation programme will use this feedback to inform the prioritisation, development and delivery of changes that benefit small-business customers.

Taxpayers Simplification Panel

We set up a Taxpayers Simplification Panel to give New Zealanders an active voice in simplifying, modernising and transforming the way we pay tax. Owners of small to medium-sized businesses and individuals make up the panel. The panel will evaluate customer feedback from our Savetime campaign and our customer research.

Ensuring that our customers are satisfied with our services contributes to voluntary compliance. In 2013–14, 79% of customers thought we made it easy to get it right, and 82% of our customers were confident that we were fair.



Our customer information guides won the “Best Plain English Turnaround” category at the WriteMark 2013 Plain English Awards. The rewritten guides presented clear and customer-focused tax information.

Helping student loan borrowers manage their loans

We made improvements to make it easier for student loan borrowers to manage their loans. Our new online calculator shows borrowers how much they need to repay, how long it will take to repay their loan in full and how making extra repayments can help them pay their loan faster.

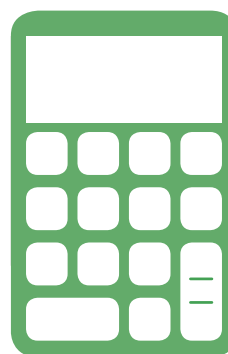
We made it easier for overseas-based borrowers to repay their loans by removing fees for their payments.

Working with KiwiSaver scheme providers

The overall KiwiSaver membership has continued its steady increase during the last year. There are now 2.35 million members in KiwiSaver. We have continued to share a productive working partnership with KiwiSaver scheme providers. This year Inland Revenue transferred \$4.096 billion to scheme providers on behalf of members, an increase of 33% on the previous year.

Privacy

Inland Revenue is committed to ensuring that customer information is protected. Any personal information that is provided to us will be kept for as long as necessary to achieve the purpose we collected it for. For information about privacy breaches, see the Additional Information section.



Providing customers with certainty

Tax and social policy can be difficult to understand. We continued to make it easier for customers to understand their obligations by providing education and assistance in the community, and certainty through interpreting tax and social policy laws and their application.

Growing community contact

Our community compliance officers were out and about in the community at 118 mobile office sites through the year. This meant fewer customers needed to travel to see someone in a branch office. We delivered 3,858 seminars, expos, workshops and appointments, which involved 41,896 customer contacts.

We told our customers about activities that could result in us taking a closer look at their business practices, and followed this up with a booklet giving small and large enterprises clear information about their tax obligations.

Interpreting the law and clarifying its application

We provided certainty by issuing binding rulings for taxpayers with specific transactions, public rulings and statements. We reviewed tax disputes to ensure that we applied the law correctly, which gives taxpayers confidence in the integrity of the tax system and helps them meet their tax obligations.

We finalised 27 public rulings and statements, which included a significant Interpretation Statement clarifying the tax residence rules and two public rulings on the tax treatment of some standard terms in Public Private Partnership contracts.

Understanding what influences customer behaviour

We have a compliance model that helps us design strategies and interventions to facilitate customer compliance. We are redesigning the model to provide us with a more comprehensive view of the factors that influence customer behaviour. The additional factors reflected in the new model will relate to customers' capabilities, motivation and opportunities. Understanding customer behaviour makes it easier for us to design more effective approaches to improve compliance.

Updating tax and social policy laws

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An important part of our approach to the development and review of tax policy is public consultation. This provides greater transparency of our policy-making process, and allows us to listen and respond to New Zealanders, tax professionals and associations.

During the year we worked on six tax and social policy-related bills, which are now enacted. The bills focused on:

- tightening laws to ensure fairness
- simplifying the law to make it easy to understand
- supporting growth and innovation.

Tightening laws to ensure fairness

The Taxation (Livestock Valuation, Assets Expenditure, and Remedial Matters) Act 2013 included changes to ensure fairness in the tax system. These included tightening the tax rules for assets like holiday homes, boats and aircraft used by the owners privately and to earn income. It introduced new rules for the disposal of herd scheme livestock to prevent some farmers switching between the two main livestock valuation methods to receive an unfair tax advantage.

The Student Loan Scheme Amendment Act 2014 introduced tougher ways to deal with overseas-based student loan borrowers who continually refuse to make repayments. It introduced higher repayment obligations for overseas-based borrowers so they pay off their loans sooner. For more information see *Child support and Student loan debt* on pages 24–25.

We developed the policies in the Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Act 2014. This simplified the rules for taxing foreign superannuation interests, making it

easier for people to understand and comply with their obligations. It aligned the tax treatment of certain mineral miners with other taxpayers to make the rules fairer in this sector.

Simplifying the law to make it easy to understand

The Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Act 2014 introduced practical rules to make it easier for businesses and other taxpayers to understand their tax obligations. It included ways to give businesses more certainty about how to apply employee allowances, such as employer-provided accommodation and other payments made to employees to reimburse them for expenses. It helps businesses understand what is taxable and what is not. Changes to the thin capitalisation rules³ are intended to protect our tax base by ensuring that offshore companies with New Zealand subsidiaries pay their fair share of New Zealand tax.

The financial reporting obligations for some medium-sized companies have been simplified following changes introduced by the Financial Reporting Act 2013. This act came into effect on 1 April 2014 and means lower compliance costs for most companies with annual revenue between \$2 million and \$30 million.

We have also clarified GST rules and various other tax rules to make them easier for people to understand and apply.

³ The thin capitalisation rules are part of New Zealand's international tax rules and are designed to protect our tax base by limiting how much debt foreign companies can allocate to their New Zealand investments. The use of debt is one way that non-residents can use to take profits out of New Zealand by claiming a deduction for the interest they pay on this debt. This reduces the amount of tax they have to pay here.

Student loan redesign project

We completed an extensive programme of work to implement changes to the administration of the student loan scheme. This was the result of legislative amendments and included significant changes to our systems.

Supporting growth and innovation

Changes have been made to help support business growth and innovation by clarifying and removing distortions in the previous rules. The new rules clarify what is able to be deducted for certain company running costs and money spent on abandoned applications for patents, resource consents and plant variety rights. We have removed some distortions relating to Research & Development to encourage businesses to undertake these activities.

Implementing changes to the child support scheme

We have delayed implementing changes to the child support scheme. The changes relate mainly to new payment formulas. The complexity of these changes and flow-on effects for our IT systems contributed to delaying the implementation by a year, from April 2014 to April 2015. The Government requested the delay in December, and Parliament legislated the deferment in the Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Act 2014.

As a result of the delay, we commissioned an independent review of the way we had managed the project. In March, external consultants produced a report examining the reasons for missing the original implementation date, as well as assessing

the feasibility of the new implementation date. The report concluded the revised date was achievable. It also made a number of recommendations, which we accepted and are putting into effect. The recommendations covered:

- project governance arrangements
- planning
- forecasting and change control
- project team structure
- reporting
- stakeholder management.

Our contribution in helping to address international tax issues

Base erosion and profit shifting⁴ by multinationals is a global problem. Over the past year we have strengthened our involvement in international tax through the OECD-led work programme. The G20/OECD Action Plan was released in July 2013. The first set of proposals is expected around the time of the G20 Finance Ministers' Meeting in September 2014.

On 1 March 2014 the Multilateral Convention on Mutual Administrative Assistance in Tax Matters took effect. This was approved by New Zealand in November 2013. The convention allows us to request information and assistance from other tax authorities to collect outstanding debts from tax evaders who move overseas.

⁴ Base erosion and profit shifting (BEPS) refers to tax planning strategies that exploit gaps and mismatches in tax rules to make profits "disappear" for tax purposes or to shift profits to locations where there is little or no real activity but the taxes are low resulting in little or no overall corporate tax being paid.

The United States requires information to be shared with it on relevant financial transactions under its Foreign Account Tax Compliance Act (FATCA). This US law is aimed at reducing international tax avoidance by its citizens. New Zealand and the United States entered into an intergovernmental information-sharing agreement to minimise costs to New Zealand financial institutions complying with FATCA.

Three new double tax agreements (DTAs) came into force during the year. DTAs help encourage growth and promote cross-border trade by preventing businesses and individuals from being taxed twice on income earned. They are important in helping authorities prevent tax evasion and avoidance. DTAs that came into force were with Japan, Papua-New Guinea and Viet Nam.

New legislation included:

- The Taxation (Livestock Valuation, Assets Expenditure, and Remedial Matters) Bill, introduced in September 2012, enacted in July 2013.
- The Student Loan Scheme Amendment Bill No 3, introduced in August 2013, enacted in March 2014.
- The Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Bill introduced in May 2013, enacted in February 2014.
- The Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Bill introduced in November 2013, enacted 30 June 2014.
- The Budget Measures (Miscellaneous Fiscal Matters) Bill and the Budget Measures (Financial Support for Newborn Children) Bill, introduced on 15 May 2014 as part of Budget 2014, resulting in the Cheque Duty Repeal Act 2014 and the Taxation (Parental Tax Credit) Act 2014.

Our response to people who don't file and pay on time

We try to make it easy for people to pay the right amount on time. Most people do this and they expect us to take action against those who don't. When people don't file and pay, the government has less money for the things we all need.

Filing returns and making payments on time

We encourage people to file their returns and pay on time. Two key payment dates are 7 February and 7 April. Payments for outstanding income tax, student loans and Working for Families Tax Credits fall on these dates. Customers using a tax agent have until the later date to pay. We sent more than 37,000 letters and more than 100,000 text messages to remind individuals and businesses of these deadlines.

After each deadline passed, we ran a direct-contact campaign to follow up on those who had not paid. By 30 June 2014 we had resolved 86.2% of the amount overdue at 7 April compared with 83.9% last year. For those with the 7 February payment date, the result was 58.1%, compared with 57.6% last year.

The number of outstanding returns continued its year-on-year downward trend, falling 7.1%. This was helped by concentrating on high-value outstanding returns from companies, which often involve large amounts of tax. Our target was to achieve assessed value of \$14 million. The year's result was more than seven times above this, at \$105 million. The return on investment was \$19.64:\$1 (target: \$2.90).

This year we received (relating to the 2012 tax year):

- 7.3 million returns for PAYE, GST and income tax of which 83% were filed on time.
- 4.5 million payments of which 86% were paid on time.

Tax debt

Collecting and reducing tax debt

We know that when people and businesses fail to file their tax returns on time, they may struggle to pay their tax on time. Early action to get them to file their returns helps us to work with them to meet their payment obligations.

We aim to minimise debt, maximise debt recovery and deal effectively with uncollectable debt.

This year, there has been a relatively small growth in the total overdue tax debt, although the rate of increase is slightly higher than last year. Total tax debt is \$6.2 billion, which is an increase of 4% from 2012–13. Penalties and interest charges continue to increase debt and were \$3 billion of the total tax debt outstanding. The older the debt, the higher the ratio of penalties and interest to debt.

Our overall cash collections result improved this year. We collected total cash of \$4.1 billion, an increase of \$752 million compared to last year. 69% of total cash collected came from making direct contact with people and businesses in default.

Collecting debt early

We focused on collecting newer debt, which resulted in over 565,000 cases being resolved during the year. We resolved 66% of overdue debt cases within three months of opening. The amount of debt up to two years old has declined. It was \$2.88 billion in 2010 and \$2.24 billion at 30 June 2014, a drop of 22.6%.

Managing older debt

Overdue debt more than two years old increased from \$2.26 billion in June 2010 to \$4 billion in June 2014. 76% of this growth occurred by June 2012, which included some large cases and student loan overseas-based borrower debt. From June 2012, the main driver of the increase was penalties and interest charges.

Our Budget 2012 debt initiatives helped slow the growth in aged debt value. The value of debt aged over two years increased by \$173.8 million this year, compared to \$248.1 million last year. More than half of the aged debt increase from June 2010 relates to debt more than five years old where penalties and interest account for more than the principal of the debt.

Specifically funded compliance programmes

We received funding to carry out initiatives to improve collection of outstanding returns and overdue debt.

New collection initiatives have enabled us to intervene early with customers who have newer debt and we follow up with customers who fail to keep up instalment plans as soon as they default. These initiatives have produced extremely good results. During the year we collected \$293.8 million, 54.6% more than the target of \$190 million. This result was 12.5% higher than last year's. The return on investment was \$13.79:\$1 (target \$8.70).

Penalties and interest

We have started reviewing the implications of our penalties and interest regime, particularly its effect on compliance. Customers are more likely to pay their debt if we contact them early, and before penalties and interest become larger than the original debt.

We realise that sometimes payments or returns are late for a reason. This is why we have measures in places such as:

- grace periods, which means that people who normally meet their obligations are not penalised unfairly
- instalment plans
- remission/relief from penalties and interest in limited circumstances.

We charge late filing or payment penalties and interest consistently. Penalties and interest can quickly add up, so it's important that we encourage people and businesses to file and pay on time. When they don't, we aim to get them into an instalment plan as soon as possible after they miss a filing or payment date.

We reviewed how we apply penalties and interest to debt⁶, particularly non-collectable debt. This is a growing proportion of overall debt. Any changes to the way we apply penalties and interest will require legislative change.

Penalties and interest charged as at 30 June 2014 was \$3 billion, which is 48.1% of the total overdue debt. At June 2013, penalties and interest was \$2.9 billion and 47.9% of the overdue debt.

This year, 80.7% of penalties and interest is linked to cases aged two years or over. Last year, 79.4% of penalties and interest was linked to debt cases aged two years and over. This shows the continuing debt growth caused by penalties and interest and the impact of our focus on new debt.

⁶ Excluding child support debt.

Child support and student loan debt

Child support debt

We collect child support from liable parents and distribute these payments to custodial parents. This year, we collected \$449.5 million and forwarded \$241.6 million to custodial parents⁷.

There are 136,000 child support customers in debt, down 7% on a year ago. However, the total dollar amount overdue was up 9.6% at \$3.05 billion driven by penalties. Penalties charged on child support debt increased by 12.4% from last year and represent 77.6% of the total debt.

We have been successful in dealing with new child support cases before debt and penalties begin to accumulate. We have resolved 75.5% of new cases within 12 months. This compares to the previous year's result of 67.5%. We have increased our focus on liable parents living overseas who are not paying their child support debt.

About two-thirds of overseas-based liable parents who are not meeting their child support obligations live in Australia. We renewed our agreement with the Australian Department of Human Services (ADHS) to assist in the collection of child support. We collected \$50.2 million with the assistance of ADHS. This compares to the previous year's result of collecting \$51.5 million.

We are using tracing information from the ADHS and a commercial collection agency to make direct contact with Australian-based liable parents from New Zealand. We also used the debt collection company to collect debt directly from liable parents. We are using a similar approach in the United Kingdom. Passport details supplied by the Department of Internal Affairs under an information-sharing agreement have aided our efforts.

We began taking legal proceedings directly from New Zealand to recover money from more resistant New Zealand-liable parents in Australia. We have received positive judgment for two cases and are lodging these with the Australian courts.

We contacted liable parents who have recently left the country to remind them of payment dates to prevent them getting into debt. Of those contacted, 70% paid by the first due date.

Overdue student loan repayments

As at 30 June 2014, we had 110,000 borrowers with overdue payments⁸. Of these 74% were overseas. The total overdue amount was \$769.4 million, 89% of which was owed by overseas-based borrowers.

To target overseas-based borrowers we began an initiative in November 2010 to contact borrowers and remind them of their obligations and current position. We continued to issue more notices to overseas-based borrowers to help reduce the potential for default.

We are adding a fifth provider to our fee-free payment channels to make it easier for borrowers to keep up with repayments. This direct debit option will be available in Australia early in the next financial year. This year we received \$33.5 million of payments from free payment channels.

Many overseas-based defaulters live in Australia. We used a commercial company to help bring in payments, which totalled \$6.7 million from 1,782 borrowers during the year.

We launched an online advertising campaign to encourage overseas-based borrowers to meet their obligations. The campaign began in June 2014 and runs for 12 months.

In March 2014 changes to the student loan scheme made it a criminal offence for borrowers living overseas who are in default to knowingly fail or refuse to make reasonable efforts to pay. The legislative

⁷ The balance is collected for the Government as an off-set for custodial families supported through the benefit system.

⁸ Overdue amounts are any unpaid amounts where the due date for the amount is passed and may include late payment interest.

For more information on the student loan scheme, please read the Student Loan Annual Report available at www.educationcounts.govt.nz

changes allow us to request an arrest warrant for persistent defaulters returning to or leaving the country. Other changes have allowed us to increase repayments from compliant overseas-based borrowers, obtain the contact details of any borrower from third parties, and align the treatment of student loans with those of other tax types.

How we take action against those who try to avoid paying their tax

Our investigators use risk assessments and intelligence to identify potential non-compliance by individuals, companies and sectors of the economy. The immediate goal is to uncover undeclared or under-declared income. The wider goal is to strengthen public confidence in the tax system and encourage voluntary compliance.

We also investigate complicated areas of tax law that can allow taxpayers to put in place complex arrangements to reduce the tax they pay. Disputes about such arrangements can end up before the courts. Disputes usually focus on the difference between the tax position filed by a taxpayer and the position determined by our investigators. We call this difference a discrepancy. We identified discrepancies during the year of \$1.24 billion⁹. The overall return on investment was \$8.00:\$1 (target \$7.70).

Aggressive tax planning

Work to counter aggressive tax planning contributed \$539.8 million toward the total discrepancies result. Of this, \$414.2 million came from work examining complex finance and trust losses. This produced a return on investment of \$62.40:\$1 (target \$11.40).

The most significant contribution came as a result of an out-of-court settlement with Alesco New Zealand Limited over its use of optional convertible notes, which the courts had ruled to be tax avoidance. Eleven other companies agreed to be bound by the outcome of the Alesco action because of their similar use of optional convertible notes. Alesco and the other companies agreed to discrepancies of \$355.8 million.

The hidden economy

We set a target of identifying discrepancies of \$44 million in the hidden economy. We exceeded that target by \$5.8 million. Areas subjected to greater scrutiny included the hospitality, construction, inbound tourism and independent contracting sectors. The return on investment for this initiative was \$5.51:\$1 (target \$5.00). We supplemented investigations work with seminars, compliance checks and providing online tools to ensure more people in these sectors declared all income.

⁹ We do not necessarily collect the amount in question because assessments often relate to loss adjustments and future values.

Property

Property is another sector where short-term trading and other speculation produces undeclared or under-declared income. We identified discrepancies during the year of \$52.4 million. At the end of four years we identified discrepancies for the Budget 2010-funded programme of \$195.1 million¹⁰. The target was \$180 million. The return on investment was \$7.88:\$1 (target \$6.80).

We concentrated on identifying developer speculation, particularly in Auckland and Queenstown, and examining residential property sales. We visited 2,500 property industry participants and other interest groups to increase awareness of tax-related responsibilities. We monitored about 26,000 properties and property-related assets.

Fraud

We identified fraud-related discrepancies totalling \$10.4 million (target \$10 million), a return on investment of \$3.73:\$1 (target \$3.10) for this Budget 2012-funded work. Most discrepancies were connected with Working for Families Tax Credits or personal tax summaries, and involved improper use of documentation or obtaining a financial gain which the taxpayer was not entitled to.

Legal action

The Court of Appeal upheld the High Court finding against Sovereign over certain financial reinsurance arrangements. A 2012 High Court judgment found Sovereign had not given the right tax treatment to reinsurance arrangements with three reinsurers. A subsequent leave to appeal request to the Supreme Court against that finding was rejected, leaving Sovereign with a tax liability of up to \$90 million (\$47.5 million tax plus interest). The result is important in defining the boundary between insurance and financial arrangements and the tax treatment applicable to each.

During the year, we completed 74 prosecutions for tax evasion or knowledge offences.¹¹ This compared with 92 last year. The decrease was related to the timing of cases before the courts. At 30 June 2014, there were 89 such cases pending.

¹⁰ To the year ended 30 June 2014.

¹¹ Knowledge offences relate to knowingly breaching a tax obligation, such as deliberately not keeping legally required books and documents, or not providing information.

PART 03

How we work with other agencies

Better public services

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We are increasingly working with other government agencies to build better public services that are more innovative, open and responsive, and offer “joined-up” services for customers.

Inland Revenue is supporting a number of cross-agency initiatives through the Government’s Better Public Services programme. We are continuing to contribute significantly to the achievement of Better Public Services Result areas 9 and 10. We also contribute to a third, result 7.

Result 9—New Zealand businesses have a one-stop online shop for all government advice and support they need to run and grow their business

Result 9 roadmap and blueprint

We worked with other agencies to develop the Result 9 Roadmap and Blueprint. These documents describe the future development of government services for business to 2023. This approach was endorsed by Cabinet in July 2014.

Employer registration

We worked with the Companies Office to develop a new digital service to help New Zealand companies register with the Companies Office. The Integrating Employer Registration service gives new companies the option to electronically register with Inland Revenue as an employer at the same time.

New Zealand Business Number (NZBN)

Inland Revenue contributed to the design of the New Zealand Business Number initiative and supported the Ministry of Business, Innovation and Employment (MBIE) in developing its business case. The New Zealand Business Number is a unique number, assigned to each New Zealand business to make it easier to interact with government agencies and other businesses. The number will make a big difference to compliance time and costs for businesses. We will work with MBIE to incorporate the NZBN into our Business Transformation programme.

Result 10—New Zealanders can complete their transactions with government easily in a digital environment

Result 10 blueprint

We worked with other agencies to develop the blueprint outlining the approach to achieving 70% of common transactions being completed digitally by 2017. This was endorsed by ministers as government policy for digital services in July 2014.

Digital registration for immigrants

We worked collaboratively with MBIE to develop a business case that looked at creating a service for new immigrants that integrates digital registration for an IRD number with their digital visa application. This is now being considered as part of our Business Transformation programme.

IRD numbers for newborns

From 1 July 2013, parents of newborns can apply for an IRD number for their child by ticking a box on the Department of Internal Affairs (DIA) birth registration form. Since we signed the agreement over 48,000 people—that’s nearly 95%—have used this service. This new, paper-based service means parents no longer need to duplicate details on separate forms to access social policy entitlements or open a child’s bank account. DIA is looking at moving this application process online.

Result 7—Reduce the rates of total crime, violent crime and youth crime

We have worked with the New Zealand Police to implement an Approved Information Sharing Agreement to allow a reciprocal sharing of Inland Revenue information with the Police in relation to serious offences. We signed this agreement in June 2014 and it comes into effect on 22 September 2014. It assists with the prevention, detection, investigation, or use as evidence of a serious crime.

We continue to manage the systems that run our core tax and social policy systems to a level that meets our commitments to New Zealanders, as well as ensuring that technology and information remain safe.

All of Government ICT

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We are investing in our ICT systems and infrastructure to provide better, smarter and more cost-effective services. Through the year we have taken advantage of the all-of-government services, in particular Infrastructure as a Service and Storage as a Service.

We are simplifying our technology environment and taking advantage of externally provided common and repeatable services. We will continue to take advantage of these services where it makes sense to do so.

In October 2013, we signed an agreement with Unisys to buy a mainframe service to replace an ageing mainframe platform. This service will provide Inland Revenue with the necessary continuity of core tax and social policy systems while we transform. Our initial plan was that this would be operational before our 2013–2014 peak season. We decided to reschedule this implementation until November 2014 to ensure successful implementation outside our peak period.

We share and match information with other agencies

People tell us it's not easy dealing with different government agencies over the same thing. We have been working to fix this. One way is collecting information once and sharing that information with other agencies. Information sharing and matching is important because it reduces duplication of processes and saves our customers time.

Sharing information between agencies allows us to check whether customers are paying what they need to and getting what they are entitled to. We are continuing to work with other agencies to develop approved information sharing agreements, in particular those related to welfare, business and serious crime.

Over the past year we signed six Memoranda of Understanding with other government agencies. This has enabled us to reduce duplication of some activities for some customers.

Department of Internal Affairs (DIA)

We developed an information-sharing agreement with DIA to share the contact details of overseas-based child support liable parents and student loan borrowers who apply to renew a passport. This agreement came into effect in October 2013.

We have an information-matching agreement with DIA. This allows us to follow up on defaulters living overseas when they apply to renew their passports. We were able to collect \$6.7 million from 1,501 defaulters through this arrangement, which came into effect in October 2013.

We have been working with DIA to establish a new information-sharing agreement regarding overseas-based student loan borrowers who are not in default, but whose contact details seem to be out of date. This will take effect in August 2014. For details on this agreement, please see the "Additional Information" section.

Your privacy and sharing agreements

We take customers' privacy seriously when we share information.

Full details of our sharing agreements with New Zealand Police and the Department of Internal Affairs are available on the "About Us" section of our website www.ird.govt.nz

New Zealand Customs

In July 2013, we started a new information match with the New Zealand Customs Service. Now we get an alert when persistent student loan defaulters return to New Zealand. Using this information we made contact with 1,095 student loan borrowers in default and collected \$3.1 million from 471 borrowers during the year. We began taking court action from New Zealand to obtain judgment against Australian-based borrowers in default. Legal action against United Kingdom-based borrowers resulted in payments of \$1.3 million.

Ministry of Education

We signed an agreement with the Ministry of Education to help deal with the problem of people in serious default on their student loans.

Ministry of Social Development (MSD)

We have been sharing information with MSD since March 2013. We identified all working-age beneficiaries who also have employment income. At 30 June 2014 over 6,000 benefits had been cancelled because the person was not entitled to them, with just under 5,000 benefits identified as being overpaid (valued at \$47.7 million), and 30 benefits identified as being underpaid (valued at \$32,000).

We also identified 67 instances of suspected benefit fraud. These were referred to MSD.

Integrated services with other government agencies

Shared services with DIA

We completed a project to put in place a shared financial management information system with DIA. We also now provide other financial services for DIA, including accounts receivable, accounts payable and bank reconciliations. The project went live in three stages:

- trust accounts—November 2013
- Crown financial services—April 2014
- Departmental financial services—1 July 2014.

Sharing offices with other government agencies

We continued to reduce property overheads to lower our running costs. This year we made the best use of existing office space through sharing offices with other government agencies where possible. Options taken up this year included sharing with the Ministry of Education in Rotorua and with DIA in Dunedin and Invercargill.

Helping rebuild Christchurch

Inland Revenue has continued to contribute to the rebuilding and recovery of Christchurch, which is a Government priority. Our work in the reconstruction falls into three categories:

- compliance
- social recovery
- working with other agencies to deliver coordinated and innovative services.

Unique compliance initiatives required

The rebuild has created an environment with unique compliance risks associated with increased cash payments. We have identified and addressed risks as they arise to help ensure that the Government receives the appropriate revenue from the considerable investment in rebuilding Christchurch. This has included focusing resources to ensure GST and PAYE obligations are met, especially by new businesses. We strengthened local relationships with industry associations, funding distributors, insurance companies and government agencies. With MBIE, we increased migrant workers' and their employers' awareness about their tax obligations.

Our people working on social recovery

Some of our people worked as earthquake support coordinators to provide government agency support to Cantabrians. We continued to provide additional support to our own Christchurch people and worked with other government agencies to support the government sector in Christchurch.

Working with other agencies in Canterbury

We continued to work with the Canterbury Earthquake Recovery Authority and other agencies in various forums to support the overall reconstruction effort. This included planning for the Public Sector Precinct.

We also worked with MBIE and the Christchurch Central Development Unit in the procurement process for big government-funded projects.

We continue to work with other agencies to investigate co-location opportunities as they arise.

Evaluating work in Christchurch

Inland Revenue is leading a long-term study of the impacts of the Christchurch earthquakes on small and medium enterprises (SMEs). The study looks at compliance behaviour, tax debt, potential hidden economy activity, and how Inland Revenue's responses influenced SME behaviour. This study began in 2012 and results can be found on our website www.ird.govt.nz under the Research and Evaluation section of "About Us".

Over the past year we have been involved in an evaluation of the immediate and long-term economic effects of the Christchurch Rebuild. We are also involved in research into the Christchurch Rebuild Workforce—understanding their characteristics and compliance challenges. This research will enable us to assess the impact the rebuild has on our revenue streams.

PART 04

How we are transforming

We have started work to change the way we deliver our services. Our Business Transformation programme is our key mechanism to achieve the long-term change required to create our new modern revenue system. At the same time, we're making everyday improvements that help us keep pace with New Zealanders' diverse needs and expectations for an efficient tax administration.

Our challenge is to create a modern revenue system that makes managing tax easier and faster for customers, that is able to implement government policy changes with greater agility and that delivers better value for New Zealand. This means providing services that are cost-effective, digital by default and the product of agencies working together with the goal of making it easier for the customer. This also supports the Government's Better Public Service Results 9 and 10.

Inland Revenue is responding to this challenge by planning changes that will overhaul the entire organisation and how it works with the wider revenue system. This includes:

- how we administer tax policy
- the services we provide
- the way customers interact with us
- the systems required to support our future direction.

Our plans take into account Inland Revenue's portfolio of tax and social policy products, and New Zealanders' expectations that we will keep pace with their diverse and changing needs.

Cabinet confirmed our business case for change

During the past few years, we have been in the planning phase of our Business Transformation programme. In late 2013, Cabinet confirmed the case for change and the need for investment, and agreed to modernise the revenue system through a business-led, technology-enabled transformation programme. We achieved these key milestones for engaging a

strategic programme design partner:

- received expressions of interest from potential providers
- completed a "competitive dialogue" process with the two providers we selected to progress to the next stage
- issued a Request for Proposal (RFP) for the design phase.

The Business Transformation programme's investment objectives are as follows:

- improving agility so that policy changes can be made in a timely and cost-effective manner
- delivering more effective services to improve customer compliance and help support the outcomes of social policies
- improving productivity and reducing the cost of providing our services
- improving the customer experience by making it easier and simpler for our taxation and social policy customers
- increasing the secure sharing of intelligence and information across government to improve delivery of services to New Zealanders and improve public sector performance
- minimising the risk of protracted system outages and intermittent systems failure.

Cabinet also confirmed our programme roadmap. The programme roadmap was developed as a plan to deliver the Business Transformation programme in a number of steps and enables the Government to make investment choices throughout the life of the programme. The roadmap's four stages are:

Stage 1: Enabling secure digital services—to enable the majority of customers to self-manage and reduce businesses' compliance burden in fulfilling their PAYE obligations.

Stage 2: Streamline income and business tax processes—this will leverage the foundations delivered in the previous stage and further reduce businesses' compliance burden to fulfil their tax obligations.

Stage 3: Streamline social policy delivery—this will improve the delivery of the social policies that Inland Revenue administers.

Stage 4: Complete delivery of the future revenue system—this will include transitioning any remaining tax and social policies to a new platform, and decommissioning technical platforms that are no longer required.

We started work on business cases for further investment decisions. The first business cases will seek approval for the scope of the design phase, and for initiatives aimed at improving our digital services.

Getting ready for change

Since approval of the Programme Business Case in March 2014, we have been undertaking further work. This has included:

- strengthening our governance frameworks
- establishing core programme management capabilities and delivery methodologies
- mapping the current state processes, and undertaking a detailed assessment of all current state technology, in preparation for transition to new processes and systems
- developing personas and scenarios to show how customer experiences will change, and developing a future state architecture
- assessing what our systems and people currently deliver, what needs to be changed, and the order in which to make those changes

Stage 1

Stage 1 focuses on modernising and expanding our online and digital capacity, improving information collection processes from businesses and streamlining PAYE. Process modernisation, supported by new technology systems, will lower compliance costs and improve customer service as well as give us more flexibility and capacity to deal with future change.

- conducting a robust procurement process to select a transformation services provider(s) to provide design services
- putting in place risk management and assurance plans
- learning from the experiences of other organisations, including site visits to major transformation projects carried out by the two shortlisted Request for Proposal (RFP) participants
- educating ourselves about core tax and social policy technology platforms.

Selecting a provider

In early October 2013, we asked for expressions of interest from vendors interested in providing design services for our Business Transformation programme. We held workshops and forums to explain the programme to interested industry groups and the public. We received nine responses and chose Accenture and Capgemini to engage in the next stage of competitive dialogue.

The use of the competitive dialogue process was a first for us. This process helps manage large, complex procurement contracts and it aligns with the Government's Procurement Strategy. It involves a two-way discussion of options, leading to an RFP for the design stage. We discussed the design, commercial and legal frameworks for both the RFP and the contract for design services, and the cultural and organisational change implications.

In April 2014, we issued an RFP to Accenture and Capgemini to undertake the detailed design for stage 1 of the programme and the high-level design for stages 2, 3 and 4. A decision on the preferred provider is scheduled for late 2014.

A separate part of our work has been investigating off-the-shelf commercial software options. This helps us understand their capabilities before we start on our design phase. This work continues into 2015.

Engaging New Zealanders

Creating a modern revenue system will have a significant impact on the lives of many New Zealanders, and we have been talking with a range of industry groups and taxpayers on what people want from the change. Among the groups we engaged with this year were ICT industry groups, accounting and financial services professionals, academics and businesses.

The recent "Tax Administration for the 21st Century" conference highlighted strong levels of engagement among stakeholders, identifying a number of issues that the future tax system needs to address.

Our Transformation Reference Group also provides us with external advice on the programme and related issues.

Further input from the New Zealand ICT industry is planned for the 2014–15 year when we will launch our ICT reference group. The group will ensure ICT industry perspectives are heard at a high level, and be an opportunity for an open exchange of views.

In December 2013, we began the first of a series of discussions with sections of the community to get their input into the change programme. Our business designers held talks with employers, tax agents and bookkeepers in Auckland, Christchurch and Napier to get their views on how to improve the PAYE system. We held a session with a group of software developers in Wellington. How our customers interact with us and their preferences will help shape the design for the new system.

Our people

Our people offer the best service they can while learning new skills and new ways of working. We want to be an organisation that has a healthy, inclusive culture where our people thrive and are valued.

Working with unions representing our people

Over the past year, Inland Revenue reached agreement about staff employment conditions with the three unions representing our employees: the Public Service Association (PSA), Taxpro and the National Union of Public Employees.

The PSA and Taxpro agreements run until February 2015 and the National Union of Public Employees until May 2015. We are working with the unions to develop new performance and remuneration arrangements for their members.

Developing our leaders to lead change

We want our leaders to provide change leadership and strong direction. We are helping them develop the skills to achieve this through:

- a talent management and succession process to identify and grow our future leaders
- creating common expectations and development plans for senior leaders
- participating in the State Services Commission's Career Board
- "Leader as Coach" training for 228 leaders

- 78 people participating in our "EMERGE" leadership programme for future leaders, and 54 people participating in our "LEAD" programme for frontline leaders.

Training our frontline leaders

We train our frontline leaders to improve our processes, while making sure we are offering taxpayers value for money.

Training by our Operations Management programme helps improve efficiency by ensuring our frontline leaders get the skills, tools and processes to plan and manage their work. We have 187 leaders managing about 2,100 staff from our customer services, collections and investigations areas. The Operations Management programme enabled us to complete an extra 350,000 hours of work during the year, to the value of \$8.57 million.

Training our tax technical staff

Inland Revenue now provides advice across a wider range of topics and handles more complex customer contacts. Ensuring our people have high levels of technical knowledge is critical for delivering the services our customers need.

This year we continued to run regular tax technical training sessions. A particular highlight was our Tax Technical Conference for our senior tax technical staff. This conference helped our staff gain new knowledge into emerging tax and policy issues.

Supporting staff wellbeing

We launched a Supporting Positive Attendance initiative to support the wellbeing of our people. This initiative aims to get people to come to work ready to do their best when they are well and stay away when they are sick. The initiative has contributed to a decrease in the use of sick leave.

Keeping our people safe

Providing a safe working environment for our people is something we take very seriously. We are continually assessing our workplaces to ensure that we minimise risks and concerns so that our staff feel safe.

Where we work

We relocated 400 staff between various offices in Wellington. Half were moved into the Asteron Centre after we made better use of space in the building.

Our goal is to get our office footprint to no more than 14 m² of office space per FTE. This year we reduced our office footprint from 16.0 m² to 14.8 m² per FTE.

Risks to our business

Risk management is an important part of Inland Revenue's good governance and management practice. We use an enterprise risk management approach to managing risks across Inland Revenue. We improved our enterprise risk management policy, framework and guidelines to provide greater clarity to our decision-making processes.

A summary of our enterprise risks and associated mitigations is set out below.

We regularly review our enterprise risks to ensure the mitigation strategies are appropriate and effective.

FIGURE 3 – ENTERPRISE RISKS

Enterprise risk	Our mitigations include the following actions:
We fail to balance all-of-government strategies effectively with the delivery of our core business leading to sub-optimal outcomes	<p>We will align our long-term planning with the Government's Better Public Services goals.</p> <p>We will participate in all-of-government steering groups to understand and anticipate impending public sector changes.</p>
We are unable to source sufficient government funding to deliver our Business Transformation programme	<p>Our four-year and 10-year plans will make a compelling case for the investment we need to implement changes.</p> <p>We will present rigorous, well-considered business cases for government funding that set out the costs and benefits of proposed spending.</p> <p>Our Investment Board will provide strong governance oversight of our Business Transformation programme investments.</p>
Natural hazards such as earthquakes disrupt delivery of critical services	<p>We will identify and assess potential business impacts and regularly review our response plans, which include business impact assessments, business continuity plans, disaster recovery plans and business continuity emergency management procedures.</p>
We don't have enough experienced and qualified people to deliver the Business Transformation programme and other programmes	<p>We will develop and implement strategies to promote workforce capability, employment relations, leadership and workplace culture.</p>
The expanding availability of our information in digital form to others reduces our ability to control that information	<p>We will ensure our security policies, procedures and standards are strong and enforced.</p> <p>We will develop and monitor information-sharing protocols.</p> <p>We will align our protocols with government security and privacy standards.</p> <p>We will continue to review staff training and awareness.</p> <p>We will continue to assess our security processes and performance.</p>
Individuals and organisations represent themselves as Inland Revenue, affecting the integrity of the tax system	<p>We will keep our security incident database up to date.</p> <p>We will monitor social media and internet sites for signs of security breaches.</p> <p>We will respond rapidly to reports of misrepresentation.</p> <p>We will develop communications strategies to alert the public to scams.</p>

FIGURE 3 – ENTERPRISE RISKS (CONTINUED)

Enterprise risk	Our mitigations include the following actions:
Outdated technology and unsupported software result in systems failures that affect delivery of critical services	<p>We will continue to invest in stabilising our IT systems.</p> <p>We will invest in the upgrade of some key systems and applications.</p> <p>We will increasingly buy technology services, rather than buy technology for in-house operation.</p>
Ineffective or incomplete delivery of the Business Transformation programme reduces our ability to meet government revenue forecasts	<p>We will continue to work towards reaching our target operating model.</p> <p>Our governance boards will monitor progress of the Business Transformation programme.</p> <p>Our management will coordinate and report on progress of the Business Transformation programme.</p>
Ineffective or incomplete delivery of the Business Transformation programme reduces our ability to implement government policy	<p>We will continue to work towards reaching our target operating model.</p> <p>Our governance boards will monitor progress of the Business Transformation programme.</p> <p>Our management will coordinate and report on progress of the Business Transformation programme.</p>
Confidence among customers and stakeholders in our ability to protect their data as a result of information-sharing with government agencies results in a drop in voluntary compliance	<p>We will ensure our security policies, procedures and standards are strong.</p> <p>We will develop and monitor information-sharing protocols.</p> <p>We will align our protocols with government security and privacy standards.</p> <p>We will continue to review staff training and awareness.</p> <p>We will align our security processes with other agencies and continuously monitor performance.</p>
A downturn in the world's economy affects New Zealand's ability to fund and deliver government priorities	<p>We will continuously identify and monitor changes in overseas economic trends through research and forecasting.</p>
The changing customer profile affects voluntary compliance	<p>We will monitor and report on the effect of changes to the customer base.</p> <p>We will use research and planning to develop tailored responses to customer base changes.</p>
We lose the trust and confidence of stakeholders by not recognising or understanding how their expectations change	<p>We will continue to work closely with the Ministers' offices.</p> <p>The Executive Leadership Team will engage closely with key stakeholders.</p> <p>We will monitor and respond to changes in the integrity of the tax system.</p> <p>We will monitor and respond to emerging trends in policy and strategy.</p> <p>We will take part in forums with our key stakeholders.</p>
Complex international transactions affect our ability to collect revenue	<p>We are members of the OECD and work with overseas tax administrations to identify changes to practices.</p> <p>We are joint advisors with the Treasury in developing policy and strategies to work on complex international practices.</p>

PART 05

Measuring our performance

Our outcomes framework

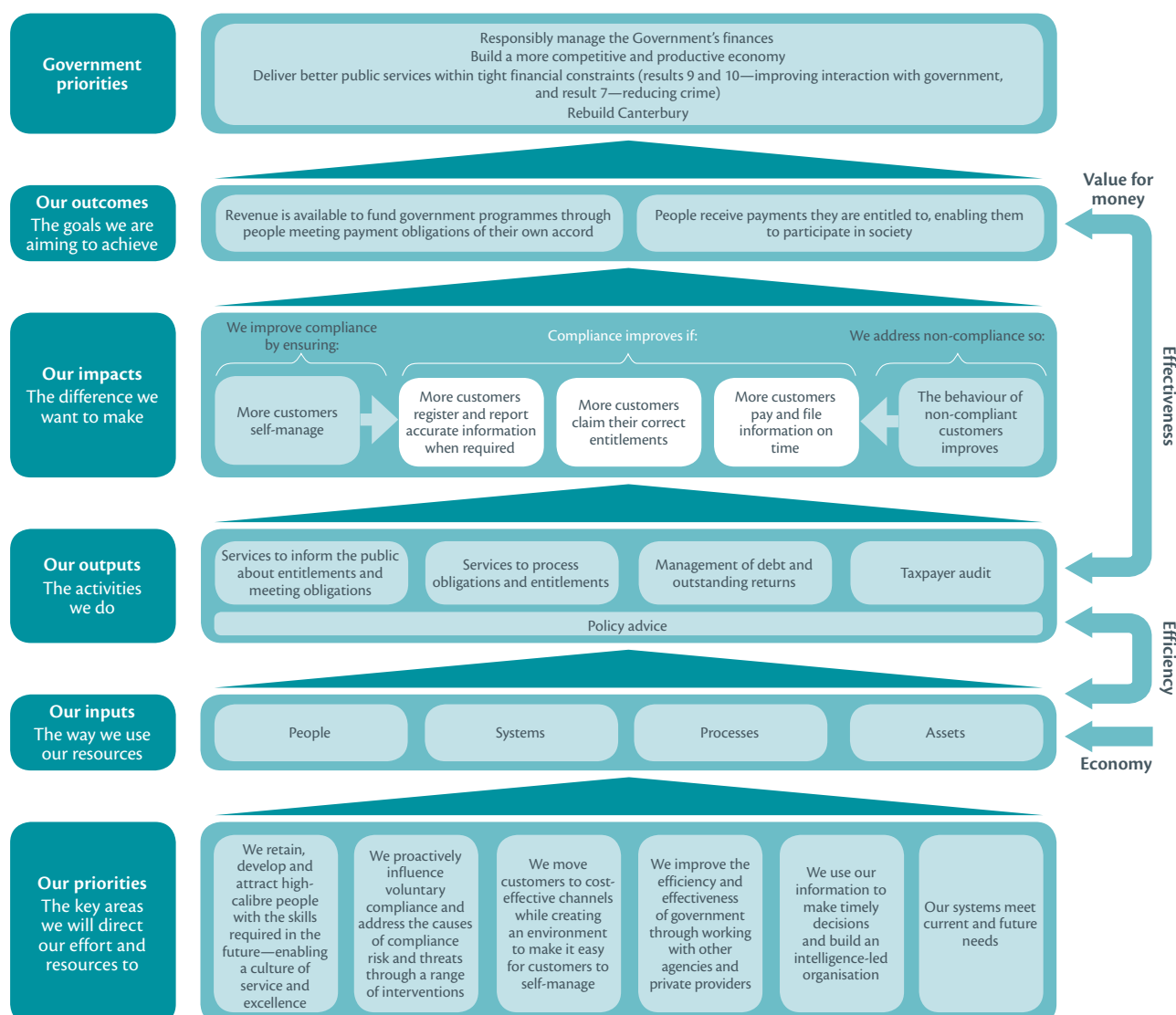
Our outcomes framework sets out what we want to achieve. It shows how we intend to organise and use our resources to deliver services to New Zealanders, and contribute to the social and economic wellbeing of New Zealand by collecting and distributing money.

We must provide the best value for money from public funds. The framework shows how we carefully consider the relationship between

our resources, outputs and impacts to ensure we stay focused on delivering value for money. Three elements contribute to this:

- Economy—getting and using our resources as economically as possible
- Efficiency—producing more for the same or less
- Effectiveness—operating in a way that achieves our outcomes.

FIGURE 4 – OUR OUTCOMES FRAMEWORK



Impact indicators

Our impacts describe the difference we want our activities and interventions to make to improve customer compliance and achieve our outcomes. We use impact indicators to measure the effectiveness of our activities on customer compliance.

We set targets that take into account our strategic intentions (including transformation goals), our operating environment (including government priorities), the economy, our resources and customer expectations.

We have refined our impact indicators, including improving measurement methodologies, and added four new

indicators to broaden our social policy coverage. See figure 5 for information on our performance and our 2016 targets.

We have 14 impact indicators and four contextual indicators that provide information on Inland Revenue's progress towards maintaining and improving customer compliance. The results show improvements in the accuracy of submitted returns, driven by lower error rates for individual income tax returns submitted electronically. On time filing and paying, customer satisfaction and perceptions levels remained high.

Social policy-related compliance levels remained stable. Two new social policy

indicators for child support were introduced this year. These were previously reported as output performance measures.

Non-compliance impact indicator results have remained high in 2013–14, except for the collectable debt to total debt ratio. This is the fourth consecutive annual decrease in this impact indicator. A lower collectable debt ratio was the result of our improved performance in reducing new debt (preventative initiatives) and collecting new debt, without a corresponding reduction to the value of non-collectable debt. This is consistent with the significant improvement on the impact indicator “% of collectable debt recovered increases”.

FIGURE 5 – OUR IMPACT INDICATORS

Impact indicator	Recent performance	Current performance	Target by June 2016
More customers are able to self-manage¹²			
% of customers who are aware of their obligations and entitlements increases	Year end June 2013: 82% ¹³	Year end June 2014: 83%	Increase to 85% or more
% of customers who find it easy to comply increases	Year end June 2013: 79% ¹⁴	Year end June 2014: 80%	Increase to 80% or more ¹⁵
Factors that influenced target setting: this impact is key to enabling improved customer compliance and cost-effectiveness in a fiscally constrained environment.			
More customers register and report accurate information when required			
% of returns filed without errors increases	Year end June 2013: 85% ¹⁶	July 2013 – March 2014: 87%	Increase to 90% or more
% of applications submitted without errors increases	Year end June 2013: 83%	Year end June 2014: 90%	Maintain at 80% or more ¹⁷
% of correct student loan deductions for NZ-based borrowers is maintained	Year end June 2013: 99% ¹⁸	July 2013 – March 2014: 99%	Maintain at 98% ¹⁹
Employer registrations follow an appropriate trend ²⁰	Year end June 2013: correlation of 99%	Year end June 2014: correlation of 98%	n/a (contextual)
GST assessed to consumer spending follows an appropriate trend ²¹	Year end March 2013: correlation of 97% ²²	Year end March 2014: correlation of 98%	n/a (contextual)
Factors that influenced target setting: this impact is key to improving customer self-management, reducing unnecessary contacts and improving end-to-end processing.			

¹² We only include results for the contextual indicator under this impact “customer compliance costs are minimised” when the data is less than two years old. The survey that this indicator uses was last undertaken in 2009 and results were included in the 2011 *Annual Report*.

¹³ Result was updated using revised methodology to enable comparison with current year. 2012–13 performance based on the previous methodology (reported in the 2013 *Annual Report*) was 78%. Satisfaction with online services is now included in this indicator.

¹⁴ Result was updated using revised methodology to enable comparison with current year. 2012–13 performance based on the previous methodology (reported in the 2013 *Annual Report*) was 69%. Satisfaction with online services is now included in this indicator.

¹⁵ Incorrect target was listed in the 2013 *Annual Report*.

¹⁶ Result updated to June 2013 (results reported in 2013 *Annual Report* were to March 2013).

¹⁷ Incorrect target was listed in the 2013 *Annual Report*.

¹⁸ This result has been measured retrospectively for 2012–13. It was a new measure introduced in 2013–14.

¹⁹ No target set in 2013–16 *Statement of Intent*. The target set in the 2014–18 *Statement of Intent* has been used.

²⁰ We report on this indicator to provide additional contextual information. Employers' correlation is between the number of employers who register for PAYE and the percentage of the labour force that is employed (from the Statistics New Zealand Household Labour Force Survey).

²¹ We report on this indicator to provide additional contextual information. This measure highlights a link between consumer spending and the amount of GST assessed, showing the completeness of information provided by GST customers. As this indicator is beyond our influence, no formal target has been set.

²² Correlation results updated as a result of Statistics New Zealand revising the historical data for gross national expenditure.

FIGURE 5 – OUR IMPACT INDICATORS (CONTINUED)

Impact indicator	Recent performance	Current performance	Target by June 2016
More customers claim their correct entitlements			
% of accurate Working for Families Tax Credits payments increases ²³	Tax year 2012: 67%	Tax year 2013: 67%	Tax year 2015: Increase to 70% or more
% of child support assessments collected increases	Year end June 2013: 74.5% ²⁴	Year end June 2014: 75%	Maintain at 75% or more
Working for Families registrations follow an appropriate trend ²⁵	Year end June 2013: correlation of 13%	Year end June 2014: correlation of 32%	n/a (contextual)
Donations rebates claimed follow an appropriate trend ²⁶	Tax year 2012: 59% ²⁷	Tax year 2013: 59%	n/a (contextual)
Factors that influenced target setting: the expected impact of the upcoming changes to Working for Families Tax Credits eligibility rules has been taken into account when assessing our ability to improve accuracy.			
More customers pay and file information on time			
% of returns filed on time increases	Tax year 2012: 83%	Tax year 2013: 83%	Tax year 2015: Increase to 85% or more
% of payments made by customers on time increases	Tax year 2012: 86%	Tax year 2013: 86% ²⁸	Tax year 2015: Increase to 90% or more
% of child support assessments paid on time increases	Year end June 2013: 63.4% ²⁹	Year end June 2014: 65%	Maintain at 68% or more
Factors that influenced target setting: this impact is a key compliance driver and consequently stretch targets are appropriate.			
The behaviour of non-compliant customers improves			
The compliance behaviour of customers who received an audit intervention improves	Year end June 2013: 85%	Year end June 2014: 86%	Maintain at 80% or more
% of collectable debt to total debt increases	Year end June 2013: 63%	Year end June 2014: 62%	Increase to 70% or more
% of collectable debt recovered increases	Year end June 2013: 10.3%	Year end June 2014: 13%	Maintain at 10% or more by year end
% of collectable debt to revenue assessed decreases	Year end June 2013: 7.1%	Year end June 2014: 6.8%	Decrease to 7.0% or less
Factors that influenced target setting: the current economic environment is a significant factor in debt performance. Maintaining or making small improvements will be challenging.			

²³ Payments are considered accurate if customers' total yearly payments are within \$1,000 of their entitlement. The accuracy of payments is primarily a reflection of the quality of information provided to us by our customers.

²⁴ This measure was reported as an output performance measure in the 2013 *Annual Report*.

²⁵ We report on this indicator to provide additional contextual information. Working for Families Tax Credits correlation is between the number of customers who receive payments from Inland Revenue and the number of households with dependent children (from the Statistics New Zealand Household Labour Force Survey). Incorrect target was listed in the 2013 *Annual Report*. Target of 80% was listed, the target should have been listed as n/a contextual.

²⁶ We report on this indicator to provide additional contextual information. A ratio between total donation claimed to Inland Revenue for taxation rebate and total donation reported to Charities Service was reported.

²⁷ This result has been measured retrospectively for 2012–13. It was a new measure introduced in 2013–14.

²⁸ Measured using provisional results. Final results will be confirmed in October 2014.

²⁹ This measure was reported as an output performance measure in the 2013 *Annual Report*.

PART 06

Statement of Service Performance

Statement of Responsibility

In terms of the Public Finance Act 1989 I am responsible, as Chief Executive of Inland Revenue, for the preparation of the department's financial statements and statements of service performance, and for the judgments made in them. I am also responsible for the preparation of the department's forecast financial statements including the appropriateness of the underlying assumptions and all other required disclosures.

I have the responsibility for establishing a system of internal control designed to provide reasonable assurance as to the integrity and reliability of financial reporting.

In my opinion, these financial statements fairly reflect the financial position and operations of the department for the year ended 30 June 2014 and the forecast financial statements reflect the financial position and operations of the department for the year ended 30 June 2015 based on Government decisions and information as at 29 April 2014.



Naomi Ferguson
Chief Executive and Commissioner
of Inland Revenue
29 September 2014

Countersigned by:



Giles Southwell
Chief Financial Officer
29 September 2014

Statement of Service Performance

For the year ended 30 June 2014

Reporting performance

Our service performance is divided into two groups:

- **Activity forecasts**—these are forecasts of expected customer demand for our services that provide context for our results. Significant variation from the forecast figures can influence the achievement of the targets set for our performance measures.
- **Performance measures**—these are measures we use to set our performance targets. They measure our performance in terms of quantity, quality, timeliness and cost.

The following sections report on our performance against our targets. Where a performance measure is expressed in terms of a range of characteristics that the output should meet, the result is reported as 'achieved' or 'not achieved' (eg, see Output Expense 5).

We have provided comments for:

- key activity forecasts where actual demand was outside the expected range
- performance measures that were not achieved
- performance measures with a positive variance greater than 10%.

Some performance measures are calculated using a sample of the customer population. We have marked these performance measures with a hash mark (#) in the "Actual" columns.

Comparative performance data

Where appropriate, we have included comparative performance information against the activity forecast and performance measures for the previous year (2012–13 actual). We have not included comparative performance information for new performance measures, or where there has been a change in the performance measure or measurement methodology that made the results incomparable. These are indicated by "n/a".

Performance context

We have included information to give context to the performance achieved. For each output expense we have included a summary of the impacts we want to contribute to. Further information about our outcomes framework can be found in Part 5. This forms part of the overall performance picture and should be read in conjunction with the activity forecasts and narrative in the other sections of this report. Our non-financial performance targets for the coming year are also included, and provide context to this year's results. These reflect those approved as part of Budget 2014 and can be found in our 2014–18 *Statement of Intent*.

Summary of service performance

Figure 6 summarises the performance measure achievement. We achieved 45 of 53 performance targets (85%) set at the start of the year, compared with 76% last year.

FIGURE 6 – PERFORMANCE TARGETS ACHIEVED

Output expense	2011–12	2012–13	2013–14
Policy advice	5 of 5	1 of 1*	1 of 3
Services to inform the public about entitlements and meeting obligations	9 of 14	12 of 18	14 of 16
Services to process obligations and entitlements	11 of 17	17 of 20	14 of 15
Management of debt and outstanding returns	6 of 12	6 of 11	8 of 11
Taxpayer audit	7 of 7	8 of 8	8 of 8
Total	38 of 55	44 of 58*	45 of 53

* This total excludes one performance measure that was not measured due to change in Minister of Revenue.

Review of 2013–14 output performance measures and targets

As in previous years, we reviewed our output measures before the start of the new financial year. The purpose of this review was to:

- create or update measures to reflect changes in our business
- remove items that were not true measures of our performance.

We have 45 measures which are comparable with last year. Our performance improved for 27 of these measures (60%), remained the same for 9 measures (20%) and deteriorated for 9 measures (20%). For 7 (78%) of the 9 measures where performance deteriorated, the change in performance between years was less than 5%.

Output expense 1 Policy advice

Description

This output expense provides policy advice services (including second opinion advice and contributions to policy advice led by other agencies) to support decision making by Ministers on government policy matters.

Performance context

The impacts we contribute to

Providing policy advice services protects and maintains the integrity of the tax system while ensuring that our tax system is as simple as possible and is internationally competitive. This contributes to achieving all of our impacts:

- More customers self-manage.

- More customers register and report accurate information when required.
- More customers claim their correct entitlements.
- More customers pay and file information on time.
- The behaviour of non-compliant customers improves.

When customers comply with their obligations and receive their entitlements we make progress towards Inland Revenue's outcomes:

- Revenue is available to fund government programmes through people meeting payment obligations of their own accord
- People receive payments they are entitled to, enabling them to participate in society.

Commentary on our performance during 2013–14

We continued to support the Government's priorities through delivering the Government's tax policy work programme.

Highlights for 2013–14 include:

- policy development for Budget 2014
- the enactment of six tax and social policy-related bills
- participation in the OECD-led international response to the global problem of base erosion and profit shifting
- entering into an intergovernmental information-sharing agreement with the United States to help New Zealand financial institutions meet the United States' Foreign Account Tax Compliance Act (FATCA) requirements
- the entry into force of:
 - the Multilateral Convention on Mutual Administrative Assistance in Tax Matters
 - new double tax agreements with Japan, Papua New Guinea, and Viet Nam
- consultation on proposals to:
 - clarify the tax rules for deregistered charities
 - improve cash flow and remove distortions on Research & Development (R&D) costs for start-up businesses
 - deal with problems around the tax deductibility of some types of business-related R&D expenditure
 - determine minimum financial reporting requirements for companies
 - clarify the GST treatment of bodies corporate.

See Part 2 for more information about our policy work.

Financial performance for the year ended 30 June 2014 (\$000)

Revenue	Expenses	Net surplus/(deficit)
8,172	8,118	54

Output 1.1 Policy advice in relation to tax and social policy

Description

This output involves:

- advising on all aspects of tax policy and social policy measures that interact with the tax system
- developing tax and social policy in line with the Generic Tax Policy Process
- drafting tax legislation for introduction in the House of Representatives and assisting its passage through the House of Representatives
- negotiating and maintaining New Zealand's network of double tax agreements with other countries
- forecasting future tax and non-tax Crown revenue receipts and disbursements for the government
- analysing revenue implications of changes in tax and social policy.

Performance measures

Measure	2012–13 Actual	2013–14 Target*	2013–14 Actual	2013–14 Variance %	2014–15 Target*
Quality					
Minimum percentage of policy advice papers that meet quality standards.	n/a	90%	73.0%	–18.9%	90%
Minimum percentage of ministerial satisfaction for policy advice.	n/a	95%	87.0%	–8.4%	95%
Cost					
Maximum average cost per hour of producing policy advice outputs.	n/a				
Original formula		\$150.00	\$97.79	34.8%	\$150.00
Updated formula [^]		\$150.00	\$112.62	24.9%	\$150.00

* These figures are not subject to audit

[^] This formula was recently updated by Treasury to align it with the amended definition of policy advice costs. Performance measures calculated using both the original and updated formulae are provided to help readers understand how this change has affected the assessment of performance.

Original formula		Updated formula
Total cost per output hour	$\frac{\text{Total policy advice costs}}{\text{Total policy output and non-policy output hours}}$	$\frac{\text{Total policy advice costs}}{\text{Total policy hours (excluding non-policy advice hours)}}$

Commentary on targets not achieved

Minimum percentage of policy advice papers that meet quality standards

This is the first year of external reporting on quality using the common performance indicators for agencies that provide policy advice. We are making improvements that were identified in the quality review.

Minimum percentage of ministerial satisfaction for policy advice

This is the first year of external reporting on ministerial satisfaction using the common performance indicators for agencies that provide policy advice. The target was deliberately set high.

Commentary on significant positive variance

Maximum average cost per hour of producing policy advice outputs.

This is the first year of external reporting for this performance measure, using the common performance indicators for agencies that provide policy advice. The maximum average cost per hour target of \$150 was set based on the best available information at the time.

Output statement: Policy advice

FOR THE YEAR ENDED 30 JUNE 2014

	2012–13 Actual	2013–14 Budget*	2013–14 Revised Budget*	2013–14 Actual	2014–15 Forecast*
	\$000	\$000	\$000	\$000	\$000
Revenue					
Crown	8,265	8,098	8,166	8,166	8,051
Other	144	2	2	6	2
Total revenue	8,409	8,100	8,168	8,172	8,053
Expenses					
Annual appropriations	7,912	8,100	8,168	8,118	8,053
Total expenses	7,912	8,100	8,168	8,118	8,053
Net surplus/(deficit)	497	–	–	54	–

* The statement of accounting policies provide explanations of these figures which are not subject to audit.

Output expense 2

Services to inform the public about entitlements and meeting obligations

Description

This output expense provides services that help taxpayers and other customers to meet their payment obligations of their own accord and to receive payments they are entitled to. This is achieved through a range of proactive and reactive services to make people aware of their entitlements and obligations, and the services available to help them comply. This output expense also contributes to confidence in the tax administration system through managing individual customer complaints quickly, fairly and in confidence. It also provides services to Ministers to enable them to discharge their portfolio responsibilities, other than those relating to policy decision-making.

Performance context

The impacts we contribute to

Providing customers with relevant information and advice, certainty in relation to the application of the law, and a choice in how they engage with us ensures that customers are aware of and understand their obligations and entitlements. This means more customers can self-manage and consequently:

- More customers register and report accurate information when required.
- More customers claim their correct entitlements.
- More customers pay and file information on time.

When customers comply with their obligations and receive their entitlements we make progress towards Inland Revenue's outcomes:

- Revenue is available to fund government programmes through people meeting payment obligations of their own accord
- People receive payments they are entitled to, enabling them to participate in society.

Commentary on performance during 2013–14

Successful peak planning and a balanced approach to managing our people across contact channels were key factors in improving our customer satisfaction and perception results this year. Satisfaction with our phone and correspondence service improved from last year and we achieved our target, while satisfaction with our online services remained high. Customers are also more confident that we are ensuring people receive their social support entitlements.

Demand for our phone service remains high and this year we have answered 90% of calls received from our customers, an improvement from 73% last year.

This year we introduced a single combined telephone timeliness measure to replace two separate measures for priority and general queues.

We also introduced a single combined correspondence timeliness measure, to replace two separate measures for electronic and paper items. Earlier in the year we had high volumes of aged correspondence on hand. As a result of a sustained effort and planning, performance in answering correspondence improved and the target was achieved in the final month of the year.

Financial performance for the year ended 30 June 2014 (\$'000)

Revenue	Expenses	Net surplus/(deficit)
266,836	248,037	18,799

Output 2.1 Information services

Description

This output involves responding to customer enquiries on tax and social support programmes (including child support and KiwiSaver) through electronic channels, correspondence, telephone, personal appointments, actively providing advice through a range of communication approaches delivered in the community and through our complaints management service.

Activity forecasts

Activity forecast	2012–13 Actual	2013–14 Forecast*	2013–14 Actual	2014–15 Forecast*
Number of customer service contacts.	6.41 million	4.70–5.20 million	5.53 million	5.70–6.30 million
Number of self-help service contacts.	17.95 million	13.40–14.80 million	26.10 million	19.20–21.20 million

* Forecasts are not subject to audit.

Commentary on demand outside forecast range

Number of customer services contacts

We are focused on improving our processing of returns, payments and entitlements, making it easier for customers to self-manage and reducing unnecessary contacts. We received more correspondence and phone contacts than forecast. However, the number of contacts reduced by 14% from last year, as we received 794,000 fewer phone calls.

Number of self-help services contacts

All types of self-help services contacts have increased this year, which reflects our efforts to encourage customers to use self-service channels

Performance measures

Measure	2012–13 Actual	2013–14 Target*	2013–14 Actual	2013–14 Variance %	2014–15 Target*
Quality					
Minimum percentage of customers who are satisfied with the quality of phone and correspondence contacts. ²⁹	82.2%#	85%	85.0%#	0%	85%
Minimum percentage of customers who are satisfied with the quality of online services.	94.5%#	90%	94.5%#	5.0%	90%
Minimum percentage of customers confident that Inland Revenue takes appropriate action to ensure people receive their social support entitlements.	70.5%#	70%	72.5%#	3.6%	70%
Quantity					
Minimum percentage of attempted calls that we answer.	73.2%	75%	89.5%	19.3%	75%
Timeliness					
Minimum percentage of telephone calls answered within two minutes.	n/a	75%	68.8%	–8.3%	75%
Minimum percentage of correspondence answered within two weeks.	n/a	75%	76.0%	1.3%	75%
Cost					
Maximum average cost of a customer initiated contact.	\$32.92	\$34.00	\$32.96	3.1%	\$40.00

Measured using a sample of the customer population.

* These figures are not subject to audit.

²⁹ Phone service surveyed for the full 12 month, and correspondence for the last quarter only.

Commentary on target not achieved

Minimum percentage of telephone calls answered within two minutes.

Several factors have affected our ability to answer calls within the two minute target. These include a 7% (51 second) increase in the average call handling time (of more than 12 minutes) compared with last year. We believe that this increase is because more customers are using self-service to answer easier questions, so our phone channel is dealing with harder questions.

We consider this to be a critical performance measure which has flow-on impacts to the overall customer experience and satisfaction.

Commentary on significant positive variance

Minimum percentage of attempted calls that we answer.

Successful planning has enabled us to improve the percentage of calls answered throughout the year.

Output 2.2 Adjudication and rulings

Description

This output involves:

Adjudication

- providing a technical review of existing taxation disputes referred to the Adjudication Unit
- issuing an adjudication report (or other formal communication of conclusions) to the parties concerned
- directing the issuing, where required, of an assessment consistent with the conclusions of the technical review.

Taxpayer Rulings

- considering applications for and providing binding private and product rulings, and financial arrangement determinations.

Public Rulings

- preparing and issuing binding public rulings
- developing and publishing non-binding statements on the Commissioner's view of the law administered by Inland Revenue eg, interpretation statements and interpretation guidelines
- considering applications for and providing taxpayer-specific depreciation determinations
- preparing and publishing depreciation and other determinations eg, livestock valuations
- considering and responding to technical correspondence.

Performance measures

Measure	2012–13 Actual	2013–14 Target*	2013–14 Actual	2013–14 Variance %	2014–15 Target*
Quality					
Percentage of all rulings reports, adjudication reports, public items and technical correspondence or advice that meet the applicable purpose, logic, alternatives, consultation and practicality standards.	100%	100%	100%	0.0%	100%
Quantity					
Minimum number of published or finalised public items that give the Commissioner's interpretation of the law.	11	25	27	8.0%	25
Timeliness					
Minimum percentage of adjudication cases completed within three months of receipt.	100%	90%	98.2%	9.1%	90%
Minimum percentage of taxpayer ruling applications that have a draft ruling completed within three months of receipt.	100%	90%	100%	11.1%	90%
Minimum percentage of non-qualifying ruling applications that have a draft ruling completed within six months of receipt.	100%	90%	100%	11.1%	90%
Minimum percentage of public items (including relevant public consultation), completed within 18 months of allocation.	100%	90%	92.0%	2.2%	90%
Minimum percentage of submissions by the applicant on any draft ruling responded to within one month of receipt.	n/a	90%	97.9%	8.8%	90%

* These figures are not subject to audit.

Commentary on significant positive variances

Minimum percentage of taxpayer ruling applications that have a draft ruling completed within three months of receipt.

Minimum percentage of non-qualifying ruling applications that have a draft ruling completed within six months of receipt.

We continue to see longer term benefits from our improved rulings processes.

Output 2.3 Government and Executive Services

Description

This output involves all activities associated with ministerial services, including responding to ministerial correspondence and parliamentary questions. It includes all tax, child support, student loan, KiwiSaver and family assistance ministerial correspondence and supply of information.

Performance measures

Measure	2012–13 Actual	2013–14 Target*	2013–14 Actual	2013–14 Variance %	2014–15 Target*
Timeliness					
Minimum percentage of ministerial correspondence responded to within 10 days.	98.0%	95%	92.7%	–2.4%	95%
Percentage of parliamentary questions responded to within required timeframes.	100%	100%	100%	0.0%	100%

* These figures are not subject to audit.

Commentary on target not achieved

Minimum percentage of ministerial correspondence responded to within 10 days.

There were a number of contributing factors in not meeting the performance target this year. At the start of the year, we received a greater number of complex items than usual, requiring further consultation. A significant increase in overall workload also affected our results.

Output statement: services to inform the public about entitlements and meeting obligations

FOR THE YEAR ENDED 30 JUNE 2014

	2012–13	2013–14	2013–14 Revised Budget*	2013–14 Actual	2014–15 Forecast*
	Actual \$000	Budget* \$000	Budget* \$000	Actual \$000	Forecast* \$000
Revenue					
Crown	254,601	265,541	265,591	265,591	249,846
Other	5,263	1,961	1,461	1,245	1,461
Total revenue	259,864	267,502	267,052	266,836	251,307
Expenses					
Annual appropriations	243,448	267,502	267,052	248,037	251,307
Total expenses	243,448	267,502	267,052	248,037	251,307
Net surplus/(deficit)	16,416	–	–	18,799	–

* The statement of accounting policies provide explanations of these figures which are not subject to audit.

Output expense 3

Services to process obligations and entitlements

Description

This output expense provides services that contribute to the availability of revenue to fund government programmes, as well as ensuring that taxpayers and other customers receive payments they are entitled to, including tax refunds. This is achieved through services designed to achieve timely, efficient and effective assessment and processing of:

- tax payments, tax credit claims and refunds for taxpayers
- entitlements for social support programmes.

Performance context

The impacts we contribute to

Accurate, timely, complete and efficient processing of notices, statements and social policy entitlements increases customers' confidence in the tax system. When customers have confidence in the tax system they are more likely to self-manage their compliance obligations. This means:

- More customers register and report accurate information when required.
- More customers claim their correct entitlements.
- More customers pay and file information on time.

When customers comply with their obligations and receive their entitlements we make progress towards Inland Revenue's outcomes:

- Revenue is available to fund government programmes through people meeting payment obligations of their own accord.
- People receive payments they are entitled to, enabling them to participate in society.

Commentary on our performance during 2013–14

This year, we have maintained strong performance across our core high transactional activities involved in return and payment processing and issuing refunds and entitlements to customers.

Peak season planning also enabled us to maintain strong service levels across all our transactional channels over the peak season, in particular in our priority activities. These priorities include activities we believe help our customers the most, such as employer monthly schedules (EMS), income tax and GST refunds, returns and regular social policy payments.

Of the 15 performance measures in this output class, results for 10 of them were either the same or improved from last year. The results for the timeliness of processing refunds and entitlements in particular have improved.

We did not achieve the timeliness target for issuing child support administrative review decisions. While we had a full year using a new measurement methodology, it became apparent that this new methodology wasn't compatible with the current timeframe requirement of issuing a decision within seven weeks. For 2014–15, we have adjusted the timeframe requirement from seven weeks to ten weeks to better reflect the true amount of time taken to issue administrative review decisions.

Financial performance for the year ended 30 June 2014 (\$000)

Revenue	Expenses	Net surplus/(deficit)
158,286	144,965	13,321

Output 3.1 Registrations, applications and processing

Description

This output involves processing all registrations, applications and assessments for the tax and social policy programmes we administer.

Activity forecasts

Activity forecast	2012–13 Actual	2013–14 Forecast*	2013–14 Actual	2014–15 Forecast*
Number of tax and social policy registrations (excluding child support) received.	726,902	680,000–750,000	689,290	690,000–765,000
Number of child support applications received.	41,268	46,000–51,000	39,849	44,000–49,000
Number of applications for administrative review of child support assessments received.	4,130	4,300–4,800	3,718	4,300–4,700
Number of returns received.	9.28 million	8.40–9.30 million	9.14 million	8.10–8.90 million
Percentage of returns filed electronically.	53.0%	55%	59.8%	60%
Percentage of income tax returns filed electronically.	84.1%	84%	86.9%	86%
Percentage of GST returns filed electronically.	47.6%	50%	54.9%	55%
Number of payments received.	8.38 million	8.10–9.00 million	8.71 million	8.40–9.30 million
Percentage of payments received electronically.	69.8%	75%	74.2%	75%

* Forecasts are not subject to audit.

Commentary on forecasts outside range or not met

Number of child support applications received

The trend of reduced volumes year-on-year has continued. While the forecast range for this year was reduced from the previous year, we did not anticipate this larger reduction. It has been further reduced for 2014–15.

Number of applications for administrative review of child support assessments received

Forecast range further reduced for 2014–15 based on current trend.

Percentage of payments received electronically

Forecast increased this year from 70% to 75%. This reflected the increasing trend, consistent with our strategy of customers opting to pay electronically.

Performance measures

Measure	2012–13 Actual	2013–14 Target*	2013–14 Actual	2013–14 Variance %	2014–15 Target*
Timeliness					
Minimum percentage of income tax returns finalised within four weeks.	94.4%	90%	94.6%	5.1%	90%
Minimum percentage of GST returns finalised within three weeks.	99.6%	95%	99.6%	4.8%	95%
Minimum percentage of employer monthly schedule employee deductions finalised within four weeks.	99.8%	95%	99.7%	4.9%	95%
Minimum percentage of social policy and tax registrations processed within five working days.	85.0%	85%	89.6%	5.4%	85%
Minimum percentage of payments banked on the day of receipt.	99.3%	99%	99.3%	0.3%	99%
Quality					
Minimum percentage of payments correctly processed to customers' accounts.	99.7%	99.5%	99.8%	0.3%	99.5%
Cost					
Maximum average cost of processing income tax returns, GST returns and employer monthly schedules.	\$3.78	\$4.00	\$3.95	1.3%	\$5.00

* These figures are not subject to audit.

Output 3.2 Statements, notices, refunds and payments

Description

This output involves:

- issuing statements, notices, rebates and refunds
- receiving and banking payments.

It covers all the tax and social policy programmes that we administer.

Performance measures

Measure	2012–13 Actual	2013–14 Target*	2013–14 Actual	2013–14 Variance %	2014–15 Target*
Quality					
Minimum percentage of notices and statements produced without error.	99.5%#	98.5%	99.4%#	0.9%	98.5%
Timeliness					
Minimum percentage of Income Tax refunds issued within six weeks.	86.2%	85%	90.2%	6.1%	85%
Minimum percentage of GST refunds issued within four weeks.	97.7%	95%	97.8%	3.0%	95%
Minimum percentage of tax credit claim payments made within three weeks.	92.7%	90%	96.1%	6.8%	90%
Minimum percentage of Working for Families Tax Credit (WfFTC) payments made on the first regular payment date following an application.	95.1%	95%	98.9%	4.1%	95%
Minimum percentage of paid parental leave payments issued to customers on the first regular pay day following the agreed date of entitlement.	97.8%	97%	98.4%	1.4%	97%

Measured using a sample of the customer population.

* These figures are not subject to audit.

Output 3.3 Child support

Description

This output involves dealing with child support assessments and providing an administrative process for reviewing child support assessments that is both inexpensive and readily accessible to custodians and paying parents.

Performance measures

Measure	2012–13 Actual	2013–14 Target*	2013–14 Actual	2013–14 Variance %	2014–15 Target*
Timeliness					
Minimum percentage of child support assessments issued within two weeks.	82.2%	80%	80.7%	0.9%	80%
Minimum percentage of child support administrative review decisions issued within seven weeks.	Not achieved ³¹	85%	55.9%	–34.2%	Measure removed
Minimum percentage of child support administrative review decisions issued within 10 weeks.	n/a	–	–	–	85%

* These figures are not subject to audit.

Commentary on target not achieved

Minimum percentage of child support administrative review decisions issued within seven weeks

This year we put in place a more relevant measurement methodology, measuring from the day we receive the review rather than from our first contact with the customer. For 2014–15 we have increased the measure timeframe to 10 weeks to better reflect the required processing time. During 2013–14 we issued 94% of decisions within 10 weeks.

Output statement: Services to process obligations and entitlements

FOR THE YEAR ENDED 30 JUNE 2014

	2012–13 Actual \$000	2013–14 Budget* \$000	2013–14 Revised Budget* \$000	2013–14 Actual \$000	2014–15 Forecast* \$000
Revenue					
Crown	102,619	112,514	137,696	137,696	119,575
Other	22,674	20,997	20,997	20,590	20,997
Total revenue	125,293	133,511	158,693	158,286	140,572
Expenses					
Annual appropriations	116,645	133,511	158,693	144,965	140,572
Total expenses	116,645	133,511	158,693	144,965	140,572
Net surplus/(deficit)	8,648	–	–	13,321	–

* The statement of accounting policies provide explanations of these figures which are not subject to audit.

³¹ The measurement methodology was reviewed during the year and we are unable to report a final achievement percentage to the level of accuracy required.

Output expense 4

Management of debt and outstanding returns

Description

This output expense provides services that contribute to the availability of revenue to fund government programmes. This involves all activities associated with collecting outstanding returns and overdue payments, taking appropriate action, and providing people with assistance on the actions they need to take to meet their obligations. This includes collection on behalf of other agencies and external parties.

Performance context

The impacts we contribute to

Using a tailored approach to our interventions, based on the PARE³² model, that reflects customers' individual circumstances and compliance behaviour should ensure that the behaviour of non-compliant customers improves. Consequently, more customers will pay and file information on time in the future.

If more customers comply with their obligations and receive their entitlements, we make progress towards Inland Revenue's outcomes:

- Revenue is available to fund government programmes through people meeting payment obligations of their own accord.
- People receive payments they are entitled to, enabling them to participate in society.

Commentary on performance during 2013–14

We conduct a range of activities to:

- collect revenue for Government
- collect overdue child support payments from parents who no longer live with their children
- help prevent customers from missing return filing deadlines and follow up when returns are overdue
- positively influence voluntary compliance.

We make earlier contact with customers when they get into debt or miss their filing deadline, and make greater use of targeted, high-volume messaging through letters and texts together with outbound calling campaigns.

Our approach towards overdue debt and returns collection with the budget funded initiatives has contributed to an increase in cash collected, slowed the growth of tax debt, improved our child support case closures and supported a continued reduction in the number of outstanding returns this year.

Focusing on early intervention has affected our ability to achieve targets for the aged proportion of collectable debt and outstanding returns. We have adjusted our aged debt target and removed the aged returns measure for next year to better align performance measures with our collections approach.

Our performance measure to finalise returns within six months achieved its target at year-end. This year we had a dedicated focus on overdue returns between July and December following the 7th July filing date. This focus has helped us achieve the performance target, to finalise returns within six months, for the first time since its introduction.

We have reduced the child support debt owed by custodial parents and contained the growth in assessment debt for liable parents. Our domestic child support portfolio has moved to "campaign approach", similar to that used by the tax debt portfolios. The "campaign approach" with early intervention as our main focus has helped increase our level of coverage. This approach has helped us achieve our "cases resolved" measure, for the first time since 2011–12. We will continue our active case management for those cases that require a greater level of focus until we receive payment in full, or a sustainable payment arrangement is in place.

Financial performance for the year ended 30 June 2014 (\$'000)

Revenue	Expenses	Net surplus/(deficit)
136,647	132,610	4,037

³² Prevention, assistance, recovery or enforcement.

Output 4.1 Outstanding returns

Description

This output involves all activities associated with collecting outstanding returns, including taking appropriate follow-up action against taxpayers who do not file a return.

Performance measures

Measure	2012–13 Actual	2013–14 Target*	2013–14 Actual	2013–14 Variance %	2014–15 Target*
Quantity					
Maximum percentage growth in outstanding returns.	–3.5%	0%	–7.1%	7.1%	0%
Maximum percentage of outstanding returns over one year old.	62.3%	57%	63.3%	–11.1%	Measure removed
Timeliness					
Minimum percentage of outstanding returns finalised within six months.	61.9%	65%	67.4%	3.7%	65%
Minimum percentage of outstanding employer monthly schedules finalised within three months.	85.6%	85%	92.0%	8.2%	85%
Cost					
Maximum average cost of finalising an outstanding return.	\$9.13	\$15.00	\$5.60	62.7%	\$15.00

* These figures are not subject to audit.

Commentary on target not achieved

Maximum percentage of outstanding returns over one year old

Our collections approach is targeting returns based on risk and assessment value, regardless of age. Based on this, our focus on newer returns has increased the proportion of older returns. This measure has been removed for 2014–15.

Commentary on significant positive variance

Maximum average cost of finalising an outstanding return

Efficiency gains through continuous improvement and managing our returns' cost has resulted in a lower cost to finalise.

Output 4.2 Overdue debt

Description

This output covers all activities associated with collecting overdue debt (excluding child support debt). It involves taking appropriate follow-up action when customers do not meet their obligations, including providing them with assistance on how they can meet their tax obligations.

Performance measures

Measure	2012–13 Actual	2013–14 Target*	2013–14 Actual	2013–14 Variance %	2014–15 Target*
Quantity					
Minimum debt value cleared, as a percentage of debt book (debt turnover).	78.3%	100%	86.6%	–13.4%	Measure removed
Maximum percentage of collectable debt value over two years old.	53.3%	50%	52.2%	–4.4%	60%
Timeliness					
Minimum percentage of debt cases resolved within three months.	65.3%	65%	66.5%	2.2%	Measure removed
Minimum percentage of debt cases resolved within six months.	n/a	–	–	–	80%
Minimum percentage of debt value resolved for those who did not have a debt at the start of the year.	68.7%	65%	73.3%	12.8%	65%
Cost					
Minimum cash collected for every debt dollar spent.	\$45.88	\$40.00	\$45.95	14.9%	\$40.00

* These figures are not subject to audit.

Commentary on targets not achieved

Minimum debt value cleared, as a percentage of debt book (debt turnover)

Our performance against this target is heavily influenced by cash received from large-value cases making use of extension-of-time arrangements. This arrangement produces a variable result, which is not indicative of our overall collections activity for the majority of cases. The measure has been removed for 2014–15.

Maximum percentage of collectable debt value over two years old

Our focus on newer debt directly affects the proportion of aged debt, although this result is an improvement on last year. The target has been increased to 60% for 2014–15. This new target is more relevant to our debt strategy, reflects the current level of debt over two years old and our success in tackling new debt.

Commentary on significant positive variances

Minimum percentage of debt value resolved for those who did not have a debt at the start of the year

Our focus on new debt has seen an improvement in the result from last year. This measure is also influenced by the degree to which extension-of-time arrangements are used by large enterprise customers.

Minimum cash collected for every debt dollar spent

This measure is influenced by the degree to which extension-of-time arrangements are used by large enterprise customers. The result is in line with last year (\$45.88), with higher cash collected and similarly increased costs being captured.

Output 4.3 Child support debt management

Description

This output involves all activities associated with the recovery of overdue child support payments. It includes taking appropriate enforcement action against non-compliers.

Performance measures

Measure	2012–13 Actual	2013–14 Target*	2013–14 Actual	2013–14 Variance %	2014–15 Target*
Timeliness					
Minimum percentage of NZ paying parent child support debt cases resolved within 12 months.	67.5%	70%	75.5%	7.9%	75%

* These figures are not subject to audit.

Output statement: Management of debt and outstanding returns

FOR THE YEAR ENDED 30 JUNE 2014

	2012–13 Actual \$000	2013–14 Budget* \$000	2013–14 Revised Budget* \$000	2013–14 Actual \$000	2014–15 Forecast* \$000
Revenue					
Crown	115,831	121,934	134,788	134,788	140,297
Other	3,886	2,962	2,962	1,859	2,962
Total revenue	119,717	124,896	137,750	136,647	143,259
Expenses					
Annual appropriations	116,251	124,896	137,750	132,610	143,259
Total expenses	116,251	124,896	137,750	132,610	143,259
Net surplus/(deficit)	3,466	–	–	4,037	–

* The statement of accounting policies provide explanations of these figures which are not subject to audit.

Output expense 5

Taxpayer audit

Description

This output expense provides services to ensure that the revenue base for funding government programmes is protected. This is achieved by verifying through audit activity, that all taxpayer groups are meeting their obligations, specifically targeting risk areas, and taking appropriate enforcement action when obligations are not being met. It also includes managing tax litigation.

Performance context

The impacts we contribute to

We use intelligence analysis to target our compliance activities to customers who are non-compliant or at risk of non-compliance. This creates an environment where customers believe we will detect non-compliance and are deterred from providing inaccurate information. It also protects the revenue base and provides certainty to customers in relation to the application of the law.

We also use our compliance activities to educate customers who are unaware of their obligations and help them get it right. We only use enforcement action where necessary. This ensures that the behaviour of non-compliant customers improves. Consequently, more customers pay and file information on time in the future.

When customers comply with their obligations and receive their entitlements we make progress towards Inland Revenue's outcomes:

- Revenue is available to fund government programmes through people meeting payment obligations of their own accord.
- People receive payments they are entitled to, enabling them to participate in society.

Commentary on performance during 2013–14

We continue to target our investigations based on risk and intelligence. This year, our return on investment was 3.9% higher than the target, with a total of over \$1.2 billion in discrepancies being assessed.

In the hidden economy area we continued targeting businesses and individuals that deliberately choose to avoid the payment of tax through under-reporting or operating outside the tax system. We identified \$49.8 million in discrepancies, 13.1% above the target of \$44 million.

In the property compliance area we identified \$52.4 million in discrepancies against the target of \$45 million. We continue to focus on individuals speculating on residential property and expanding our monitoring of property hot spots, where we monitored over 26,000 properties.

This year, in our aggressive tax planning Budget work we identified \$414.2 million of discrepancies (target \$74 million). The most significant contribution came as a result of an out-of-court settlement with Alesco New Zealand Limited over its use of optional convertible notes, which the courts had ruled to be tax avoidance. Eleven other companies agreed to be bound by the outcome of the Alesco action because of their similar use of optional convertible notes. Alesco and the other companies agreed to discrepancies of \$355.8 million.

This year we identified and prevented over \$10.4 million in fraudulent claims from being issued.

Customers' perception of how we deal with non-compliers has improved since last year, with overall customer satisfaction at the same level. We continue to work on improving quality and will be measuring satisfaction each quarter of the coming year, instead of once per annum.

Timeliness of the completion of audits across all categories is well within targets and a review of our open cases indicates these positive results will continue.

Financial performance for the year ended 30 June 2014 (\$000)

Revenue	Expenses	Net surplus/(deficit)
172,031	165,269	6,762

Output 5.1 Taxpayer audit

Description

This output involves the auditing of taxpayers including individuals, small to medium businesses and larger businesses. It includes audits of duties and non-residents.

Performance measures

Measure	2012–13 Actual	2013–14 Target*	2013–14 Actual	2013–14 Variance %	2014–15 Target*
Quality					
Minimum percentage of cases completed that are correct, complete, clear and appropriately referenced.	94.9%#	85%	95.1%#	11.9%	90%
Minimum percentage of audited customers who are satisfied with their experience.	74.4%#	65%	74.4%#	14.5%	65%
Minimum percentage of customers confident that Inland Revenue takes appropriate action against those who don't comply.	75.4%	75%	77.1%#	2.8%	75%
Minimum percentage of audits that result in a material discrepancy.	77.4%	75%	79.2%	5.6%	75%
Timeliness					
On average, we will complete audits within agreed timeframes:	Achieved	Achieved	Achieved	–	Achieved
<ul style="list-style-type: none"> • 4 months for general audits • 12 months for risk-based audits • 16 months for evasion and fraud audits • 28 months for aggressive tax planning audits. 					
Minimum percentage of disputed cases completed within 15 months.	78.5%	75%	79.1%	5.5%	75%
Cost					
Minimum discrepancy identified for every output dollar spent.	\$7.47	\$7.70	\$8.00	3.9%	\$7.00

Measured using a sample of audit cases.

* These figures are not subject to audit.

Commentary on significant positive variances

Minimum percentage of cases completed that are correct, complete, clear and appropriately referenced

This is the first year of using a new methodology to measure this achievement, and we were uncertain what results might be achieved. For 2014–15, we have increased the target to 90%.

Minimum percentage of audited customers who are satisfied with their experience

This is measured annually by surveying audited customers and is the third year of measurement. From 2014–15, we expect to carry out surveys once per quarter, which may influence our results.

Output 5.2 Litigation management

Description

This output involves the management of litigation of disputed tax cases, including the requirement to state the case through to resolution by the courts.

Performance measures

Measure	2012–13 Actual	2013–14 Target*	2013–14 Actual	2013–14 Variance %	2014–15 Target*
Quality					
Minimum percentage of litigation judgments found in favour of the Commissioner.	77.0%	66%	83.3%	26.2%	66%

* These figures are not subject to audit.

Commentary on significant positive variance

Minimum percentage of litigation judgments found in favour of the Commissioner

This achievement reflects a total of 78 judgments for the year, up from 52 judgments last year. The result relates to cases that were found fully in the Commissioner's favour (ie, in relation to all issues). With the small number of cases, any slight variation in judgments found in the Commissioner's favour can alter the percentage achieved significantly.

Output statement: Taxpayer audit

FOR THE YEAR ENDED 30 JUNE 2014

	2012–13 Actual \$000	2013–14 Budget* \$000	2013–14 Revised Budget* \$000	2013–14 Actual \$000	2014–15 Forecast* \$000
Revenue					
Crown	177,684	182,531	171,597	171,597	165,866
Other	4,477	265	265	434	265
Total revenue	182,161	182,796	171,862	172,031	166,131
Expenses					
Annual appropriations	171,769	182,796	171,862	165,269	166,131
Total expenses	171,769	182,796	171,862	165,269	166,131
Net surplus/(deficit)	10,392	–	–	6,762	–

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

PART 07

Departmental financial statements

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 30 JUNE 2014

	Notes	2012–13 Actual \$000	2013–14 Budget* \$000	2013–14 Estimated Actual* \$000	2013–14 Actual \$000	2014–15 Forecast* \$000
Income						
Revenue Crown		659,000	690,618	689,898	717,838	683,635
Other income	1	36,444	26,187	26,645	25,698	28,747
Total income		695,444	716,805	716,543	743,536	712,382
Expenditure						
Personnel	2	395,992	447,965	442,563	431,986	457,750
Operating	3	181,350	187,264	200,291	194,845	177,191
Depreciation	4	18,994	18,339	14,070	13,440	16,848
Amortisation and impairment	5	37,085	41,549	38,003	37,925	38,528
Capital charge	6	20,796	21,628	21,616	21,616	22,031
Finance costs	7	150	60	–	74	34
Total Output Expenses		654,367	716,805	716,543	699,886	712,382
Net surplus/(deficit)		41,077	–	–	43,650	–
Other comprehensive income		–	–	–	–	–
Total comprehensive income		41,077	–	–	43,650	–

The accompanying accounting policies and notes form part of these financial statements.

Explanations of significant variances against budget are detailed in note 25.

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

STATEMENT OF CHANGES IN TAXPAYERS' FUNDS

FOR THE YEAR ENDED 30 JUNE 2014

	Note	2012–13	2013–14	2013–14	2013–14	2014–15
		Actual \$000	Forecast* \$000	Estimated Actual* \$000	Actual \$000	Forecast* \$000
Balance at start of year		259,951	270,346	270,343	270,343	275,393
Total comprehensive income		41,077	–	–	43,650	–
Repayment of surplus to the Crown	8	(41,080)	–	–	(43,651)	–
Capital contribution		11,041	3,177	5,329	5,329	2,336
Capital repayment		(646)	–	(279)	(279)	–
		(30,685)	3,177	5,050	(38,601)	2,336
Balance at end of year		270,343	273,523	275,393	275,392	277,729

The accompanying accounting policies and notes form part of these financial statements.

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

STATEMENT OF FINANCIAL POSITION

AS AT 30 JUNE 2014

	Notes	2012–13	2013–14	2013–14	2013–14	2014–15
		Actual \$000	Budget* \$000	Estimated Actual* \$000	Actual \$000	Forecast* \$000
Taxpayers' funds						
Taxpayers' funds		270,343	273,523	275,393	275,392	277,729
Total taxpayers' funds		270,343	273,523	275,393	275,392	277,729
Represented by:						
Current assets						
Cash and cash equivalents		45,631	12,000	12,000	30,643	12,000
Debtor Crown		198,755	149,568	204,271	238,430	195,502
Debtors and prepayments	9	18,698	15,422	15,266	16,811	15,422
Inventories held for distribution	10	1,365	1,200	999	879	1,000
Total current assets		264,449	178,190	232,536	286,763	223,924
Non-current assets						
Prepayments	9	402	136	646	834	66
Property, plant and equipment	4	53,552	63,246	56,024	55,450	59,176
Intangible assets	5	117,126	143,171	112,015	107,853	113,487
Total non-current assets		171,080	206,553	168,685	164,137	172,729
Total assets		435,529	384,743	401,221	450,900	396,653
Current liabilities						
Creditors and other payables	11	35,385	27,200	38,595	44,303	33,200
Surplus payable to the Crown	8	41,080	–	–	43,651	–
Employee entitlements	12	46,148	43,078	46,190	47,931	43,815
Provision for other liabilities	13	1,056	116	116	53	–
Derivative financial instruments	14	3	–	–	1	–
Finance leases	15	381	253	253	386	274
Other financial liabilities	16	131	111	208	183	205
Total current liabilities		124,184	70,758	85,362	136,508	77,494
Non-current liabilities						
Employee entitlements	12	38,945	37,942	38,558	36,626	39,948
Provision for other liabilities	13	839	1,743	798	912	851
Finance leases	15	540	286	286	593	12
Other financial liabilities	16	678	491	824	869	619
Total non-current liabilities		41,002	40,462	40,466	39,000	41,430
Total liabilities		165,186	111,220	125,828	175,508	118,924
Net assets		270,343	273,523	275,393	275,392	277,729

The accompanying accounting policies and notes form part of these financial statements.

Explanations of significant variances against budget are detailed in note 25.

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 30 JUNE 2014

	Notes	2012–13	2013–14	2013–14	2013–14	2014–15
		Actual \$000	Budget* \$000	Estimated Actual* \$000	Actual \$000	Forecast* \$000
Cash flows – operating activities						
Receipts from Crown		617,131	685,811	684,382	678,163	692,404
Receipts from government departments		2,758	1,219	2,127	1,310	7,572
Receipts from third parties		34,029	25,065	24,531	21,977	21,397
Payments to employees		(400,294)	(449,184)	(442,908)	(432,522)	(458,735)
Payments to suppliers		(189,375)	(189,171)	(193,001)	(184,028)	(180,903)
Payments for capital charge		(20,796)	(21,628)	(21,616)	(21,616)	(22,031)
Goods and Services tax (net)		1,894	449	(1,292)	2,252	(1,779)
Net cash flow from operating activities	17	45,347	52,561	52,223	65,536	57,925
Cash flows – investing activities						
Receipts from sale of property, plant and equipment		1,500	–	–	114	–
Purchase of property, plant and equipment		(19,022)	(21,277)	(16,574)	(15,564)	(20,000)
Purchase of intangible assets		(29,918)	(55,979)	(32,868)	(29,102)	(40,008)
Net cash flow from investing activities		(47,440)	(77,256)	(49,442)	(44,552)	(60,008)
Cash flows – financing activities						
Capital contribution		11,041	3,177	5,329	5,329	2,336
Repayment of surplus		(5,777)	(9,100)	(41,080)	(41,080)	–
Capital repayment		(646)	–	(279)	(279)	–
Payments of finance leases		(1,434)	(382)	(382)	58	(253)
Net cash flow from financing activities		3,184	(6,305)	(36,412)	(35,972)	2,083
Net increase/(decrease) in cash and cash equivalents		1,091	(31,000)	(33,631)	(14,988)	–
Opening cash and cash equivalents		44,540	43,000	45,631	45,631	12,000
Closing cash and cash equivalents		45,631	12,000	12,000	30,643	12,000

The accompanying accounting policies and notes form part of these financial statements.

The net Goods and Services tax (GST) component of operating activities reflects the net GST paid to and received from Inland Revenue. The GST components have been presented on a net basis, as the gross amounts do not provide meaningful information for financial statement purposes.

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

STATEMENT OF COMMITMENTS

AS AT 30 JUNE 2014

	Note	2012–13 Actual \$000	2013–14 Actual \$000
Capital commitments			
Property, plant and equipment		2,406	930
Intangible assets		1,654	2,841
Total capital commitments		4,060	3,771
Operating commitments			
<i>Non-cancellable accommodation leases</i>			
Not later than one year		27,755	32,642
Later than one year and not later than five years		88,537	115,685
Later than five years		86,548	77,667
Total operating commitments		202,840	225,994
Total commitments	18	206,900	229,765

The accompanying accounting policies and notes form part of these financial statements.

STATEMENT OF CONTINGENT LIABILITIES AND CONTINGENT ASSETS

AS AT 30 JUNE 2014

	Note	2012–13 Actual \$000	2013–14 Actual \$000
Contingent liabilities			
Legal proceedings and disputes – taxpayer		1,097	843
Personal grievances		33	30
Total contingent liabilities	19	1,130	873
Contingent assets			
Legal proceedings and disputes – taxpayer		3,486	2,867
Total contingent assets	19	3,486	2,867

The accompanying accounting policies and notes form part of these financial statements.

STATEMENT OF DEPARTMENTAL EXPENSES AND CAPITAL EXPENDITURE AGAINST APPROPRIATIONS

FOR THE YEAR ENDED 30 JUNE 2014

	2012–13 Expenditure ¹	2013–14 Budget*	2013–14 Revised Budget** ²	2013–14 Expenditure ¹	2014–15 Forecast*
	\$000	\$000	\$000	\$000	\$000
Vote: Revenue					
<i>Output expenses</i>					
Policy advice	7,912	8,100	8,168	8,118	8,053
Services to inform the public about entitlements and meeting obligations	243,448	267,502	267,052	248,037	251,307
Services to process obligations and entitlements	116,645	133,511	158,693	144,965	140,572
Management of debt and outstanding returns	116,251	124,896	137,750	132,610	143,259
Taxpayer audit	171,769	182,796	171,862	165,269	166,131
Total departmental output expenses¹	656,025	716,805	743,525	698,999	709,322
Services to other agencies RDA ³	–	–	710	555	3,060
Total output expenses	656,025	716,805	744,235	699,554	712,382
Other expenses – administration and use of another department's appropriation	–	–	1,308	973	–
Total expenditure	656,025	716,805	745,543	700,527	712,382
<i>Departmental capital expenditure</i>					
Property, plant and equipment	19,022	21,277	17,000	15,564	20,000
Intangible assets	29,918	55,723	38,000	29,127	42,336
Total departmental capital expenditure	48,940	77,000	55,000	44,691	62,336

¹ Excludes remeasurement of \$641,000 (2012–13, \$1,658,000).

² Includes adjustments made in the Supplementary Estimates and transfers under the Public Finance Act 1989.

³ Revenue-dependent appropriation (RDA). The amount of an RDA is limited to the amount of revenue earned.

The accompanying accounting policies and notes form part of these financial statements.

Explanations of significant variances against budget are detailed in note 25.

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

STATEMENT OF UNAPPROPRIATED EXPENSES AND CAPITAL EXPENDITURE

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FOR THE YEAR ENDED 30 JUNE 2014

In the 2013–14 financial year there were no instances of:

- expenses and capital expenditure incurred in excess of appropriation (2012–13, \$nil).
- expenses and capital expenditure incurred without appropriation or other authority, or outside scope of appropriation (2012–13, \$nil).

In the 2013–14 financial year there were no breaches of the projected departmental net asset schedule (2012–13, \$nil).

The accompanying accounting policies and notes form part of these financial statements.

Statement of accounting policies

These financial statements include financial statements for the year ended 30 June 2014 and forecast financial statements for the year ended 30 June 2015. The statements have been combined to provide a single view of budget, actual and forecast information.

References to the financial statements incorporate the forecast financial statements, unless otherwise stated.

REPORTING ENTITY

Inland Revenue is a government department as defined by section 2 of the Public Finance Act 1989 and is domiciled in New Zealand. It is a wholly owned entity of the Crown whose primary objective is to provide services to the public rather than making a financial return. Accordingly, Inland Revenue has designated itself as a Public Benefit Entity (PBE) for the purpose of New Zealand equivalents to International Financial Reporting Standards (NZ IFRS PBE).

REPORTING PERIOD

The reporting period for these financial statements is for the year ended 30 June 2014. The forecast financial statements are for the year ended 30 June 2015.

The financial statements were authorised for issue by the Chief Executive of Inland Revenue on 29 September 2014.

STATEMENT OF COMPLIANCE

The financial statements have been prepared in accordance with the requirements of the Public Finance Act 1989, which includes the requirement to comply with New Zealand generally accepted accounting practice (NZ GAAP), and Treasury Instructions. These financial statements have been prepared in accordance with NZ GAAP. They comply with NZ IFRS (PBE), and other applicable financial reporting standards, as appropriate for public benefit entities.

BASIS OF PREPARATION

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

These financial statements have been prepared on a historical cost basis, unless otherwise stated. The accrual basis of accounting has been used, unless otherwise stated.

These financial statements are presented in New Zealand dollars, and all values are rounded to the nearest thousand dollars (\$000). The functional currency of Inland Revenue is New Zealand dollars.

JUDGEMENTS AND ESTIMATIONS

In preparing these financial statements, judgements, estimates and assumptions have been made concerning the future. These estimates and their associated assumptions may differ from the subsequent actual results. Estimates and assumptions are continually evaluated and are based on experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Revisions to accounting estimates are recognised in the period the estimate is revised in if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year are related to retiring and long-service leave.

An analysis is provided in Note 12 of the exposure in relation to estimates and uncertainties surrounding retiring and long-service leave liabilities.

Finance leases

Determining whether a lease agreement is a finance lease or an operating lease requires judgement as to whether the agreement transfers substantially all the risks and rewards of ownership to Inland Revenue. Judgement is required on various aspects that include, but are not limited to, the fair value of the leased asset, the economic life of the leased asset, whether or not to include renewal options in the lease term, and determining an appropriate discount rate to calculate the present value of the minimum lease payments. Classification as a finance lease means the asset is recognised in the *Statement of Financial Position* as property, plant and equipment, whereas with an operating lease no such asset is recognised.

Inland Revenue has exercised its judgement on the appropriate classification of equipment leases, and has determined that one of these arrangements included a finance lease.

STANDARDS AND INTERPRETATIONS ISSUED AND NOT YET ADOPTED

The External Reporting Board (XRB) was given the responsibility for issuing accounting standards on 1 July 2011. Prior to that date the Accounting Standards Review Board (ASRB) issued standards. The XRB is a legal continuation of the ASRB. All accounting standards on issue on 30 June 2011 have been carried across to the XRB.

The Minister of Commerce has approved a new Framework (incorporating a Tier Strategy) developed by the External Reporting Board. Under this Framework, Inland Revenue is classified as a Tier 1 reporting entity and it will be required to apply full PBE accounting standards. These standards are being developed by the External Reporting Board based on current International Public Sector Accounting Standards (IPSAS). The effective date for the new standards for public sector entities is for reporting periods beginning on or after 1 July 2014. This means Inland Revenue will transition to the new standards in preparing its 30 June 2015 financial statements.

The forecast financial statements for the 2014–15 year have been prepared in accordance with public sector PBE Accounting Standards (PBE IPSAS). This is a change from actual and budget figures as at 30 June 2014 which were prepared in accordance with NZ IFRS (PBE) as appropriate for public benefit entities. At this stage we have not identified any material changes between these standards that will impact the Forecast Financial Statements. A detailed assessment will be performed shortly for PBE IPSAS.

There are no new relevant standards and interpretations issued this year and Inland Revenue has not early adopted any new standards and interpretations.

ACCOUNTING POLICIES

The following accounting policies, which materially affect the measurement of financial results, financial position, and output statements within the *Statement of Service Performance* have been applied.

Budget and forecast figures

The Budget figures for 2013–14 are those included in *The Estimates of Appropriations for the year ending 30 June 2014*.

The Revised Budget figures for 2013–14 are those included in *The Supplementary Estimates of Appropriations and Supporting Information for the year ending 30 June 2014*.

The Estimated Actual figures for 2013–14 and the Forecast figures for 2014–15 are those included in *The Estimates of Appropriations for the year ending 30 June 2015*. The Estimated Actual figures represent forecasts submitted to Treasury based on all Government decisions and assumptions as at 29 April 2014.

No changes were made to the 2014–15 forecast figures in the *Pre-election Economic and Fiscal Update (PREFU) 2014*.

The Budget, Revised Budget, Estimated Actual and Forecast figures have been prepared in accordance with NZ GAAP, using accounting policies that are consistent with those adopted in preparing these financial statements.

GST

All items in the financial statements, including appropriation statements, are stated exclusive of GST, except for “debtor Crown”, “net debtors” and “accounts payable”, which are stated on a GST-inclusive basis. Where GST is not recoverable as input tax, it is recognised as part of the related asset or expense.

The net amount of GST owing to or from Inland Revenue at balance date, being the difference between output GST and input GST, is included in “creditors and other payables” or “debtors and prepayments” in the *Statement of Financial Position*.

The net GST paid to or received from Inland Revenue, including the GST relating to investing and financing activities, is classified as an operating cash flow in the *Statement of Cash Flows*.

Commitments and contingencies are disclosed exclusive of GST.

Income tax

Government departments are exempt from income tax as public authorities, so accordingly, no charge for income tax has been provided for.

Revenue

Revenue is measured at the fair value of consideration received or receivable. Revenue is recognised as follows:

Revenue Crown

Revenue earned from the supply of outputs to the Crown is recognised as revenue when earned.

Sale of services

Sale of services are recognised in the accounting period the services are provided in, by reference to completion of specific transactions, assessed on the basis of actual services provided as a proportion of the total services to be provided.

Revenue from recoveries

Revenue from recoveries is recognised as revenue when earned.

Sub-leases

Income from sub-leased property is recognised in the *Statement of Comprehensive Income* on a straight-line basis over the term of the lease.

Insurance proceeds

Insurance claim proceeds are recognised as revenue when the claim has been accepted by the insurer or when receipt of the insurance proceeds is considered virtually certain. The insurance proceeds will be disclosed as a contingent asset if the receipt is only probable.

Cost allocations

Inland Revenue uses an integrated cost allocation process to derive the cost of its outputs. This process involves the initial costing of business processes followed by the full costing of outputs.

Business processes represent Inland Revenue's key functional activities. These business processes are used to capture direct costs.

Direct personnel costs are charged to business processes, based on actual hours and standard activity rates. Other related direct costs, including depreciation, are allocated to business processes, based on planned hours or relevant activity drivers.

Premises lease costs are charged to business processes based on headcount or relevant activities.

Other indirect costs and corporate overheads that cannot be attributed directly to a business process are apportioned to outputs, based on planned business process activity allocation to outputs.

There have been no material changes in cost accounting policies since the date of the last audited financial statements.

Capital charge

The capital charge is recognised as an expense in the period to which the charge relates.

Leases

A lease is classified as a finance lease if it transfers substantially all the risks and rewards of ownership of an asset, whether or not title is eventually transferred. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to the ownership of an asset.

Operating leases

Rentals payable under operating leases are recognised as an expense on a straight-line basis over the term of the relevant lease. Lease incentives received as incentive to enter into an operating lease are also recognised evenly over the term of the lease as a reduction in the rental expense.

Contractual arrangements considered to be operating leases have been recognised during the reporting period.

Finance leases

At the commencement of the lease term, finance leases are recognised as assets and liabilities in the *Statement of Financial Position* at the lower of the fair value of the leased item or the present value of the minimum lease payments.

The finance charge is charged to the surplus or deficit over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability.

The amount recognised as an asset is depreciated over its useful life. If there is no certainty as to whether Inland Revenue will obtain ownership at the end of the lease term, the asset is fully depreciated over the shorter of the lease term and its useful life.

Contractual arrangements considered to be finance leases have been recognised during the reporting period.

Financial instruments

Financial assets

Inland Revenue classifies its financial assets into two categories: financial assets at fair value through surplus or deficit, and debtors and receivables. The classification depends on the purpose for which the assets were acquired.

a) Financial assets at fair value through surplus or deficit

Financial assets designated at fair value through surplus or deficit are recorded at fair value with any realised and unrealised gains or losses recognised in the *Statement of Comprehensive Income*. Gains or losses from foreign exchange and other fair value movements are separately reported in the *Statement of Comprehensive Income*. Transaction costs are expensed as they are incurred. Derivatives (e.g., foreign currency forward exchange contracts) are classified under this category.

Derivative financial instruments are recognised both initially on the date a derivative contract is entered into and subsequently at fair value at each balance date. They are reported as either assets or liabilities, depending on whether the derivative is in a net gain or net loss position, respectively. The fair value gains or losses on derivatives are recognised in the *Statement of Comprehensive Income*.

b) Debtors and receivables

Debtors and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are recognised initially at fair value plus transaction costs and subsequently measured at amortised cost using the effective interest rate method. Debtors and receivables issued with durations of less than 12 months are recognised at their nominal value, unless the effect of discounting is material.

Impairment of financial assets

Allowances for estimated irrecoverable amounts are recognised when there is objective evidence that Inland Revenue will not be able to collect all amounts due according to the original terms of the receivable. Significant financial difficulties of the debtor, probability that the debtor will enter into bankruptcy, and default in payments are considered indicators that the debtor is impaired.

The amount of the provision is the difference between the asset's carrying amount and the estimated impaired value. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the impairment loss is recognised in the *Statement of Comprehensive Income*.

Financial liabilities

Inland Revenue classifies its financial liabilities into two categories: financial liabilities at fair value through surplus or deficit, and financial liabilities measured at amortised cost. The classification depends on the purpose for which the liabilities were incurred.

a) Financial liabilities at fair value through surplus or deficit

Financial liabilities designated at fair value through surplus or deficit are recorded at fair value with any realised and unrealised gains or losses recognised in the *Statement of Comprehensive Income*. Gains or losses from foreign exchange and other fair value movements are reported separately in the *Statement of Comprehensive Income*. Transaction costs are expensed as they are incurred. Derivatives (e.g., foreign currency forward exchange contracts) are classified under this category.

b) Financial liabilities measured at amortised cost

Financial liabilities measured at amortised cost are recognised initially at fair value less transaction costs and subsequently measured at amortised cost using the effective interest rate method. Financial liabilities entered into with durations of less than 12 months are recognised at their nominal value, unless the effect of discounting is material. "Creditors and other payables" are recognised at their nominal value as the effect of discounting is immaterial.

Cash and cash equivalents

Cash and cash equivalents include all cash held in the bank accounts. All cash held in bank accounts is held in "on demand" accounts and no interest is payable to Inland Revenue.

Inventories held for distribution

Inventories held for distribution comprise forms, booklets and returns held for distribution to the public at no or nominal consideration in the ordinary course of operations.

Inventories held for distribution for public benefit purposes are carried at cost, calculated using the first-in, first-out (FIFO) cost method, adjusted where applicable for any loss of service potential. The cost of inventories includes all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. Where inventories are acquired at no cost, or for nominal consideration, the cost is deemed to be the current replacement cost at the date of acquisition.

The carrying amount is recognised as an expense in the period in which the goods are distributed. The amount of any write-down of inventories and all losses of inventories is recognised as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories is recognised as a reduction in the amount of inventories recognised as an expense in the period the reversal occurs in.

Hedge accounting, hedging activities and foreign currency transactions

Inland Revenue's activities expose it primarily to risks of changes in foreign exchange rates. Inland Revenue uses derivative financial instruments (primarily, foreign currency forward exchange contracts) to mitigate its risks associated with foreign currency

fluctuations relating to certain commitments. The use of financial derivatives is governed by Inland Revenue's foreign exchange policy, which provides written principles on the use of financial derivatives consistent with Inland Revenue's risk management strategy.

Inland Revenue does not hold or issue derivative financial instruments for trading purposes. It also has not adopted hedge accounting.

Foreign currency transactions (including those for which forward exchange contracts are held) are translated into New Zealand dollars using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions are recognised in the *Statement of Comprehensive Income*.

Property, plant and equipment

Inland Revenue has operational assets that include IT equipment, furniture and office equipment, motor vehicles, and leasehold improvements. The capitalisation thresholds are:

- | | |
|--|--|
| • IT equipment – desktop computers and laptops | all |
| • IT equipment – other | \$2,000 and over (or \$20,000 for bulk purchased IT equipment) |
| • Furniture and office equipment | \$2,000 and over (or \$20,000 for bulk purchased furniture) |
| • Motor vehicles | \$2,000 and over |
| • Leasehold improvements | \$20,000 and over |

Property, plant and equipment are shown at historical cost, less accumulated depreciation and impairment losses. Historical cost is the value of consideration given to acquire or create the asset and any directly attributable costs of bringing the asset to working condition for its intended use.

Additions

The cost of an item of property, plant and equipment is recognised as an asset if it is probable that future economic benefits or service potential associated with the item will flow to Inland Revenue and the cost of the item can be measured reliably. In most instances, an item of property, plant and equipment is recognised at its cost. Where an asset is acquired at no cost, or for a nominal cost, it is recognised at fair value as at the date of acquisition.

Subsequent costs

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits or service potential associated with the item will flow to Inland Revenue and the cost of the item can be measured reliably. All repairs and maintenance are charged to the *Statement of Comprehensive Income* during the financial period in which they are incurred.

Depreciation

Depreciation is provided on a straight-line basis on all property, plant and equipment, other than assets under construction. The rate of depreciation will write off the cost of the asset to the estimated residual value over the useful life of the asset. The useful life of major classes of assets have been estimated as follows:

- IT equipment 3 to 6 years
- Furniture and office equipment 5 to 7 years
- Motor vehicles 5 to 7 years
- Leasehold improvements up to 10 years

All fixed assets other than motor vehicles are assumed to have no residual value. Motor vehicles are assumed to have a 20% residual value.

The cost of leasehold improvements is capitalised and depreciated over the unexpired period of the lease, or the estimated remaining useful life of the improvements, whichever is shorter, up to a maximum of 10 years.

Assets under construction are not depreciated. The total cost of a capital project is transferred to the appropriate asset class on its completion and then depreciated.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance date.

Impairment

Property, plant and equipment that has a finite useful life is reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If any indication of impairment exists, the recoverable amount is estimated to determine the extent of the impairment loss, if any.

If an asset's recoverable amount is less than its carrying amount, the asset is impaired and it will be reported at its recoverable amount. The impairment loss is recognised in the *Statement of Comprehensive Income*.

The reversal of an impairment loss is also recognised in the *Statement of Comprehensive Income*.

Disposals

Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These are included in the *Statement of Comprehensive Income*.

Intangible assets

Inland Revenue has intangible assets in the form of software, licences and business process design.

Additions

Intangible assets are initially recorded at cost. Inland Revenue only has intangible assets with finite useful lives. The three main categories are: software – developed, software and licences – purchased and business process design.

a) Software – developed

The cost of an internally generated intangible asset represents expenditure incurred in the development phase of the asset only. The cost of developed computer software comprises direct labour, material purchased and an appropriate portion of relevant overheads. These costs are directly associated with the development of identifiable and unique software controlled by Inland Revenue, and will generate future economic benefits.

Expenditure incurred on research of an internally generated intangible asset is expensed when it is incurred. Where the research phase cannot be distinguished from the development phase, the expenditure is expensed when it is incurred.

Costs associated with maintaining computer software programmes are recognised as an expense when incurred. Costs of configuring and customising purchased software for intended use are capitalised.

Staff training costs are recognised as an expense when incurred.

b) Software and licences – purchased

Intangible assets acquired by Inland Revenue such as computer software and licences are stated at cost less accumulated amortisation and impairment losses. Acquired computer software and licences are capitalised on the basis of costs incurred to acquire and bring to use the specific software.

Costs associated with maintaining computer software programmes are recognised as an expense when incurred. Costs of configuring and customising purchased software for intended use are capitalised.

c) Business process design

Expenditure on development activities, where research findings are applied to a plan or design for new or substantially improved business processes, is capitalised if the business process is technically and commercially feasible and Inland Revenue has sufficient resources to complete development. Other development expenditure is recognised in the *Statement of Comprehensive Income* as an expense as incurred.

The capitalisation thresholds for intangible assets are:

- Software – developed \$50,000 and over
- Software and licences – purchased \$5,000 and over
- Business process design \$50,000 and over

Subsequent cost

The cost of intangible assets with finite lives is subsequently recorded at cost less any amortisation and impairment losses.

Amortisation

The carrying value of an intangible asset with a finite life is amortised on a straight-line basis over its estimated useful life. Amortisation begins when the asset is available for use and ceases at the date that the asset is de-recognised. The amortisation charge for each period is recognised in the *Statement of Comprehensive Income*.

The useful lives of major classes of intangible assets have been estimated as follows:

- | | |
|-------------------------------------|---------------|
| • Software – developed | 5 to 10 years |
| • Software and licences – purchased | 5 to 10 years |
| • Business process design | 5 to 10 years |

Assets under construction are not amortised. The total cost of a capital project is transferred to the appropriate asset class on its completion and then amortised.

Impairment

Intangible assets including assets under construction are reviewed for impairment at each balance date. If any indication of impairment exists, the recoverable amount is estimated to determine the extent of the impairment loss, if any.

If an intangible asset's recoverable amount is less than its carrying amount, the asset is impaired and it will be reported at its recoverable amount. The impairment loss is recognised in the *Statement of Comprehensive Income*.

The reversal of an impairment loss is also recognised in the *Statement of Comprehensive Income*.

De-recognition

The gain or loss arising from the de-recognition of an intangible asset is recognised in the *Statement of Comprehensive Income* when the asset is de-recognised.

Employee entitlements

Short-term entitlements

Employee entitlements that Inland Revenue expects to be settled within 12 months of balance date are measured at nominal values based on accrued entitlements at current rates of pay. These include salaries and wages accrued up to balance date, annual leave and time off in lieu earned up to but not yet taken at balance date, retiring, long-service leave and sick leave entitlements expected to be settled within 12 months.

Inland Revenue recognises a liability for sick leave to the extent that absences in the coming year are expected to be greater than the sick leave entitlements earned in the coming year. The amount is calculated based on the unused sick leave entitlement that can be carried forward at balance date, to the extent that Inland Revenue anticipates it will be used by staff to cover those future absences.

Inland Revenue recognises a liability and an expense for bonuses where it is contractually obliged to pay them, or where a past practice has created a constructive obligation.

Long-term entitlements

Employee entitlements that are payable beyond 12 months such as long-service leave and retiring leave have been calculated on an actuarial basis.

The actuarial calculations for long-service leave and retiring leave liabilities are based on:

- Employee contractual entitlements.
- Years of service accrued to balance date and years remaining to entitlement.
- Present value of the estimated future cash outflows using an applicable discount rate and salary inflation rate.

Superannuation schemes

Obligations for contributions to the Inland Revenue Superannuation Scheme, State Sector Retirement Savings Scheme, KiwiSaver and the Government Superannuation Fund are accounted for as defined contribution schemes and are recognised as an expense in the *Statement of Comprehensive Income* as they fall due.

Termination benefits

Termination benefits are payable when an employee's employment contract is terminated before their normal retirement or when an employee accepts voluntary redundancy in exchange for these benefits. Inland Revenue recognises the expenditure in the *Statement of Comprehensive Income* when it is demonstrably committed to either terminate the employment of current employees, according to a detailed formal plan without the possibility of withdrawal, or as a result of an offer for voluntary redundancy.

Termination benefits to be settled within 12 months are reported at the amount expected to be paid, otherwise they are reported as the present value of the estimated future cash outflows.

Provisions

Inland Revenue recognises a provision for future expenditure of uncertain amounts or timing where there is a present obligation (either legal or constructive) as a result of a past event, and it is probable that expenditure will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Provisions are not recognised for future operating losses.

Provisions are recorded at the best estimate of the expenditure required to settle the obligation. Provisions to be settled beyond 12 months are recorded at their present value.

Taxpayers' funds

This is the Crown's net investment in Inland Revenue. It is measured as the difference between total assets and total liabilities. Taxpayers' funds are disaggregated and classified into a number of components:

- Capital contribution
- Capital repayment
- Repayment of surplus to the Crown

Statement of Cash Flows

Cash and cash equivalents mean cash balances in bank accounts.

Operating activities include cash received from all income sources of Inland Revenue, and cash payments made for the supply of goods and services.

Investing activities are those activities relating to the acquisition and disposal of non-current assets.

Financing activities comprise capital injections by, or repayment of capital to, the Crown.

Commitments

Expenses and liabilities yet to be incurred on non-cancellable contracts that have been entered into on or before balance date are disclosed as commitments to the extent that they are unperformed obligations.

Contingent liabilities and assets

Contingent liabilities and assets are recorded in the *Statement of Contingent Liabilities and Contingent Assets* at the point at which the contingency is evident. Contingent liabilities are disclosed if the possibility that they will crystallise is not remote. Contingent assets are disclosed if it is probable that the benefits will be realised. Insurance claim proceeds will be disclosed as a contingent asset if the receipt of the insurance proceeds is probable.

Comparatives

Certain comparative information has been reclassified, where required, to conform with the current year's presentation.

CHANGES IN ACCOUNTING POLICIES

For the preparation of the department's financial statements and statements of service performance as at 30 June 2014 there have been no changes in accounting policies and cost allocation policies since the date of the last audited financial statements. All policies have been applied on a basis consistent with the previous year.

The forecasts for the 2014–15 year have been prepared in accordance with PBE IPSAS. This is a change from actual and budget figures as at 30 June 2014 which were prepared in accordance with NZ IFRS (PBE) as appropriate for public benefit entities. At this stage we have not identified any material changes between these standards that will impact the Forecast Financial Statements.

FORECAST FINANCIAL STATEMENTS

The forecast financial statements have been prepared in accordance with the Public Finance Act 1989.

The purpose of the forecast financial statements is to facilitate Parliament's consideration of appropriations for, and planned performance of, the department. These forecast financial statements may not be appropriate for other purposes.

The forecast financial statements have been prepared in accordance with the accounting policies detailed above. Additional accounting policies relating to the forecasts are set out below.

The forecast financial statements comply with NZ GAAP and have been prepared in accordance with Financial Reporting Standard 42: Prospective Financial Statements.

Forecast Policies

The forecasts have been compiled on the basis of existing government policies and ministerial expectations at the time the statements were finalised and reflect all government decisions and circumstances as at 29 April 2014.

The main assumptions are as follows:

- The department's main activities will remain substantially the same as for the previous year.
- Operating costs are based on historical experience. The general historical pattern is expected to continue.
- Estimated year-end information for 2013–14 is used as the opening position for the 2014–15 forecasts.

These assumptions are adopted as at 29 April 2014.

Variations to forecast

The actual financial results for the forecast period covered are likely to vary from the information presented in these forecasts. Factors that may lead to a material difference between information in these forecast financial statements and the actual reported results include:

- Changes to the budget through initiatives approved by Cabinet.
- Technical adjustments to the budget including transfers between financial years.
- The timing of expenditure relating to significant programmes and projects.

Any changes to budgets during 2014–15 will be incorporated into *The Supplementary Estimates of Appropriations for the year ending 30 June 2015*.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1: OTHER INCOME

	2012–13 Actual \$000	2013–14 Actual \$000	2014–15 Forecast* \$000
Accident Compensation Corporation (ACC) – agency fees	20,500	20,500	20,500
Court costs recovery	3,178	2,081	2,828
Rulings	781	1,061	1,088
Services on behalf of other government agencies	–	1,009	–
Support services to other government agencies	–	555	3,060
Sub-leases	252	475	1,100
Secondment to other agencies – salary recovery	150	–	–
Net gains on property, plant and equipment	476	1	–
Insurance proceeds	9,101	–	–
Net gains on derivative financial instruments	1,943	–	–
Supply of information to other agencies	13	13	170
Other	50	3	1
Total other income	36,444	25,698	28,747

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

NOTE 2: PERSONNEL

	2012–13 Actual \$000	2013–14 Actual \$000	2014–15 Forecast* \$000
Salaries and wages	350,352	371,178	395,310
Contractors and temporary staff	26,578	37,489	39,926
Employer contributions to defined contribution plans	9,816	11,745	11,952
Terminating benefits	948	1,926	2,051
ACC levies	1,224	1,536	1,714
Annual leave	1,160	1,114	759
Retiring, long-service and sick leave	2,704	242	3,000
Bonuses	192	258	275
Other	3,018	6,498	2,763
Total personnel	395,992	431,986	457,750

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

NOTE 3: OPERATING

	2012–13 Actual \$000	2013–14 Actual \$000	2014–15 Forecast* \$000
Information technology costs	43,549	50,545	50,312
Accommodation lease rentals	30,223	31,471	33,280
Consultants	26,223	23,348	13,763
Printing and postage	17,901	17,943	18,623
Communication	14,195	15,845	15,404
Premises costs	8,747	9,505	8,120
Travel and transport	7,934	9,027	7,905
Legal expenses	5,723	8,568	8,642
Staff development	6,566	6,882	6,860
Office supplies	3,392	3,604	3,435
Bank fees	3,437	3,400	3,241
Realised foreign exchange losses	1,447	2,310	106
Advertising and publicity	2,368	1,881	2,086
Equipment maintenance	1,739	1,780	1,297
Audit fees for audit of the financial statements	1,033	1,033	1,100
Disbursements for audit of the financial statements	55	20	–
Fees to Audit NZ for other services	13	30	–
Bad debts written off	26	18	–
Net loss on disposal of intangible assets	–	478	–
Net loss on disposal of property, plant and equipment	–	87	8
Inc/(Dec) in provision for debt impairment	–	–	9
Inc/(Dec) in provision for onerous leases	(391)	–	–
Other operating expenses	7,170	7,070	3,000
Total operating	181,350	194,845	177,191

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

NOTE 4: PROPERTY, PLANT AND EQUIPMENT BY CATEGORY

	IT equipment \$000	Furniture and office equipment \$000	Motor vehicles \$000	Leasehold improvements \$000	Assets under construction – leasehold \$000	Total \$000
Cost						
Balance as at 1 July 2013	65,621	29,298	4,904	53,003	4,334	157,160
Additions by purchase	4,935	1,437	–	8,388	184	14,944
Other movements ¹	–	–	–	(175)	–	(175)
Transfers between category	25	–	–	3,905	(3,112)	818
Disposals	(13,910)	(11)	(309)	(3,110)	–	(17,340)
Balance as at 30 June 2014	56,671	30,724	4,595	62,011	1,406	155,407
Depreciation and impairment losses						
Balance as at 1 July 2013	54,952	21,190	1,123	26,343	–	103,608
Depreciation charge – expensed	6,100	2,638	547	4,455	–	13,740
Depreciation charge – capitalised ²	12	11	–	–	–	23
Impairment reversals	–	(300)	–	–	–	(300)
Transfers between category	–	–	–	–	–	–
Disposals	(13,832)	(11)	(162)	(3,109)	–	(17,114)
Balance as at 30 June 2014	47,232	23,528	1,508	27,689	–	99,957
Carrying amount as at 30 June 2014	9,439	7,196	3,087	34,322	1,406	55,450
Forecast carrying amount at 30 June 2015³	9,710	5,145	2,649	40,672	1,000	59,176
Cost						
Balance as at 1 July 2012	63,572	31,189	4,594	54,620	4,312	158,287
Additions by purchase	4,175	2,147	3,260	5,540	4,286	19,408
Other movements ¹	526	–	–	(559)	–	(33)
Transfers between category	11	–	–	3,969	(4,264)	(284)
Disposals	(2,663)	(4,038)	(2,950)	(10,567)	–	(20,218)
Balance as at 30 June 2013	65,621	29,298	4,904	53,003	4,334	157,160
Depreciation and impairment losses						
Balance as at 1 July 2012	46,762	21,967	2,882	32,125	–	103,736
Depreciation charge – expensed	10,845	2,688	509	4,457	–	18,499
Depreciation charge – capitalised ²	–	67	–	–	–	67
Impairment losses	(44)	238	–	301	–	495
Transfers between category	5	–	–	–	–	5
Disposals	(2,616)	(3,770)	(2,268)	(10,540)	–	(19,194)
Balance as at 30 June 2013	54,952	21,190	1,123	26,343	–	103,608
Carrying amount as at 30 June 2013	10,669	8,108	3,781	26,660	4,334	53,552

¹ This relates to the addition/reduction of lease make-good costs on leased buildings.

² The depreciation charge for existing assets that are used in the development of intangible assets under construction.

³ The statement of accounting policies provides explanations of these figures which are not subject to audit.

Finance leases – The net carrying amount of IT equipment held under finance leases is \$935,000 (2012–13, \$890,000).

NOTE 5: INTANGIBLE ASSETS BY CATEGORY

	Software – developed \$000	Business process design \$000	Software and licences – purchased \$000	Assets under construction – intangibles \$000	Total \$000
Cost					
Balance as at 1 July 2013	456,739	8,262	124,343	26,517	615,861
Additions by purchase	–	–	5,445	–	5,445
Additions internally developed	6,826	–	–	17,706	24,532
Transfers between category	13,009	–	369	(14,196)	(818)
Disposals	(5,969)	–	(4,354)	–	(10,323)
Balance as at 30 June 2014	470,605	8,262	125,803	30,027	634,697
Amortisation and impairment losses					
Balance as at 1 July 2013	384,012	7,140	102,989	4,594	498,735
Amortisation charge – expensed	26,902	1,036	8,338	–	36,276
Amortisation charge – capitalised ¹	32	–	–	–	32
Impairment losses	–	–	–	1,649	1,649
Transfers between category	–	–	–	–	–
Disposals	(5,971)	–	(3,877)	–	(9,848)
Balance as at 30 June 2014	404,975	8,176	107,450	6,243	526,844
Carrying amount as at 30 June 2014	65,630	86	18,353	23,784	107,853
Forecast carrying amount at 30 June 2015²	80,631	–	12,856	20,000	113,487
Cost					
Balance as at 1 July 2012	437,190	8,262	120,285	20,231	585,968
Additions by purchase	–	–	4,069	–	4,069
Additions internally developed	9,681	–	–	15,888	25,569
Transfers between category	9,897	–	(11)	(9,602)	284
Disposals	(29)	–	–	–	(29)
Balance as at 30 June 2013	456,739	8,262	124,343	26,517	615,861
Amortisation and impairment losses					
Balance as at 1 July 2012	358,492	6,104	94,137	2,947	461,680
Amortisation charge – expensed	27,046	1,036	8,857	–	36,939
Amortisation charge – capitalised ¹	4	–	–	–	4
Impairment losses	146	–	–	–	146
Transfers between category	(1,647)	–	(5)	1,647	(5)
Disposals	(29)	–	–	–	(29)
Balance as at 30 June 2013	384,012	7,140	102,989	4,594	498,735
Carrying amount as at 30 June 2013	72,727	1,122	21,354	21,923	117,126

There is no restriction over the title of Inland Revenue's intangible assets, nor are any intangible assets pledged as security for liabilities.

¹ Refers to the amortisation charge for existing assets that are utilised in the development of intangible assets.

² The statement of accounting policies provides explanations of these figures which are not subject to audit.

Software – developed and business process design includes the following items and carrying amounts: FIRST technology environment \$34,276,000, KiwiSaver \$4,587,000, student loans \$25,207,000 (2012–13, FIRST technology environment \$42,114,000, KiwiSaver \$11,684,000, student loans \$20,055,000). The amortisation period for these intangible assets range from 5–10 years.

Software and licences – purchased includes the following items and carrying amounts: FIRST technology environment \$17,372,000, KiwiSaver \$974,000 (2012–13, FIRST technology environment \$20,206,000, KiwiSaver \$1,144,000). The amortisation period for these intangible assets range from 5–10 years.

NOTE 6: CAPITAL CHARGE

Inland Revenue pays a capital charge to the Crown on taxpayers' funds as at 30 June and 31 December each year. The capital charge rate for the year ended 30 June 2014 was 8.0% per annum (2012-13, 8.0%, forecast 2014-15, 8.0%).

NOTE 7: FINANCE COSTS

	2012-13 Actual \$000	2013-14 Actual \$000
Interest on finance leases	150	74
Total finance costs	150	74

NOTE 8: REPAYMENT OF SURPLUS TO THE CROWN

	2012-13 Actual \$000	2013-14 Actual \$000
Total comprehensive income	41,077	43,650
Inc/(Dec) Unrealised losses/(gains) in relation to forward foreign exchange contracts	3	1
Repayment of surplus to the Crown	41,080	43,651

NOTE 9: DEBTORS AND PREPAYMENTS

	2012–13 Actual \$000	2013–14 Actual \$000
Current assets		
<i>Debtors</i>		
Accounts receivable	2,923	5,098
Less provision for impairment	(9)	(8)
Other debtors	243	474
<i>Net debtors</i>	3,157	5,564
Prepayments	15,541	11,247
Total current assets	18,698	16,811
Non-current assets		
Prepayments	402	834
Total non-current assets	402	834
Total debtors and prepayments	19,100	17,645

Given their short-term nature, the carrying value of accounts receivable and other debtors approximates their fair value.

Overdue receivables have been assessed for impairment and appropriate provisions applied, as detailed below:

Net debtors	Gross debtors \$000	Impairment \$000	Net debtors \$000
2013–14			
Due within 30 days	3,076	–	3,076
Overdue by 31 to 60 days	2,093	–	2,093
Overdue by 61 to 90 days	299	–	299
Overdue by > 90 days	104	(8)	96
Total	5,572	(8)	5,564
2012–13			
Due within 30 days	2,837	–	2,837
Overdue by 31 to 60 days	82	–	82
Overdue by 61 to 90 days	144	–	144
Overdue by > 90 days	103	(9)	94
Total	3,166	(9)	3,157

The provision for impairment has been calculated based on expected losses for Inland Revenue's debtors. Expected losses have been determined based on a review of each debtor.

Movements in the provision for impairment are as follows:

	2012–13 Actual \$000	2013–14 Actual \$000
Opening balance	(4)	(9)
Additional provisions made during the year	(11)	(8)
Unused amounts reversed	–	–
Receivables written off during the year	6	9
Closing balance	(9)	(8)

NOTE 10: INVENTORIES HELD FOR EXTERNAL DISTRIBUTION

Inventories comprise forms, booklets and returns held for external distribution. The carrying amount of inventories held for distribution that are measured at cost as at 30 June 2014 amounted to \$879,000 (2012-13, \$1,365,000).

The write-down of inventories held for distribution amounted to \$331,000 (2012-13, \$404,000). There have been no reversals of write-downs. The carrying amount of inventories held for distribution included the write-down of \$331,000.

No inventories are pledged as security for liabilities.

NOTE 11: CREDITORS AND OTHER PAYABLES

	2012-13 Actual \$000	2013-14 Actual \$000
Accounts payable	6,455	9,164
Accrued expenses – other	19,859	23,816
GST payable	9,071	11,323
Total creditors and other payables	35,385	44,303

Creditors and other payables are normally settled on 30-day terms, therefore the carrying value of creditors and other payables approximates their fair value.

NOTE 12: EMPLOYEE ENTITLEMENTS

	2012–13 Actual \$000	2013–14 Actual \$000
Current liabilities		
Annual leave	24,383	25,139
Terminating benefits	2,410	886
Accrued salaries and wages	15,637	18,212
Sick leave	1,259	1,138
Retiring leave	1,552	1,539
Long-service leave	901	1,007
Time off in lieu	6	10
Total current liabilities	46,148	47,931
Non-current liabilities		
Retiring leave	30,796	28,971
Long-service leave	8,149	7,655
Total non-current liabilities	38,945	36,626
Total employee entitlements	85,093	84,557

The present value of retiring and long-service leave obligations depend on a number of factors that are determined on an actuarial basis by an independent actuary using a number of assumptions. Two key assumptions used in calculating these liabilities are the discount rate and salary inflation. Any changes in these assumptions will impact on the carrying amount of the liabilities.

The following table provides a sensitivity analysis for the key assumptions:

	Discount rate		Salary inflation	
	–1.0% \$000	+1.0% \$000	–1.0% \$000	+1.0% \$000
Retiring leave	1,746	(1,558)	(1,695)	1,871
Long-service leave	446	(396)	(437)	404

Movements in the provision for terminating benefits are as follows:

	2012–13 Actual \$000	2013–14 Actual \$000
Terminating benefits		
Opening balance	8,071	2,410
Additional provisions made	916	1,907
Amounts used	(6,577)	(3,431)
Unused amounts reversed	–	–
Closing balance	2,410	886

The closing 2013–14 provision is expected to be fully utilised in the 2014–15 year.

NOTE 13: PROVISION FOR OTHER LIABILITIES

	2012–13 Actual \$000	2013–14 Actual \$000
Current liabilities		
Lease make-good	1,056	53
Total current liabilities	1,056	53
Non-current liabilities		
Lease make-good	839	912
Total non-current liabilities	839	912
Total provision for other liabilities	1,895	965

	Onerous contracts \$000	Lease make-good \$000	Total \$000
2013–14			
Opening balance	–	1,895	1,895
Additional provisions made	–	803	803
Amounts used	–	–	–
Unused amounts reversed	–	(999)	(999)
Discount unwind	–	(734)	(734)
Closing balance	–	965	965
2012–13			
Opening balance	392	3,290	3,682
Additional provisions made	–	789	789
Amounts used	(392)	(584)	(976)
Unused amounts reversed	–	(1,304)	(1,304)
Discount unwind	–	(296)	(296)
Closing balance	–	1,895	1,895

Onerous contracts

The provision for onerous contracts arises from non-cancellable accommodation leases where the unavoidable costs of meeting the lease contract exceed the economic benefits to be received from it. Inland Revenue does not currently have any leases where it is no longer able to use the surplus space due to restructuring and floor plan revision.

Lease make-good

For a number of its leased premises, Inland Revenue is required at the expiry of the lease term to make-good any damage caused to the premises and remove any fixtures and fittings it has installed. In some cases, Inland Revenue has the option to renew these leases, which impacts on the timing of expected cash flows to make-good the premises.

NOTE 14: DERIVATIVE FINANCIAL INSTRUMENTS

To hedge its currency risk Inland Revenue enters into foreign currency forward exchange contracts with the New Zealand Debt Management Office (NZDMO).

The notional principal amount of outstanding forward exchange contract derivatives as at 30 June 2014 was NZ \$95,146 (2012–13, NZ \$627,981). The contracts consist of the purchase of US \$82,720 (2012–13, AU \$485,000 and UK £25,136). The unrealised loss on the forward exchange contract derivative as at 30 June 2014 is NZ \$728 (2012–13, NZ \$3,000).

The fair value of forward exchange contracts entered into during the financial year was determined by reference to published price quotations in an active market.

NOTE 15: FINANCE LEASES

	2012–13 Actual \$000	2013–14 Actual \$000
Total minimum lease payments payable		
Not later than one year	441	456
Later than one year and not later than five years	587	637
Later than five years	–	–
Total minimum lease payments	1,028	1,093
Future finance charges	(107)	(114)
Present value of minimum lease payments	921	979
Present value of minimum lease payments payable		
Not later than one year	381	386
Later than one year and not later than five years	540	593
Later than five years	–	–
Total present value of minimum lease payments	921	979
Represented by:		
Current	381	386
Non-current	540	593
Total finance leases	921	979

Inland Revenue has entered into an agreement for the provision of telecommunications services that includes embedded finance leases. The leased items are included within the net carrying amount of IT equipment (refer note 4 Property, Plant and Equipment).

There are no restrictions placed on Inland Revenue by any of the finance leasing arrangements.

Finance lease liabilities are effectively secured, as the rights to the leased assets reverts to the lessor in the event of default in payment.

NOTE 16: OTHER FINANCIAL LIABILITIES

	2012–13 Actual \$000	2013–14 Actual \$000
Current liabilities		
Leasing incentives	131	183
Total current liabilities	131	183
Non-current liabilities		
Leasing incentives	678	869
Total non-current liabilities	678	869
Total other financial liabilities	809	1,052

NOTE 17: RECONCILIATION OF NET SURPLUS TO NET CASH FLOW FROM OPERATING ACTIVITIES

	2012–13 Actual	In 2013 Budget*	2013–14 Estimated Actual*	2013–14 Actual
	\$000	\$000	\$000	\$000
Net surplus/(deficit)	41,077	–	–	43,650
Add non-cash items				
Depreciation and impairment	18,994	18,339	14,070	13,440
Amortisation and impairment	37,085	41,549	38,003	37,925
Total non-cash items	56,079	59,888	52,073	51,365
Add items classified as investing or financing activities				
Net loss/(gain) on disposal of property, plant and equipment	(476)	–	8	86
Net loss on disposal of intangible assets	–	–	–	478
Total items classified as investing or financing activities	(476)	–	8	564
Add/(less) working capital movements				
(Inc)/Dec in debtor Crown	(41,869)	(4,807)	(5,516)	(39,675)
(Inc)/Dec in debtors and prepayments	(2,053)	2,011	3,188	1,455
(Inc)/Dec in inventories held for distribution	(133)	98	366	485
Inc/(Dec) in creditors and other payables	(676)	(2,337)	3,210	8,917
Inc/(Dec) in derivative financial instruments	(500)	(30)	(3)	(2)
Inc/(Dec) in provision for employee benefits	(4,301)	(1,219)	(345)	(536)
Inc/(Dec) in provision for other liabilities	(1,787)	(942)	(981)	(930)
Inc/(Dec) in other financial liabilities	(14)	(101)	223	243
Inc/(Dec) in finance lease liabilities	–	–	–	–
Net movements in working capital items	(51,333)	(7,327)	142	(30,043)
Net cash inflow from operating activities	45,347	52,561	52,223	65,536

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

NOTE 18: COMMITMENTS

Capital commitments

Capital commitments are the aggregate amount of capital expenditure contracted for the acquisition of property, plant and equipment and intangible assets that have not been paid for or recognised as a liability at the balance date.

Operating commitments

Operating commitments for non-cancellable accommodation leases relate to Inland Revenue's long-term leases on its premises at many locations throughout New Zealand. The annual lease payments are regularly reviewed and the amounts disclosed as future commitments are based on current rental rates. These commitments also include office space vacated by Inland Revenue as a result of organisational restructuring and sub-leased. Provision has been made in the financial statements for the expected net expenses for the duration of these leases.

The total minimum future sub-lease payments expected to be received under non-cancellable sub-leases at balance date is \$12,294,537 (2012–13, \$3,625,049). The increase is due to the establishment of a co-located building in Wellington with other government agencies. The co-location is expected to take place in the latter half of the 2014–15 financial year.

Inland Revenue's non-cancellable operating leases have varying terms, escalation clauses and renewal rights. There are no restrictions placed on Inland Revenue by any of its leasing arrangements.

NOTE 19: CONTINGENT LIABILITIES AND CONTINGENT ASSETS

Contingent liabilities

Legal proceedings and disputes – taxpayer

This contingent liability relates to potential claims against Inland Revenue for court costs associated with tax disputes and other legal proceedings being taken through the courts against taxpayers. It only relates to court costs; the actual revenue (tax) under dispute is recognised as a non-departmental contingency (refer to *Schedule of non-departmental contingent liabilities and contingent assets*).

The expected value of the contingent liability is calculated using an outcome probability model that weighs the total potential liability against outcome probabilities. Independent confirmation on the liability has been ascertained on all legal proceedings and tax disputes.

The contingent liability as at 2013–14 (excluding court costs recoverable) was \$843,283 (2012–13, \$1,096,938).

Legal proceedings and disputes – departmental

This contingent liability relates to disputes such as claims made by departmental suppliers.

Personal grievances

Personal grievances represent amounts claimed by employees for alleged breaches of contract against Inland Revenue.

Contingent assets

Legal proceedings and disputes – taxpayer

This contingent asset relates to potential court costs recoverable by Inland Revenue for court costs associated with tax disputes and other legal proceedings being taken through the courts against taxpayers. It only relates to court costs; the actual revenue (tax) under dispute is recognised as a non-departmental contingency (refer to *Schedule of non-departmental contingent liabilities and contingent assets*).

The expected value of the contingent asset is calculated using an outcome probability model that weighs the total potential court costs recoverable against outcome probabilities.

The contingent asset as at 2013–14 was \$2,867,162 (2012–13, \$3,485,927).

NOTE 20: RELATED PARTY TRANSACTIONS AND KEY MANAGEMENT PERSONNEL

Inland Revenue is a wholly owned entity of the Crown. The government significantly influences the role of Inland Revenue as well as being its major source of revenue. In 2013–14 Inland Revenue has been provided with operating funding from the Crown of \$718 million (2012–13, \$659 million) for specific purposes as set out in the scope of relevant government appropriations.

Inland Revenue enters into related party transactions with other government departments, Crown agencies and state-owned enterprises which are controlled, significantly influenced, or jointly controlled by the Crown. All related party transactions have been entered into on an arm's length basis.

In 2013–14 the purchase of goods and services by Inland Revenue from entities controlled, significantly influenced, or jointly controlled by the Crown totalled \$30 million (2012–13, \$29 million). These purchases include postal services from New Zealand Post, and air travel from Air New Zealand.

In 2013–14 Inland Revenue paid capital charge on taxpayers' funds to the Crown totalling \$22 million (2012–13, \$21 million).

In 2013–14 the services provided by Inland Revenue to entities controlled, significantly influenced, or jointly controlled by the Crown totalled \$22 million (2012–13, \$21 million). These services include the collection of levies payable by earners on behalf of the Accident Compensation Corporation (ACC), financial transaction processing services for the Department of Internal Affairs and the NZ Productivity Commission, and the supply of information to other agencies. No provision has been required, nor any expense recognised, for impairment of receivables from related parties.

No related party transactions were entered into with key management personnel during the year.

Compensation to key management personnel

The remuneration of key management personnel during the year was as follows:

	2012–13 Actual \$000	2013–14 Actual \$000
Salaries and other short-term employee benefits	2,835	3,270
Post-employment benefits	47	64
Other long-term benefits	5	–
Total key management personnel compensation	2,887	3,334

Key management personnel comprise the Minister of Revenue, the Commissioner, five Deputy Commissioners, Chief Tax Counsel, Chief Financial Officer, Chief Technology Officer, Chief People Officer and those formally acting in those positions during the financial year. The Commissioner's remuneration is determined and paid by the State Services Commission.

Key management personnel compensation excludes the remuneration and other benefits the Minister of Revenue receives. The Minister's remuneration and other benefits are set out by the remuneration authority and are not paid by Inland Revenue.

NOTE 21: FINANCIAL INSTRUMENTS – CATEGORIES OF FINANCIAL INSTRUMENTS

The carrying amounts of financial assets and financial liabilities in each of the NZ international accounting standard (PBE) 39 categories are as follows:

	Notes	2012–13 Actual \$000	2013–14 Actual \$000
Debtors and receivables			
Cash and cash equivalents		45,631	30,643
Debtor Crown		198,755	238,430
Net debtors	9	3,157	5,564
Total debtors and receivables		247,543	274,637
Fair value through surplus or deficit			
Derivative financial instrument liabilities	14	3	1
Total fair value through surplus or deficit		3	1
Financial liabilities measured at amortised cost			
Creditors and other payables	11	35,385	44,303
Finance lease liabilities	15	921	979
Other financial liabilities	16	809	1,052
Total financial liabilities measured at amortised cost		37,115	46,334

NOTE 22: FINANCIAL INSTRUMENTS – FAIR VALUE HIERARCHY DISCLOSURES

For those instruments recognised at fair value in the *Statement of Financial Position*, fair values are determined according to the following hierarchy:

- Quoted market price (level 1) – Financial instruments with quoted prices for identical instruments in active markets.
- Valuation technique using observable inputs (level 2) – Financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.
- Valuation techniques with significant non-observable inputs (level 3) – Financial instruments valued using models where one or more significant inputs are not observable.

The following table analyses the basis of the valuation of classes of financial instruments measured at fair value in the *Statement of Financial Position*.

	Valuation technique			Total \$000
	Quoted market price \$000	Observable inputs \$000	Significant non - observable inputs \$000	
2013–14				
Financial liabilities				
Foreign exchange derivatives	–	1	–	1
2012–13				
Financial liabilities				
Foreign exchange derivatives	–	3	–	3

There were no transfers between the different levels of the fair value hierarchy.

NOTE 23: FINANCIAL INSTRUMENTS – FINANCIAL INSTRUMENT RISKS

Market risk

Currency risk

The risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates is called currency risk.

Because Inland Revenue purchases fixed assets and services from overseas suppliers it is exposed to currency risk arising from various currency exposures, primarily for the United States and Australian dollars. Currency risk arises from future purchases of fixed assets and services which are denominated in a foreign currency.

Inland Revenue has policies in place to manage the risks associated with financial instruments and, being risk averse, seeks to minimise exposure from its treasury activities. Inland Revenue does not enter into transactions that are speculative in nature.

Under its foreign exchange policy, Inland Revenue enters into foreign currency forward exchange contracts to manage foreign exchange exposures when single foreign exchange transactions exceed NZ \$100,000, or the transaction exposure for an individual currency exceeds NZ \$100,000. This policy has been approved by Treasury and is in line with the requirements of Treasury *“Guidelines for the Management of Crown and Departmental Foreign Exchange Exposure”*.

Interest rate risk

Interest rate risk is the risk that the fair value of a financial instrument will fluctuate or, the cash flows from a financial instrument will fluctuate, due to changes in market interest rates.

Inland Revenue has no interest-bearing financial instruments so it has no exposure to interest rate risk.

Credit risk

The risk that a third party will default on its obligations to Inland Revenue, causing a loss to be incurred is called credit risk. In the normal course of its business credit risk from trade debtors is concentrated with the Crown and other government agencies.

The carrying amount of financial assets recognised in the *Statement of Financial Position* best represents Inland Revenue's maximum exposure to credit risk at balance date.

Inland Revenue does not require any collateral, security, or other credit enhancements to support financial instruments with financial institutions that it deals with or the NZDMO, because these entities have high credit ratings. For its other financial instruments, Inland Revenue does not have significant concentrations of credit risk.

The carrying amount of financial assets that would otherwise be past due or impaired whose terms have been renegotiated is not material.

Liquidity risk

Liquidity risk is the risk that Inland Revenue will encounter difficulty raising liquid funds to meet commitments as they fall due.

As all but an insignificant proportion of funds come from the New Zealand Government and cash is drawn down on a fortnightly basis, Inland Revenue does not have significant liquidity risk. In meeting its liquidity requirements, Inland Revenue closely monitors its forecast cash requirements with expected cash drawdowns from the NZDMO. Inland Revenue maintains a target level of available cash to meet liquidity requirements.

Contractual maturity analysis of financial liabilities, excluding derivatives

The table below analyses Inland Revenue's financial liabilities that will be settled, based on the remaining period at the balance date to the contractual maturity date. The amounts disclosed are the contractual undiscounted cash flows.

	Notes	Carrying amount \$000	Contractual cash flows \$000	Up to 1 year \$000	1 to 5 years \$000	Over 5 years \$000	Total \$000
2013–14							
Creditors and other payables	11	44,303	44,303	44,303	–	–	44,303
Finance lease liabilities	15	979	1,093	456	637	–	1,093
Other financial liabilities	16	1,052	1,052	183	604	265	1,052
Closing balance		46,334	46,448	44,942	1,241	265	46,448
2012–13							
Creditors and other payables	11	35,385	35,385	35,385	–	–	35,385
Finance lease liabilities	15	921	1,028	441	587	–	1,028
Other financial liabilities	16	809	809	131	489	189	809
Closing balance		37,115	37,222	35,957	1,076	189	37,222

Contractual maturity analysis of derivative financial instrument liabilities

The table below analyses Inland Revenue's forward exchange contract derivatives into relevant maturity groupings based on the remaining period at balance date to the contractual maturity date. The amounts disclosed are the contractual undiscounted cash flows.

	Note	Liability carrying amount \$000	Asset carrying amount \$000	Contractual cash flows NZ\$ \$000	Less than 6 months NZ\$ \$000	6–12 months NZ\$ \$000	1–2 years NZ\$ \$000
2013–14							
Gross settled forward foreign exchange contracts	14	1	–	–	–	–	–
–Outflow		–	–	95	95	–	–
		1	–	95	95	–	–
2012–13							
Gross settled forward foreign exchange contracts	14	3	–	–	–	–	–
–Outflow		–	–	628	628	–	–
		3	–	628	628	–	–

The following provides a sensitivity analysis for the key assumptions:

At 30 June 2014, if the NZ dollar had strengthened by 5% against the US dollar, with all other variables held constant, the surplus for the year would have been \$4,769 (2012–13, \$1,619,000) higher. At 30 June 2014, if the NZ dollar had weakened by 5% against the US dollar, with all other variables held constant, the surplus for the year would have been \$5,271 (2012–13, \$1,790,000) lower. This movement is attributable to translation of US dollar-denominated creditors.

At 30 June 2014, if the NZ dollar had strengthened by 5% against the Australian dollar, with all other variables held constant, the surplus for the year would have been \$8,232 (2012–13, \$28,000) higher. At 30 June 2014, if the NZ dollar had weakened by 5% against the Australian dollar, with all other variables held constant, the surplus for the year would have been \$9,098 (2012–13, \$30,000) lower. This movement is attributable to translation of Australian dollar-denominated creditors.

NOTE 24: CAPITAL MANAGEMENT

Inland Revenue's capital is its taxpayers' funds, which comprise of general funds. Taxpayers' funds are represented by net assets.

Inland Revenue manages its revenues, expenses, assets, liabilities and general financial dealings prudently. Inland Revenue's taxpayers' funds are largely managed as a by-product of managing income, expenses, assets, liabilities, and compliance with the Government Budget processes and with Treasury Instructions and the Public Finance Act 1989.

The objective of managing Inland Revenue's taxpayers' funds is to ensure that it effectively achieves its strategic direction, while remaining a going concern.

NOTE 25: EXPLANATION OF MAJOR VARIANCES

The following major budget variances occurred between the 2013–14 Actuals and the 2013–14 Budget. The Budget figures for 2013–14 are those included in *The Estimates of Appropriations for the year ending 30 June 2014*.

	Notes	2013–14 Actual \$000	2013–14 Budget \$000	Variance \$000	Variance %
Statement of Comprehensive Income					
Income					
Revenue Crown	(a)	717,838	690,618	(27,220)	(4%)
Expenditure					
Personnel	(b)	431,986	447,965	15,979	4%
Operating	(c)	194,845	187,264	(7,581)	(4%)
Depreciation	(d)	13,440	18,339	4,899	27%
Amortisation and impairment	(e)	37,925	41,549	3,624	9%
Statement of Financial Position					
Current assets					
Cash and cash equivalents	(f)	30,643	12,000	(18,643)	(155%)
Debtor Crown	(g)	238,430	149,568	(88,862)	(59%)
Debtors and prepayments	(h)	16,811	15,422	(1,389)	(9%)
Non-current assets					
Property, plant and equipment	(i)	55,450	63,246	7,796	12%
Intangible assets	(j)	107,853	143,171	35,318	25%
Current liabilities					
Creditors and other payables	(k)	44,303	27,200	(17,103)	(63%)
Statement of Departmental Expenses and Capital Expenditure Against Appropriations					
Departmental capital expenditure					
Property, plant and equipment	(l)	15,564	21,277	5,713	27%
Intangible assets	(m)	29,127	55,723	26,596	48%

Statement of Comprehensive Income

a) *Revenue Crown* was higher than budget by \$27,220,000 (4%). The increase was mainly due to additional funding of \$19,000,000 for Business Transformation, which included a \$9,000,000 transfer from 2012–13. The remainder reflects expense transfers from 2012–13 of \$4,000,000 for personnel expenditure and \$3,214,000 for the child support legislative initiative.

b) *Personnel expenses* were lower than budget by \$15,979,000 (4%). The variance in expenditure was due to \$13,000,000 of expenditure for the child support legislative initiative and \$2,300,000 for Budget 2013 legislative initiatives that were planned to be incurred in 2013–14, but will now be incurred in 2014–15.

c) *Operating expenses* were higher than budget by \$7,581,000 (4%). This variance reflects additional funding for Business Transformation and increased technology costs for storage assets and mainframe services.

d) *Depreciation* was lower than budget by \$4,899,000 (27%). This variance was mainly due to lower spending on IT infrastructure, driven in part by a change towards infrastructure as a service resulting in operating expenditure rather than capital expenditure.

e) *Amortisation and impairment* was lower than budget by \$3,624,000 (9%). The variance was mainly due to capital expenditure on the child support legislative project occurring later than originally planned and a decision to deliver a mainframe upgrade through a service model rather than capital.

Statement of Financial Position

f) *Cash and cash equivalents* were higher than budget by \$18,643,000 (155%). This was due to holding cash for salaries and wages that were due on 2 July 2014.

g) *Debtor Crown* was higher than budget by \$88,862,000 (59%). This variance was mainly due to \$35,318,000 of underspending in intangible assets, \$7,796,000 of underspending in property, plant and equipment and the repayment of surplus to the Crown of \$43,651,000.

h) *Debtors and prepayments* were higher than budget by \$1,389,000 (9%). This is due to an invoice payment for a large debtor that occurred in July rather than June.

i) *Property, plant and equipment* was lower than budget by \$7,796,000 (12%). Most of the underspend is due to the planned purchase of \$7,600,000 of IT storage assets that did not eventuate. This storage will now be purchased through a service model resulting in operating expenditure being incurred rather than capital.

j) *Intangible assets* were lower than budget by \$35,318,000 (25%). The variance mainly relates to mainframe capital spend that was planned for 2013–14, but will now be delivered through a service model rather than capital. The remainder of the variance is attributable to capital expenditure for the child support legislative initiative that will now be incurred in 2014–15.

k) *Creditors and other payables* were higher than budget by \$17,103,000 (63%). This was due to the timing of trade payables and a higher than planned GST payment.

Statement of Departmental Expenses and Capital Expenditure against Appropriations

l) *Property, plant and equipment* was lower than the Appropriation by \$5,713,000 (27%). This was mainly due to lower spending on IT infrastructure, driven in part by a change towards infrastructure as a service resulting in operating expenditure rather than capital expenditure.

m) *Intangible assets* were lower than the Appropriation by \$26,596,000 (48%). This was mainly due to capital expenditure on the child support legislative project occurring later than originally planned and a decision to deliver a mainframe upgrade through a service model rather than capital.

NOTE 26: EVENTS AFTER BALANCE DATE

No events have occurred between the balance date and date of signing these financial statements that materially affect the actual results within these financial statements.

PART 08

Non- departmental financial schedules

SCHEDULE OF NON-DEPARTMENTAL REVENUE

FOR THE YEAR ENDED 30 JUNE 2014

	2012–13	2013–14	2013–14	2013–14	2014–15
	Actual	Budget*	Estimated	Actual	Forecast*
	\$000	\$000	Actual*	\$000	\$000
Direct taxation					
Income tax					
Individuals					
Source deductions	21,860,369	23,099,000	23,187,000	23,125,625	24,484,000
Other persons	5,210,418	5,083,000	5,161,000	5,216,335	5,428,000
Refunds	(1,644,078)	(1,488,000)	(1,531,000)	(1,573,264)	(1,395,000)
Fringe benefit tax	479,803	477,000	487,000	488,535	512,000
Sub-total individuals	25,906,512	27,171,000	27,304,000	27,257,231	29,029,000
Corporate tax					
Gross companies tax	10,176,526	10,264,000	10,481,000	10,617,384	10,686,000
Refunds	(151,183)	(197,000)	(195,000)	(192,338)	(207,000)
Non-resident withholding tax	420,219	447,000	421,000	427,714	481,000
Foreign-source dividend withholding payments	1,757	–	2,000	8,213	2,000
Sub-total corporate tax	10,447,319	10,514,000	10,709,000	10,860,973	10,962,000
Other direct income tax					
Resident withholding tax on interest income	1,630,885	1,671,000	1,642,000	1,643,787	2,007,000
Resident withholding tax on dividend income	516,262	607,000	472,000	445,867	495,000
Employer superannuation contribution tax	907,203	1,039,000	1,079,000	1,077,974	1,209,000
Gift duties	43	–	–	(70)	–
Sub-total other direct income tax	3,054,393	3,317,000	3,193,000	3,167,558	3,711,000
Total direct taxation	39,408,224	41,002,000	41,206,000	41,285,762	43,702,000

SCHEDULE OF NON-DEPARTMENTAL REVENUE (CONTINUED)

	2012–13	2013–14	2013–14	2013–14	2014–15
	Actual \$000	Budget* \$000	Estimated Actual* \$000	Actual \$000	Forecast* \$000
Indirect taxation					
Goods and services tax					
Gross goods and services tax	23,928,121	25,988,000	25,890,000	25,751,108	27,946,000
Refunds	(9,919,736)	(10,695,000)	(11,079,000)	(11,191,411)	(11,632,000)
Sub-total goods and services tax	14,008,385	15,293,000	14,811,000	14,559,697	16,314,000
Other indirect taxation					
Cheque duties ¹	2,913	3,000	3,000	2,464	-
Approved issuer levy	81,535	84,000	90,000	90,522	90,000
Gaming duties	266,576	278,000	267,000	266,814	267,000
Other indirect taxation	3,155	5,000	5,000	2,709	5,000
Sub-total other indirect taxation	354,179	370,000	365,000	362,509	362,000
Total indirect taxation	14,362,564	15,663,000	15,176,000	14,922,206	16,676,000
Total taxation	53,770,788	56,665,000	56,382,000	56,207,968	60,378,000
Other revenue					
Child support	494,447	632,000	520,000	459,309	573,000
Interest unwind – student loans	589,500	600,000	572,000	579,318	601,000
Other revenue	95,179	96,800	84,000	86,059	92,000
Total other revenue	1,179,126	1,328,800	1,176,000	1,124,686	1,266,000
Total operating revenue	54,949,914	57,993,800	57,558,000	57,332,654	61,644,000

¹ Cheque duties were abolished from 1 July 2014.

The accompanying accounting policies and notes form part of these financial schedules.

For a full understanding of the Crown's financial position and the results of its operations, refer to the *Financial Statements of the Government of New Zealand* for the year ended 30 June 2014.

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

SCHEDULE OF NON-DEPARTMENTAL EXPENDITURE

FOR THE YEAR ENDED 30 JUNE 2014

	2012–13	2013–14	2013–14 Estimated Actual*	2013–14	2014–15
	Actual \$000	Budget* \$000	Actual* \$000	Actual \$000	Forecast* \$000
Benefits and other unrequited expenses					
Child tax credit	1,711	1,400	1,800	1,835	1,300
Family tax credit	2,017,841	2,026,000	1,976,000	1,965,263	1,934,000
In-work tax credit	544,474	511,000	523,000	533,266	494,000
KiwiSaver: Fee subsidy	(12)	–	–	(11)	–
KiwiSaver: Interest	5,060	8,000	9,000	7,294	13,000
KiwiSaver: Kick-start payment	223,762	165,000	231,000	227,772	171,000
KiwiSaver: Tax credit	494,152	575,000	582,000	569,163	643,000
Minimum family tax credit	12,077	12,000	14,000	14,275	13,000
Paid parental leave payments	165,101	176,000	164,000	164,504	176,000
Parental tax credit	17,109	15,000	17,000	17,640	19,000
Payroll subsidy	2,503	3,000	3,300	3,129	4,000
Research and development tax credit	–	–	–	(3,952)	–
Total benefits and other unrequited expenses	3,483,778	3,492,400	3,521,100	3,500,178	3,468,300
Borrowing expenses					
Adverse event interest	(1)	10	20	12	10
Environmental restoration account interest	1,636	2,000	2,000	1,636	2,000
Income equalisation interest	6,221	8,000	8,000	7,260	7,000
Total borrowing expenses	7,856	10,010	10,020	8,908	9,010
Other expenses					
Bad debt write-offs	924,731	931,000	931,000	930,158	–
Impairment of debt ¹	(36,861)	266,234	266,234	95,257	–
Impairment of debt and debt write-offs ²	–	–	–	–	1,162,098
Impairment of debt relating to child support	282,214	392,000	296,000	254,635	323,000
Impairment of debt relating to student loans	484,000	110,000	(29,566)	12,000	100,000
Initial fair value write-down – student loans	535,630	537,000	644,000	629,539	668,000
Total other expenses	2,189,714	2,236,234	2,107,668	1,921,589	2,253,098
Total expenditure	5,681,348	5,738,644	5,638,788	5,430,675	5,730,408

¹ Impairment of debt relates to general tax, Working for Families Tax Credits and KiwiSaver debt.

² Impairment of debt and debt write-offs is a new appropriation combining both bad debt write-offs and impairment of debt, effective from 1 July 2014.

The accompanying accounting policies and notes form part of these financial schedules.

For a full understanding of the Crown's financial position and the results of its operations, refer to the *Financial Statements of the Government of New Zealand* for the year ended 30 June 2014.

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

SCHEDULE OF NON-DEPARTMENTAL ASSETS

AS AT 30 JUNE 2014

	Notes	2012–13	2013–14	2013–14	2013–14	2014–15
		Actual \$000	Budget* \$000	Estimated Actual* \$000	Actual \$000	Forecast* \$000
Assets						
Current assets						
Cash and cash equivalents		2,834,321	2,000,000	2,000,000	2,489,327	1,355,000
Receivables	1	7,383,403	6,928,917	7,665,600	7,568,681	7,775,600
Receivables – child support	2	13,720	3,030	13,720	10,899	13,720
Receivables – other		79,022	85,000	123,352	111,065	128,352
Student loans	3	1,020,000	1,079,000	1,158,000	1,193,000	1,219,000
Total current assets		11,330,466	10,095,947	10,960,672	11,372,972	10,491,672
Non-current assets						
Receivables	1	438,400	457,400	438,400	467,400	438,400
Receivables – child support	2	53,325	76,749	62,325	64,506	72,325
Student loans	3	7,268,177	7,909,577	7,593,840	7,522,829	7,804,993
Total non-current assets		7,759,902	8,443,726	8,094,565	8,054,735	8,315,718
Total assets		19,090,368	18,539,673	19,055,237	19,427,707	18,807,390

The accompanying accounting policies and notes form part of these financial schedules.

For a full understanding of the Crown's financial position and the results of its operations, refer to the *Financial Statements of the Government of New Zealand* for the year ended 30 June 2014.

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

SCHEDULE OF NON-DEPARTMENTAL LIABILITIES

AS AT 30 JUNE 2014

	Notes	2012–13 Actual \$000	2013–14 Budget* \$000	2013–14 Estimated Actual* \$000	2013–14 Actual \$000	2014–15 Forecast* \$000
Liabilities						
Payables and provisions						
Child support		30,096	24,004	30,096	37,359	30,096
Refundables and payables	4	3,514,165	3,933,216	4,166,396	3,630,784	4,404,794
Unclaimed monies	5	12,475	9,828	12,475	13,818	12,475
Total payables and provisions		3,556,736	3,967,048	4,208,967	3,681,961	4,447,365
Reserve schemes						
Reserve schemes	6	288,968	334,175	277,468	245,937	294,968
Total value of the reserve schemes		288,968	334,175	277,468	245,937	294,968
Total liabilities		3,845,704	4,301,223	4,486,435	3,927,898	4,742,333

The accompanying accounting policies and notes form part of these financial schedules.

For a full understanding of the Crown's financial position and the results of its operations, refer to the *Financial Statements of the Government of New Zealand* for the year ended 30 June 2014.

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

SCHEDULE OF NON-DEPARTMENTAL MOVEMENTS BETWEEN DEPARTMENTS

FOR THE YEAR ENDED 30 JUNE 2014

	2012–13	2013–14	2013–14 Estimated Actual*	2013–14	2014–15
	Actual \$000	Budget* \$000	Actual* \$000	Actual \$000	Forecast* \$000
Opening balance	12,910,876	14,422,492	15,244,664	15,244,664	14,568,802
Net result from operating activities	49,268,566	52,255,156	51,919,212	51,901,979	55,913,592
Asset transfer between departments – Ministry of Social Development – student loans	1,481,330	1,527,792	1,556,097	1,521,537	1,597,153
New Zealand Debt Management Office	(48,416,108)	(53,966,990)	(54,151,171)	(53,168,371)	(58,014,490)
Closing balance	15,244,664	14,238,450	14,568,802	15,499,809	14,065,057

The accompanying accounting policies and notes form part of these financial schedules.

For a full understanding of the Crown's financial position and the results of its operations, refer to the *Financial Statements of the Government of New Zealand* for the year ended 30 June 2014.

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

SCHEDULE OF NON-DEPARTMENTAL CONTINGENT LIABILITIES AND CONTINGENT ASSETS

AS AT 30 JUNE 2014

	Notes	2012–13 Actual \$000	2013–14 Actual \$000
Quantifiable contingent liabilities			
Legal proceedings and disputes – assessed	7	640,758	535,388
Unclaimed monies	5	100,933	111,804
Total quantifiable contingent liabilities		741,691	647,192
Quantifiable contingent assets			
Disputes – non-assessed	7	169,313	89,798
Total quantifiable contingent assets		169,313	89,798

There were no non-quantifiable contingent liabilities and contingent assets for the year ended 30 June 2014. (2012–13: \$nil)

The accompanying accounting policies and notes form part of these financial schedules.

For a full understanding of the Crown's financial position and the results of its operations, refer to the *Financial Statements of the Government of New Zealand* for the year ended 30 June 2014.

STATEMENT OF NON-DEPARTMENTAL APPROPRIATIONS

FOR THE YEAR ENDED 30 JUNE 2014

	2012–13	2013–14	2013–14 Revised Budget*	2013–14	2014–15
	Actual \$000	Budget* \$000	Budget* \$000	Actual \$000	Forecast* \$000
Vote: Revenue¹					
Benefits and other unrequited expenses					
Child support payments PLA	227,404	237,000	240,000	241,595	267,000
Child tax credit PLA	1,711	1,400	1,800	1,835	1,300
Family tax credit PLA	2,017,841	2,026,000	1,976,000	1,965,263	1,934,000
In-work tax credit PLA	544,474	511,000	523,000	533,266	494,000
KiwiSaver: Fee subsidy	(12)	–	–	(11)	–
KiwiSaver: Interest	5,060	8,000	10,000	7,294	13,000
KiwiSaver: Kick-start payment	223,762	165,000	241,000	227,772	171,000
KiwiSaver: Tax credit	494,152	575,000	597,000	569,163	643,000
Minimum family tax credit PLA	12,077	12,000	14,000	14,275	13,000
Paid parental leave payments ²	165,101	176,000	101,311	164,504	176,000
Parental tax credit PLA	17,109	15,000	17,000	17,640	19,000
Payroll subsidy PLA	2,503	3,000	3,300	3,129	4,000
Research and development tax credit	–	–	–	(3,952)	–
Total benefits and other unrequited expenses	3,711,182	3,729,400	3,724,411	3,741,773	3,735,300
Borrowing expenses					
Adverse event interest PLA	(1)	10	20	12	10
Environmental restoration account interest PLA	1,636	2,000	2,000	1,636	2,000
Income equalisation interest PLA	6,221	8,000	8,000	7,260	7,000
Total borrowing expenses	7,856	10,010	10,020	8,908	9,010
Other expenses					
Bad debt write-offs	924,731	931,000	956,000	930,158	–
Impairment of debt ³	(36,861)	266,234	341,234	95,257	–
Impairment of debt and debt write-offs ⁴	–	–	–	–	1,162,098
Impairment of debt relating to child support	282,214	392,000	326,000	254,635	323,000
Impairment of debt relating to student loans ⁵	283,000	110,000	145,434	41,000	100,000
Initial fair value write-down - student loans	535,630	537,000	662,824	629,539	668,000
Total other expenses	1,988,714	2,236,234	2,431,492	1,950,589	2,253,098
Total appropriations	5,707,752	5,975,644	6,165,923	5,701,270	5,997,408

¹ PLA refers to appropriations established under a permanent legislative authority.

² Historically Inland Revenue had made paid parental leave payments on the basis they had PLA. During 2013–14 it was identified they did not have PLA. Refer to the *Statement of Non-departmental Unappropriated Expenditure* for further details.

³ Impairment of debt relates to general tax, Working for Families Tax Credits and KiwiSaver debt.

⁴ Impairment of debt and debt write-offs is a new appropriation combining both bad debt write-offs and impairment of debt, effective from 1 July 2014.

⁵ Excludes remeasurement of (\$29.0) million (2012–13 \$201.0 million).

The accompanying accounting policies and notes form part of these financial schedules.

For a full understanding of the Crown's financial position and the results of its operations, refer to the *Financial Statements of the Government of New Zealand* for the year ended 30 June 2014.

* The statement of accounting policies provides explanations of these figures which are not subject to audit.

STATEMENT OF NON-DEPARTMENTAL UNAPPROPRIATED EXPENDITURE

FOR THE YEAR ENDED 30 JUNE 2014

	Actual	Authority	Expenses in excess of appropriation
	\$000	\$000	\$000
Benefits and other unrequited expenses			
Paid parental leave payments: July – Nov	67,689	–	67,689

The accompanying accounting policies and notes form part of these financial schedules.

For a full understanding of the Crown's financial position and the results of its operations, refer to the *Financial Statements of the Government of New Zealand* for the year ended 30 June 2014.

In the 2013–14 financial year:

- there were no instances of expenditure incurred outside of appropriation (2012-13 \$nil).
- there was one instance of expenditure incurred without appropriation (2012-13 \$nil).
- there were no instances of expenditure incurred in excess of appropriation (2012-13 \$3.762 million).

Historically Inland Revenue had made paid parental leave payments on the basis that they had a Permanent Legislative Authority (PLA). Payments under a PLA do not require separate appropriation authority as the payments are authorised, without further appropriation, under an Act of Parliament. During 2013–14 it was identified that these payments had been incorrectly classified as having a PLA. The misclassification of paid parental leave payments was identified early in 2013–14. As a result, the breach is only for part of the year. Validation of the expenditure incurred in 2013–14 will be sought through the Appropriation (2013/14 Financial Review) Bill.

SCHEDULE OF NON-DEPARTMENTAL TRUST MONEY

FOR THE YEAR ENDED 30 JUNE 2014

	2012–13 Actual \$000	2013–14 Contributions \$000	2013–14 Distributions \$000	2013–14 Actual \$000
Child support				
Child support trust account	22,000	235,378	(239,984)	17,394
Reciprocal child support agreement trust account	337	11,802	(11,743)	397
Total child support	22,337	247,180	(251,727)	17,791
KiwiSaver				
KiwiSaver returned transactions trust account	273	–	(229)	44
Total KiwiSaver	273	–	(229)	44
Total trust money	22,610	247,180	(251,956)	17,835

The child support trust accounts were established in accordance with sections 139 and 140 of the Child Support Act 1991. Inland Revenue administers these trust accounts for amounts collected from liable parents and the subsequent child support payments that are paid to the custodial parents.

The KiwiSaver trust account was established in accordance with section 74(4) of the KiwiSaver Act 2006. Inland Revenue administers this account to hold money deposited with the Crown from KiwiSaver scheme providers, primarily for refunds and payments made in error, pending the completion of the financial transaction.

The accompanying accounting policies and notes form part of these financial schedules.

For a full understanding of the Crown's financial position and the results of its operations, refer to the *Financial Statements of the Government of New Zealand* for the year ended 30 June 2014.

STATEMENT OF ACCOUNTING POLICIES

These financial schedules and statements are for the year ended 30 June 2014 and include forecast financial schedules and statements for the year ended 30 June 2015. They have been combined to provide a single view of actual and forecast information.

References to the financial schedules incorporate the financial statements and forecast financial statements, unless otherwise stated.

REPORTING ENTITY

These non-departmental financial schedules present financial information on public funds managed by Inland Revenue on behalf of the Crown.

These non-departmental balances are consolidated into the *Financial Statements of the Government of New Zealand* for the year ended 30 June 2014. For a full understanding of the Crown's financial position, results of operations, and cash flows for the year, refer to the *Financial Statements of the Government*.

REPORTING PERIOD

The reporting period for these financial schedules is for the year ended 30 June 2014. The forecast financial schedules are for the year ended 30 June 2015.

The financial schedules were authorised for issue by the Chief Executive of Inland Revenue on 29 September 2014.

STATEMENT OF COMPLIANCE

The financial schedules have been prepared in accordance with the requirements of the Public Finance Act 1989, which includes the requirement to comply with New Zealand generally accepted accounting practice (NZ GAAP), and Treasury Instructions. Compliance with NZ GAAP in this instance meant the figures for the year ended 30 June 2014 complied with New Zealand equivalents to International Financial Reporting standards (NZ IFRS), and where appropriate, standards issued by the International Public Sector Accounting Standards Board (IPSAS) as appropriate for public benefit entities and New Zealand equivalents to NZ IAS.

BASIS OF PREPARATION

The non-departmental schedules have been prepared in accordance with the accounting policies of the *Financial Statements of the Government*, Treasury Instructions, and Treasury Circulars.

Measurement and recognition rules applied in the preparation of these schedules and statements are consistent with NZ GAAP as appropriate for public benefit entities.

JUDGEMENTS AND ESTIMATIONS

In preparing these financial schedules, estimates and assumptions have been made concerning the future. These estimates and assumptions may differ from the subsequent actual results.

Estimates and assumptions are continually evaluated and are based on experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Revisions to accounting estimates are recognised in the period the estimate is revised in if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Material judgements, estimates and assumptions impact on receivables, child support receivables, student loan debt and refundables and payables. See notes 1, 2, 3 and 4 for more information on these.

ACCOUNTING POLICIES

The following accounting policies, which materially affect the measurement of financial results and financial position, have been applied.

Budget and forecast figures

The Budget figures for 2013–14 are those included in *The Estimates of Appropriation for the year ending 30 June 2014*.

The Revised Budget figures for 2013–14 are those included in *The Supplementary Estimates of Appropriations and Supporting Information for the year ending 30 June 2014*.

The Estimated Actual figures for 2013–14 and the Forecast figures for 2014–15 are those included in *The Estimates of Appropriations for the year ending 30 June 2015*. The Estimated Actual figures represent forecasts submitted to Treasury based on all Government decisions and assumptions as at 29 April 2014.

No material changes were made to the 2014–15 forecast figures in the *Pre-election Economic and Fiscal Update (PREFU) 2014*.

The Budget, Revised Budget, Estimated Actual and Forecast figures have been prepared in accordance with NZ GAAP, using accounting policies that are consistent with those adopted in preparing these financial schedules.

The forecast financial schedules and statements for the 2014–15 year have been prepared in accordance with public sector PBE Accounting Standards (PBE IPSAS). This is a change from actual and budget figures as at 30 June 2014 which was prepared in accordance with NZ equivalents to International Financial Reporting Standards as appropriate for public benefit entities.

(NZ IFRS (PBE)). At this stage we have not identified any material changes between these standards that will impact the forecast financial schedules and statements. A detailed assessment will be performed shortly for PBE IPSAS.

Revenue

Operating revenue

The payment of tax in itself, does not entitle a taxpayer to an equivalent value of services or benefits, because there is no direct relationship between paying tax and receiving Crown services and transfers, that is, tax revenue is a non-exchange transaction.

Tax revenue is recognised when a taxable event has occurred and the tax revenue can be reliably measured. The taxable event is defined as follows:

Tax type	Taxable activity
Income tax	The earning of assessable income during the taxation period by the taxpayer.
Goods and services tax	The purchase or sale of taxable goods and services during the taxation period.

The New Zealand tax system is predicated on self-assessment where taxpayers are expected to understand the tax laws and comply with them. This has an impact on the completeness of tax revenues when taxpayers fail to comply with tax laws, for example, if they do not report all of their income. Inland Revenue has implemented systems and controls in order to detect and correct situations where taxpayers are not complying with the various acts it administers. These systems and controls include performing audits of taxpayer records where determined necessary by Inland Revenue. Such procedures cannot be expected to identify all sources of unreported income or other cases of non-compliance with tax laws. Inland Revenue is unable to estimate the amount of unreported tax.

Initial fair value write-down – student loans

When new borrowings are made to students, they are written down immediately to the fair value. The initial write-down ratio is used to determine this write-down, which is an expense.

Interest unwind – student loans

Interest unwind on student loans is accrued using the effective interest rate method. The effective interest rate exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount. Effective interest rates are assigned to new lending each year on a 'year of lending' basis.

Expenses

General

Expenses are recognised in the period to which they relate.

Benefits and other unrequited expenses

Expense type	Definition
Child tax credit	Extra assistance for low to middle income families who do not depend on the state for financial support (expenses incurred pursuant to section 185 of the Tax Administration Act 1994).
Family tax credit	Family support payments made to beneficiaries and non-beneficiaries during the year (expenses incurred pursuant to section 185 of the Tax Administration Act 1994).
In-work tax credit	Extra assistance for low to middle income families where the person works a minimum of 20 hours per week and does not have a partner, or a person and their partner work a minimum of 30 hours per week (expenses incurred pursuant to section 185 of the Tax Administration Act 1994).
KiwiSaver: Fee subsidy	Fee subsidy to KiwiSaver members in respect of their scheme provider fees as set out in the KiwiSaver Act 2006. This ceased on 31 March 2009.
KiwiSaver: Interest	Interest on KiwiSaver contributions as set out in the KiwiSaver Act 2006.
KiwiSaver: Kick-start payment	One-off payment made on opening a KiwiSaver account for members who meet the required eligibility criteria as set out in the KiwiSaver Act 2006.
KiwiSaver: Tax credit	Tax credit to KiwiSaver members and the payment of residual tax credits to employers as set out in the Income Tax Act 2007.
Minimum family tax credit	Extra payment made to families where at least one parent is working for salary or wages (expenses incurred pursuant to section 185 of the Tax Administration Act 1994).
Paid parental leave payments	Paid parental leave payments made to parents eligible under the Parental Leave and Employment Protection Act 1987.
Parental tax credit	Additional financial support made to working families for the eight-week period following the birth of a child (expenses incurred pursuant to section 185 of the Tax Administration Act 1994).
Payroll subsidy	Subsidy to a payroll agent undertaking employers' payroll-related tax compliance activities on their behalf (expenses incurred pursuant to section 185 of the Tax Administration Act 1994).
Research and development tax credit	Tax credits for expenditure on research and development where the required eligibility criteria is met as set out in the Income Tax Act 2007. Expenditure incurred up until 31 March 2009 may be eligible for credits, where claims have been filed by 31 March 2012.

Borrowing expenses

Expense type	Definition
Adverse event interest	Interest on adverse event income equalisation reserve accounts held by taxpayers in the farming and agriculture business (expenses incurred pursuant to section 185 of the Tax Administration Act 1994).
Environmental restoration account interest	Interest on environmental restoration accounts (expenses incurred pursuant to section 185 of the Tax Administration Act 1994).
Income equalisation interest	Interest on income equalisation reserve scheme accounts held by taxpayers in the farming, fishing or forestry industries (expenses incurred pursuant to section 185 of the Tax Administration Act 1994).

Other expenses

Expense type	Definition
Bad debt write-offs	Bad debt write-offs for Crown debt administered by Inland Revenue. These write-offs relate to general tax, KiwiSaver and Working for Families Tax Credits debt.
Impairment of debt	Impairment arising from objective evidence of one or more loss events that occurred after the initial recognition of the debt, and the loss event (or events) has had a reliably measurable impact on the estimated future cash flows of the Crown debt book. This impairment relates to general tax, KiwiSaver and Working for Families Tax Credits debt.
Impairment of debt and debt write-offs	Bad debt write-offs for Crown debt and impairment arising from objective evidence of one or more loss events that occurred after the initial recognition of the debt, and the loss event (or events) has had a reliably measurable impact on the estimated future cash flows of the Crown debt book. These bad debt write-offs and impairment relate to general tax, KiwiSaver and Working for Families Tax Credits debt.
Impairment of debt relating to child support	Impairment arising from objective evidence of one or more loss events that occurred after the initial recognition of the debt, and the loss event (or events) has had a reliably measurable impact on the estimated future cash flows of the collective book of child support debt.
Impairment of debt relating to student loans	Impairment arising from objective evidence of one or more loss events that occurred after the initial recognition of the loan, and the loss event (or events) has had a reliably measurable impact on the estimated future cash flows of the collective book of student loan debt.
Initial fair value write-down – student loans	The initial fair value write-down is the amount by which a student loan is discounted at the time the loan is made. The discounting reflects the expected cash flows over the life of the loan.

Cash and cash equivalents

Cash and cash equivalents include cash on hand, cash in transit and funds held in bank accounts administered by Inland Revenue.

Receivables

Receivables include taxes, levies and fines (and any penalties and interest associated with these activities) as well as social benefit receivables.

Receivables are initially assessed at nominal value, that is, the receivable reflects the amount of tax owed, levy, fine charged, or social benefit debt payable. These receivables are subsequently adjusted for penalties and interest as they are charged, and tested for impairment annually. Interest and penalties charged on receivables are presented as revenue in the *Schedule of Non-departmental Revenue*.

Allowances for estimated irrecoverable amounts are recognised when there is objective evidence that the asset is impaired. Impairment movements are recognised in the *Schedule of Non-departmental Expenditure*. Impairment losses can be reversed where there is evidence that the impaired value of the asset has increased.

Financial models have been constructed for Inland Revenue to calculate the impairment of Crown debt. These models apply a

number of assumptions on future repayment behaviour as well as economic assumptions such as the discount rate and inflation.

Financial instruments

Financial assets

Student loans

Student loans are designated as loans and receivables under NZ IAS 39. Student loans are recognised initially at fair value, plus transaction costs, and subsequently measured at amortised cost using the effective interest rate method, and adjusted for impairment movements. Fair value on initial recognition of student loans is determined by projecting forward expected repayments and discounting them back at an appropriate discount rate. The difference between the amount lent and the fair value on initial recognition is expensed on initial recognition. The subsequent measurement at amortised cost is determined using the effective interest rate calculated at initial recognition. This rate is used to spread the Crown's interest income across the life of the loan and determines the loan's carrying value at each reporting date.

Allowances for estimated irrecoverable amounts are recognised when there is objective evidence that Inland Revenue will not be able to collect all amounts due according to the original terms of the receivables. Impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more

events that occurred after the initial recognition of the loan and a loss event has an impact on the estimated future cash flows of the loan that can be reliably measured. The amount of the provision is the difference between the asset's carrying amount and estimated impaired value. The impairment losses are recognised in the *Schedule of Non-departmental Expenditure*.

Impairment losses can be reversed where there is evidence that the impaired value of the financial asset has increased.

Actuarial models have been constructed by a third party to calculate the impairment of student loan debt. Refer to Note 3 for more information on this model.

Financial liabilities

Financial liabilities are recognised initially at fair value, less transaction costs. Financial liabilities entered into with a duration of less than 12 months are recognised at their nominal value, unless the effect of discounting is material.

Contingent liabilities and assets

Contingent liabilities and assets are recorded in the *Schedule of Non-departmental Contingent Liabilities and Contingent Assets* at the point at which the contingency is evident. Contingent liabilities are disclosed if the possibility that they will crystallise is not remote. Contingent assets are disclosed if it is probable that the benefits will be realised.

Changes in accounting policies

There have been no changes in accounting policies applicable to the preparation of non-departmental financial schedules. All policies have been applied on a basis consistent with the previous year.

The forecasts for the 2014–15 year have been prepared in accordance with Public sector PBE Accounting Standards (PBE IPSAS). This is a change from actual and budget figures as at 30 June 2014 which was prepared in accordance with NZ equivalents to International Financial Reporting Standards as appropriate for public benefit entities (NZ IFRS (PBE)). At this stage we have not identified any material changes between these standards that will impact the forecast financial schedules.

Comparatives

When presentation or classification of items in the financial schedules is amended or accounting policies are changed, comparative figures have been restated to ensure consistency with the current period, unless it is impracticable to do so.

FORECAST FINANCIAL SCHEDULES

The forecast financial schedules have been prepared in accordance with the Public Finance Act 1989.

The purpose of the forecast financial schedules is to facilitate Parliament's consideration of appropriations for, and planned performance of, the department. These forecast financial statements may not be appropriate for other purposes.

The forecast financial schedules have been prepared in accordance with the accounting policies detailed above. Additional accounting policies relating to the forecasts are set out below.

The forecast financial schedules comply with NZ GAAP and have been prepared in accordance with Financial Reporting Standard 42: Prospective Financial Statements.

Forecast policies

The forecasts have been compiled on the basis of existing government policies and ministerial expectations at the time the schedules were finalised and reflect all government decisions and circumstances as at 29 April 2014.

The key assumptions in the preparation of the forecasts include:

- Tax revenue: Tax policy changes enacted and announced by the Government will take place as planned and will affect tax revenue and receipts as calculated and agreed between Inland Revenue and the Treasury.
- Student loans: The carrying value of student loans is based on a valuation model adapted to reflect current student loans policy. As such, the carrying value over the forecast period is sensitive to changes in a number of underlying assumptions, including future income levels, repayment behaviour and macroeconomic factors such as inflation and discount rates used to determine the effective interest rate for new borrowers. Any change in these assumptions would affect the present fiscal forecast.

For other key fiscal forecasts assumptions, refer to the *Budget Economic and Fiscal Update 2014*.

These assumptions are adopted as at 29 April 2014.

Variations to forecast

The actual financial results for the forecast period covered are likely to vary from the information presented in these forecasts. Factors that may lead to a material difference between information in these Forecast Financial Statements and the actual reported results include:

- Changes to the budget through initiatives or legislation approved by Cabinet.
- Macroeconomics impacting revenue, expenditure and debt levels.
- The timing of taxpayer's filing and payment of returns.
- The timing of taxpayer refund and credit claims.
- Outcomes of the disputes process including litigation.

Any changes to budgets during 2014-15 will be incorporated into *The Supplementary Estimates of Appropriations for the year ending 30 June 2015*.

NOTES TO THE FINANCIAL SCHEDULES

NOTE 1: RECEIVABLES

Receivables include tax, Working for Families Tax Credits and KiwiSaver debt, and excludes student loans and child support debt.

The recoverable amount of receivables is calculated by forecasting the expected repayments based on analysis of historical debt data, deducting an estimate of service costs and then discounting using an appropriate rate. If the recoverable amount of the portfolio is less than the carrying amount, the carrying amount is reduced to the recoverable amount. Alternatively, if the recoverable amount is more, the carrying amount is increased.

Tax pooling funds held in Crown bank accounts have been netted off against receivables. These funds have been deposited by a commercial intermediary and allow taxpayers to pool tax payments to reduce their use-of-money-interest exposure. Underpayments and overpayments are offset within the same pool. We estimate that the majority of pooling funds relate to income accruals already included in not yet due receivables.

	2012–13 \$000	2013–14 \$000
Receivables		
Gross receivables	12,191,649	12,501,184
Impairment receivables	(4,369,846)	(4,465,103)
Carrying value receivables	7,821,803	8,036,081
Current and non-current apportionment		
Receivables – current	7,383,403	7,568,681
Receivables – non-current	438,400	467,400
Carrying value receivables	7,821,803	8,036,081
Ageing profile of receivables – gross		
Not due	6,849,356	7,030,478
Past due ¹		
Less than 6 months	903,865	930,766
6–12 months	362,726	389,436
1–2 years	788,041	719,193
Greater than 2 years	3,287,661	3,431,311
Total past due	5,342,293	5,470,706
Total receivables – gross	12,191,649	12,501,184
% Past due	44%	44%
Receivables – impairment		
Opening balance	4,406,707	4,369,846
Impairment losses recognised	887,870	1,025,415
Amounts written off as uncollectable	(924,731)	(930,158)
Closing balance	4,369,846	4,465,103

¹ Figures are based on debt elements. They are not comparable with the figures in Additional information section, which are based on debt cases and also include overdue student loan debt.

Receivables are classified as past due when any outstanding revenue is not paid by the taxpayer's due date. Due dates will vary, depending on the type of revenue outstanding (eg, income tax, GST, KiwiSaver) and the taxpayer's balance date. Past due debt includes debt collected under instalment, debt under dispute, default assessments and debts of taxpayers who are bankrupt, in receivership or in liquidation. Inland Revenue has debt management policies and procedures in place to actively manage the collection of past due debt.

The estimated recoverable amount of this portfolio and significant assumptions underpinning the valuation are:

	2012–13	2013–14
Recoverable amount of receivables not due (\$000)	6,823,227	6,988,813
Recoverable amount of receivables past due (\$000)	998,576	1,047,268
Use-of-money interest rate	8.40%	8.40%
Discount rate	5.10%	6.00%
Impact on the recoverable amount of a 2% increase in discount rate (\$000)	(20,000)	(21,000)
Impact on the recoverable amount of a 2% decrease in discount rate (\$000)	21,000	22,000

The fair value of receivables is not materially different from the carrying value.

Credit risk

In determining the recoverability of receivables Inland Revenue uses information about the extent to which the taxpayer is contesting the assessment and experience of the outcomes of such disputes, from lateness of payment and other information obtained from credit collection actions taken.

Under the Tax Administration Act 1994 Inland Revenue has broad powers to ensure that people meet their obligations. Part 10 of the Act sets out the powers of the Commissioner to recover unpaid tax.

The Crown does not hold any collateral or any other credit enhancements over receivables which are past due.

Receivables are widely dispersed over a number of taxpayers and as a result the Crown does not have any material individual concentrations of credit risk.

NOTE 2: RECEIVABLES – CHILD SUPPORT

The Crown collects monies from liable parents and remits this to custodial parents. The child support receivable represents penalties which have been incurred as a result of the under-payment of the debt, and in the main, relates to penalties imposed on liable parents who default on their payments.

Child support penalties grow exponentially due to their compounding nature. The recovery of debt is challenging and 97% of child support debt is impaired as we do not expect to collect it. There are limited provisions under child support legislation to remit penalties. The non-recoverability of penalties has been allowed for in the impairment figure. Impairment is calculated by forecasting the expected repayments of this penalty debt based on analysis of historical debt data, deducting an estimate of service costs and then discounted.

The concentration of credit risk is limited and this is not a risk that is actively managed. The Crown does not hold any collateral or other credit enhancements over these receivables.

	2012–13 \$000	2013–14 \$000
Receivables – child support		
Gross receivables	2,109,031	2,372,026
Impairment receivables	(2,041,986)	(2,296,621)
Total receivables – child support	67,045	75,405
Current and non-current apportionment		
Receivables – current	13,720	10,899
Receivables – non-current	53,325	64,506
Carrying value receivables	67,045	75,405
Ageing profile of receivables – gross		
Not due	–	–
Past due		
Less than 12 months	296,558	267,192
1–2 years	81,501	296,558
Greater than 2 years	1,730,972	1,808,276
Total past due	2,109,031	2,372,026
Total receivables – gross	2,109,031	2,372,026
% Past due	100%	100%
Impairment of receivables – child support		
Opening balance	1,759,772	2,041,986
Impairment losses recognised	282,214	254,635
Closing balance	2,041,986	2,296,621

NOTE 3: STUDENT LOANS

Student loans are initially issued by StudyLink (Ministry of Social Development). The loans and any associated transactions are transferred to Inland Revenue on a daily basis. Inland Revenue holds the total nominal debt and carrying value of the scheme. The initial capital lending of student loans is administrated under Vote Social Development. The initial fair value write-down expense on new capital lending, and any subsequent impairment, is administrated under Vote Revenue.

	2012–13 \$000	2013–14 \$000
Nominal value student loans	13,562,221	14,235,007
Adjustment to nominal value	(5,274,044)	(5,519,178)
Carrying value student loans	8,288,177	8,715,829
Current and non-current apportionment		
Student loans – current	1,020,000	1,193,000
Student loans – non-current	7,268,177	7,522,829
Carrying value student loans	8,288,177	8,715,829
Movement during the year		
Opening balance	8,290,882	8,288,177
Impairment	(484,000)	(12,000)
Loans transferred from Ministry of Social Development	1,481,333	1,521,537
Initial fair value write-down – student loans	(535,630)	(629,539)
Repayments	(1,053,908)	(1,031,664)
Interest unwind	589,500	579,318
Carrying value student loans	8,288,177	8,715,829
Fair value student loans		
Opening balance	8,527,000	8,298,000
Loans transferred from Ministry of Social Development	1,481,333	1,521,537
Initial fair value write-down – student loans	(535,630)	(629,539)
Repayments	(1,053,908)	(1,031,664)
Interest unwind	524,205	527,666
Administration costs	35,000	31,000
Change in expense assumption	27,000	37,000
Change in fair value discount rate	(201,000)	176,000
Impairment	(506,000)	(6,000)
Fair value student loans	8,298,000	8,924,000

Student loan valuation model

The student loan valuation model reflects current student loan policy and macro-economic assumptions. As such, the book value is sensitive to changes in a number of underlying assumptions, including future income levels, repayment behaviour and macro-economic factors such as inflation and the discount rates used to determine the effective interest rate on new borrowers.

Three data changes have been introduced for the 2014 student loan valuation model – the integrated data infrastructure (IDI), live data transfers and the unit record monthly data (URMD).

Statistics New Zealand compiles the IDI from data provided by Inland Revenue (IR), Ministry of Social Development (MSD) and Ministry of Education. The IDI replaces the integrated dataset used in the past. The IDI is current up to 31 March 2013. It contains information on borrowings, repayments, income, educational factors and socio-economic factors amongst others which had been used in the valuation model.

This is the first year that the live transfer data has been used for the valuation. The live transfer of lending data between MSD and IR began on 1 April 2012, previously lending data was transferred annually.

Due to a 15 month data lag in the IDI and because the financial information is based on tax years, URMD is used to fill in this lag as much as possible to determine the balances for each tranche of capital lending by calendar year. The URMD extract contains monthly loan transactions, loan balances at select months, start and end dates for when participants are classified as overseas-based and customs data listing entry and exit dates for all New Zealand taxpayers. The financial impact on the valuation of adopting the URMD this year is not material.

As per last year, the valuation model also utilises Employer Monthly Schedule (EMS) information which summarises income from salaries and wages i.e. more recent data to value student loans at balance date.

The significant assumptions behind the carrying value and fair value are:

	2012–13	2013–14
Carrying value		
Carrying value (\$000)	8,288,177	8,715,829
Effective interest rate	7.08%	7.06%
Interest rate applied to loans for overseas borrowers	5.1%–6.2%	5.1%–6.2%
Consumer Price Index	1.4%–2.5%	1.8%–2.5%
Future salary inflation	2.2%–3.5%	2.8%–3.5%
	2012–13	2013–14
Fair value		
Fair value (\$000)	8,298,000	8,924,000
Discount rate	6.45%	6.62%
Impact on fair value of a 1% increase in discount rate (\$000)	(423,000)	(448,000)
Impact on fair value of a 1% decrease in discount rate (\$000)	471,000	501,000

Fair value is the amount for which the loan book could be exchanged between knowledgeable, willing parties in an arm's-length transaction as at 30 June 2014. It is determined by discounting the future cash flows at an appropriate discount rate.

Fair values will differ from carrying values due to changes in market interest rates, as the carrying value is not adjusted for such changes whereas the fair value was calculated on a discount rate that was current at 30 June 2014. At that date, the fair value was calculated on a discount rate of 6.08% which excludes expenses whereas a weighted average discount rate of 7.06% including expenses was used for the carrying value. For reference, the representative discount rate for fair value including an allowance for expenses is 6.62%. The difference between fair value and carrying value does not represent an impairment of the asset.

The *Student Loan Scheme Annual Report* contains more information on the student loan scheme.

Impairment of student loans in 2013–14 totalled \$12 million. This impairment is mainly due to higher average loan balances, partially offset by updated income CART sub-models and a policy change. Average loan balances have been adjusted upwards this year as the adjustment made in the 2013 valuation to account for lending up until 31 March 2012 did not sufficiently capture additional lending made by existing borrowers but held by StudyLink. The policy change was an extension of the freezing of the repayment threshold for two more years to 31 March 2017.

In 2012–13 the impairment of student loans totalled \$484.0 million. This was driven by lower than expected incomes and repayments as well as changes to macroeconomic assumptions for income recovery and earnings inflation.

The valuation data is still very sensitive to changes in certain areas as can be seen from the sources of impairment set out below:

	2012–13 \$000	2013–14 \$000
Sources of impairment		
Policy and legislative changes	(27,000)	53,000
Revision of predictive sub-models	64,000	–
Experience variance	(303,000)	(2,000)
Change in demographic profile of participants	(29,000)	–
Macroeconomic changes ¹	(201,000)	29,000
Remaining model and data changes	12,000	(92,000)
Total sources of impairment	(484,000)	(12,000)

¹ Macroeconomic changes are classified as a remeasurement, as defined in the Public Finance Act 1989. The *Schedule of Non-departmental Expenditure* and the note above includes remeasurement adjustments in the impairment figure. However, the *Statement of Non-departmental Appropriations* excludes remeasurement adjustments. The remeasurement relates to changes in the macroeconomic assumptions used for the valuation of the receivable.

Credit risk

Credit risk is the risk that borrowers will default on their obligation to repay their loans or die before their loan is repaid, causing the scheme to incur a loss.

The student loan scheme does not require borrowers to provide any collateral or security to support advances made. As the total sum advanced is widely dispersed over a large number of borrowers, the student loan scheme does not have any material individual concentrations of credit risk.

The credit risk is reduced by collection of compulsory repayments through the tax system.

Interest rate risk

Interest rate risk is the risk that the value of financial instruments will fluctuate due to changes in interest rates. Changes could impact on the Government's return on loans advanced. The interest rate and the interest write-off provisions attached to student loans are set by the Government.

NOTE 4: REFUNDABLES AND PAYABLES

Refundables and payables are recognised at their nominal value as they are due within 12 months. The nominal value is considered to approximate their fair value.

Taxes refundable represent refunds due to taxpayers as a result of assessments being filed. Refunds are issued to taxpayers once account and refund reviews are complete.

	2012–13 \$000	2013–14 \$000
KiwiSaver payable	801,097	943,133
Paid parental leave payable	5,791	6,659
Research and development tax credits payable	3,952	–
Taxes refundable	2,703,325	2,680,992
Total refundables and payables	3,514,165	3,630,784

NOTE 5: UNCLAIMED MONIES

Under the Unclaimed Money Act 1971, entities (eg, financial institutions, insurance companies) hand over money not claimed after six years to Inland Revenue. The funds are repaid to the entitled owner on proof of identification.

NOTE 6: RESERVE SCHEMES

	2012–13 \$000	2013–14 \$000
Adverse event income equalisation	176	2
Environmental restoration	54,927	54,927
Income equalisation	233,865	191,008
Total reserve schemes	288,968	245,937

The adverse event income equalisation scheme operates in addition to the income equalisation scheme. Deposits earn interest at a rate of 6.5% per annum from the date of receipt until the deposit is refunded. Deposits can be withdrawn immediately, but are transferred to the main income equalisation account if not withdrawn within 12 months of the deposit.

The environmental restoration account allows businesses to set aside money to cover restoration costs for monitoring, avoiding, remedying or mitigating the detrimental environmental effects which may occur in later years. Interest is calculated at a rate of 3% per annum and is payable from the day after the deposit is made until the day before a refund is made. Refunds will be made when the environmental restoration costs are incurred.

The income equalisation scheme allows taxpayers in the farming, fishing and forestry industries to make payments during the year by way of income equalisation deposits. Interest paid at a rate of 3% per annum will apply where a deposit is left in the scheme for a period of 12 months or more.

NOTE 7: CONTINGENCIES

Contingent liabilities*Legal proceedings and disputes – assessed*

Contingent liabilities arise if a legal case is still not resolved at the end of the disputes process, Inland Revenue will issue an amended assessment to the taxpayer and recognise revenue. The taxpayer is then able to file proceedings with the Taxation Review Authority or the High Court disputing the assessment. These are recorded in the *Schedule of Non-departmental Contingent Liabilities and Contingent Assets* as legal proceedings and disputes – assessed. The contingent liability is the maximum liability Inland Revenue has in respect of these cases.

Unclaimed monies

Unclaimed monies are repaid to the entitled owner on proof of identification. Based on trends from prior years, the estimated likely amount of unclaimed monies that will be paid out is recorded as a liability in the *Schedule of Non-departmental Liabilities* and the remainder is recorded as a contingent liability in the *Schedule of Non-departmental Contingent Liabilities and Contingent Assets*.

Contingent assets*Disputes – non-assessed*

Contingent assets arise as part of the tax dispute process, for example, when Inland Revenue has advised a taxpayer of a proposed adjustment to their tax assessment through a notice of proposed adjustment (NOPA). At this point there has been no amended assessment issued and no revenue has been recognised so these adjustments are recorded in the *Schedule of Non-departmental Contingent Liabilities and Contingent Assets* as disputes – non-assessed. The taxpayer has the right to dispute this adjustment and a disputes resolution process is entered into. Inland Revenue quantifies a contingent asset based on the likely cash collectable for the disputes process based on experience and similar prior cases, net of losses carried forward.

Contingent assets can also arise where the taxpayer has not filed an assessment but Inland Revenue believes they are liable for tax. In this situation Inland Revenue will issue an assessment. Where the taxpayer chooses to dispute the Inland Revenue initiated assessment, the assessment is not recognised as revenue and a contingent asset is recorded in the *Schedule of Non-departmental Contingent Liabilities and Contingent Assets*. The value of the asset is based on the likely collectable portion of the default assessment, net of losses carried forward.

NOTE 8: COLLECTION OF EARNER LEVY

Inland Revenue collects these levies on behalf of the Accident Compensation Corporation and passes the monies directly to them. The levies do not appear on the non-departmental schedules.

	2012-13 \$000	2013-14 \$000
Earners levy	1,529,912	1,546,101
Total collection of earners levy	1,529,912	1,546,101

NOTE 9: EVENTS AFTER BALANCE DATE

No events have occurred between the balance date and date of signing these financial schedules that materially affect the actual results within these financial schedules.

Audit report

Independent Auditor's Report

To the readers of Inland Revenue's financial statements, non-financial performance information and schedules of non-departmental activities for the year ended 30 June 2014

The Auditor-General is the auditor of Inland Revenue (the Department). The Auditor-General has appointed me, Ajay Sharma, using the staff and resources of Audit New Zealand, to carry out the audit of the financial statements, the non-financial performance information and the schedules of non-departmental activities of the Department on her behalf.

We have audited:

- The financial statements of the Department on pages 66 to 97, that comprise the statement of financial position, statement of commitments, statement of contingent liabilities and contingent assets as at 30 June 2014, the statement of comprehensive income, statement of changes in taxpayer funds, statement of departmental expenses and capital expenditure against appropriations, statement of unappropriated expenses and capital expenditure and statement of cash flows for the year ended on that date and the notes to the financial statements that include accounting policies and other explanatory information.
- The non-financial performance information of the Department that comprises the statement of service performance on pages 47 to 64 and the report about impact indicators on pages 43 and 44.
- The schedules of non-departmental activities of the Department on pages 100 to 122 that comprise the schedule of assets, schedule of liabilities, schedule of contingent liabilities and contingent assets as at 30 June 2014, the schedule of expenditure, statement of appropriations, schedule of unappropriated expenditure, schedule of revenue, schedule of trust money and the schedule of movements between departments, for the year ended on that date and the notes to the schedules that include accounting policies and other explanatory information.

Opinion

In our opinion:

- the financial statements of the Department on pages 66 to 97:
 - comply with generally accepted accounting practice in New Zealand; and
 - fairly reflect the Department's:
 - financial position as at 30 June 2014;
 - financial performance and cash flows for the year ended on that date;
 - expenses and capital expenditure incurred against each appropriation administered by the Department and each class of outputs included in each output expense appropriation for the year ended 30 June 2014; and
 - unappropriated expenses and capital expenditure for the year ended 30 June 2014.
- the non-financial performance information of the Department on pages 43 and 44 and 47 to 64:
 - complies with generally accepted accounting practice in New Zealand; and
 - fairly reflects the Department's service performance and outcomes for the year ended 30 June 2014, including for each class of outputs:
 - its service performance compared with the forecasts in the statement of forecast service performance at the start of the financial year; and
 - its actual revenue and output expenses compared with the forecasts in the statement of forecast service performance at the start of the financial year.
- the schedules of non-departmental activities of the Department on pages 100 to 122 fairly reflect, in accordance with the Treasury Instructions:
 - the assets, liabilities, contingencies, commitments and trust monies as at 30 June 2014 managed by the Department on behalf of the Crown; and
 - the revenues, expenses, expenditure and capital expenditure against appropriations and unappropriated expenditure and capital expenditure for the year ended on that date managed by the Department on behalf of the Crown.

Our audit was completed on 29 September 2014. This is the date at which our opinion is expressed.

The basis of our opinion is explained below. In addition, we outline the responsibilities of the Chief Executive and our responsibilities, and we explain our independence.

Basis of opinion

We carried out our audit in accordance with the Auditor-General's Auditing Standards, which incorporate the International Standards on Auditing (New Zealand). Those standards require that we comply with ethical requirements and plan and carry out our audit to obtain reasonable assurance about whether the financial statements, the non-financial performance information and the schedules of non-departmental activities are free from material misstatement.

Material misstatements are differences or omissions of amounts and disclosures that, in our judgement, are likely to influence readers' overall understanding of the financial statements, the non-financial performance information and the schedules of non-departmental activities. If we had found material misstatements that were not corrected, we would have referred to them in our opinion.

An audit involves carrying out procedures to obtain audit evidence about the amounts and disclosures in the financial statements, the non-financial performance information and the schedules of non-departmental activities. The procedures selected depend on our judgement, including our assessment of risks of material misstatement of the financial statements, the non-financial performance information and the schedules of non-departmental activities, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Department's preparation of the financial statements, the non-financial performance information and the schedules of non-departmental activities that fairly reflect the matters to which they relate. We consider internal control in order to design audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control.

An audit also involves evaluating:

- the appropriateness of accounting policies used and whether they have been consistently applied;
- the reasonableness of the significant accounting estimates and judgements made by the Chief Executive;
- the appropriateness of the reported non-financial performance information within the Department's framework for reporting performance;
- the adequacy of all disclosures in the financial statements, the non-financial performance information and the schedules of non-departmental activities; and
- the overall presentation of the financial statements, the non-financial performance information and the schedules of non-departmental activities.

We did not examine every transaction, nor do we guarantee complete accuracy of the financial statements, the non-financial performance information and the schedules of non-departmental activities. Also we did not evaluate the security and controls over the electronic publication of the financial statements, the non-financial performance information and the schedules of non-departmental activities.

We have obtained all the information and explanations we have required and we believe we have obtained sufficient and appropriate audit evidence to provide a basis for our audit opinion.

Responsibilities of the Chief Executive

The Chief Executive is responsible for preparing:

- financial statements and non-financial performance information that:
 - comply with generally accepted accounting practice in New Zealand;
 - fairly reflect the Department's financial position, financial performance, cash flows, expenses and capital expenditure incurred against each appropriation and its unappropriated expenses and capital expenditure; and
 - fairly reflect its service performance and outcomes; and
- schedules of non-departmental activities, in accordance with the Treasury Instructions, that fairly reflect those activities managed by the Department on behalf of the Crown.

The Chief Executive is also responsible for such internal control as is determined is necessary to enable the preparation of financial statements, non-financial performance information and schedules of non-departmental activities that are free from material misstatement, whether due to fraud or error. The Chief Executive is also responsible for the publication of the financial statements, non-financial performance information and schedules of non-departmental activities, whether in printed or electronic form.

The Chief Executive's responsibilities arise from the Public Finance Act 1989.

Responsibilities of the Auditor

We are responsible for expressing an independent opinion on the financial statements, the non-financial performance information and the schedules of non-departmental activities and reporting that opinion to you based on our audit. Our responsibility arises from section 15 of the Public Audit Act 2001 and the Public Finance Act 1989.

Independence

When carrying out the audit, we followed the independence requirements of the Auditor-General, which incorporate the independence requirements of the External Reporting Board.

In addition to the audit we have provided assurance services over the Expression of Interest process for the Department's Business Transformation Programme, which is compatible with the independence requirements. Other than the audit and this assignment, we have no relationship with or interests in the Department.



Ajay Sharma

Audit New Zealand
On behalf of the Auditor-General
Wellington, New Zealand

Additional Information

Customer satisfaction

FIGURE 7 – CUSTOMER SATISFACTION WITH OUR VOICE AND CORRESPONDENCE CHANNELS[#]

Overall satisfaction	2012–13		2013–14	
Customer group	Satisfied	Very satisfied	Satisfied	Very satisfied
National results	82%*	64%*	85%*	68%*
Individuals (overall)	79%*	62%*	81%	64%
Working for Families Tax Credits	90%	69%	87%	72%
Child support	74%	52%	74%	54%
KiwiSaver (employees)	83%*	75%	88%	76%
Student loan	71%*	58%	79%	57%
Business (overall)	85%	66%*	88%*	71%*
Small and medium enterprises	84%	67%	90%*	73%*
Large enterprises	85%	68%*	86%	70%
Tax agents	87%	68%	89%	69%
Not for profits	82%	60%	84%	70%*
General public				
Contacted Inland Revenue in the last three months	86%	71%	87%	65%
Not contacted Inland Revenue in the last three months	76%	36%	76%	35%

[#] Phone service surveyed for the full 12 months, and correspondence for the last quarter only.

* Statistically significant difference at the 95% confidence level between 2012–13 and 2013–14. In the 2013 Annual Report we reported statistically significant difference at the 95% confidence level between 2011–12 and 2012–13.

FIGURE 8 – CUSTOMER SATISFACTION WITH OUR ONLINE SERVICES

Overall satisfaction Customer group	2012–13		2013–14	
	Satisfied	Very satisfied	Satisfied	Very satisfied
National results	94%	78%	95%	77%
Individuals (overall)	93%	75%	94%	75%
Working for Families Tax Credits	94%	76%	93%	75%
Child support	96%	78%	93%	72%
KiwiSaver (employees)	90%	76%	95%	79%
Student loan	91%	72%	93%	71%
No social policy	94%	75%	94%	78%
Business (overall)	96%*	81%*	96%	79%
Small and medium enterprises	95%	81%	95%	78%
Large enterprises	99%	83%	98%	84%
Tax agents	97%	82%	97%	77%
Not for profits	93%*	77%*	95%	78%

* In the 2013 Annual Report we reported statistically significant difference at the 95% confidence level between 2011–12 and 2012–13. No statistically significant difference at the 95% confidence level between 2012–13 and 2013–14.

FIGURE 9 – CUSTOMER PERCEPTIONS OF THE TAX SYSTEM

	2012–13		2013–14	
	Agree	Strongly agree	Agree	Strongly agree
Overall fairness	83%	54%	82%	53%
Overall operational effectiveness	83%	56%	82%	55%
Makes it easy to get it right	78%	46%	79%	45%
Appropriate action against non-compliance	80%	54%	79%	54%
Paying tax contributes to New Zealand	96%	86%	96%	86%

Debt tables

FIGURE 10 – COMPOSITION OF OUR DEBT PORTFOLIO AT 30 JUNE (\$ MILLIONS)

Debt type	2011	2012	2013	2014	One-year change	One-year change (%)
Debt under instalments	\$1,146.6	\$1,176.3	\$1,230.2	\$1,228.2	-\$2.0	-0.2%
Other collectable debt	\$2,663.5	\$2,582.7	\$2,561.5	\$2,621.6	\$60.1	2.3%
Tax collectable debt*	\$3,810.2	\$3,759.0	\$3,791.7	\$3,849.8	\$58.0	1.5%
Tax non-collectable debt**	\$1,711.9	\$2,157.4	\$2,186.4	\$2,390.3	\$203.9	9.3%
Total debt	\$5,522.1	\$5,916.4	\$5,978.2	\$6,240.1	\$262.0	4.4%
Working for Families Tax Credit	\$275.1	\$320.8	\$371.8	\$406.6	\$34.8	9.4%
GST	\$1,908.5	\$1,947.2	\$1,873.9	\$1,775.5	-\$98.4	-5.3%
Income	\$2,207.8	\$2,372.4	\$2,365.7	\$2,519.6	\$153.9	6.5%
KiwiSaver	\$19.8	\$21.5	\$22.5	\$33.3	\$10.8	48.2%
Other tax	\$76.6	\$100.1	\$121.6	\$121.8	\$0.2	0.2%
PAYE	\$622.6	\$642.1	\$586.8	\$613.9	\$27.1	4.6%
Student loan	\$411.7	\$512.3	\$635.9	\$769.4	\$133.5	21.0%
Total debt	\$5,522.1	\$5,916.4	\$5,978.2	\$6,240.1	\$262.0	4.4%
Tax penalties and interest	\$2,359.0	\$2,711.3	\$2,862.6	\$2,998.5	\$135.9	4.7%
Penalties and interest (%)	42.7%	45.8%	47.9%	48.1%		
Customers in debt (total cases)	389,947	408,606	436,299	435,360	-938.0	-0.2%
Annual debt change (%)	7.2%	7.1%	1.0%	4.4%		

Notes

*Collectable debt:

Debt cases where the assessment value is overdue and collections activity is in progress. This activity includes instalment arrangements, deduction notices, cases linked to legal actions and other manual or automatic actions.

**Non-collectable debt:

Debt cases where the assessed value is pending or in dispute and we are unable to proceed with collection activity at present. This includes cases:

- linked to investigations
- linked to objections
- pending write-off action
- with limited or no collection activity due to insolvency.

FIGURE 11 – AGE OF DEBT AT 30 JUNE (\$ MILLIONS)

Tax debt by age (\$ millions)	2011	2012	2013	2014	One-year change	One-year change (%)
< 1 year	\$1,377.7	\$1,254.7	\$1,245.6	\$1,298.9	\$53.4	4.3%
1–2 years	\$1,387.7	\$1,079.1	\$901.9	\$936.7	\$34.8	3.9%
2–5 years	\$1,787.7	\$2,310.9	\$2,304.8	\$2,204.6	–\$100.2	–4.3%
5–10 years	\$653.9	\$903.0	\$993.3	\$1,126.5	\$133.2	13.4%
> 10 years	\$315.1	\$368.6	\$532.7	\$673.4	\$140.7	26.4%
Total	\$5,522.1	\$5,916.4	\$5,978.2	\$6,240.1	\$262.0	4.4%

Core services costs

We track the cost of providing our core services, such as answering telephone queries and processing tax returns. Figure 12 compares those costs with targets and the previous year's results. We are encouraging people and businesses to do as much as they can online to lower the number of phone calls and items of correspondence we receive.

FIGURE 12 – COST INDICATORS

Indicator	2012–13 Actual	2013–14 Target*	2013–14 Actual
Cost per telephone contact	\$29.02	\$31.00	\$29.88
Cost per correspondence contact	\$38.31	\$41.00	\$37.80
Cost per counter contact	\$61.44	\$45.00	\$64.89
Average cost per customer initiated contact	\$32.92	\$34.00	\$33.00
Cost per income tax return processed	\$5.14	\$5.20	\$4.92
Cost per GST return processed	\$1.27	\$1.60	\$1.34
Cost per employer monthly schedule processed	\$4.67	\$6.20	\$5.14
Average cost per return processed	\$3.78	\$4.00	\$3.95
Cost of collecting an overdue return	\$9.13	\$15.00	\$5.60

* These figures are not subject to audit.

Information sharing with the Department of Internal Affairs

Under information-sharing regulations, Inland Revenue must report annually, for this approved information-sharing agreement, on actions taken during each financial year.

FIGURE 13 – INFORMATION SHARING WITH THE DEPARTMENT OF INTERNAL AFFAIRS (DIA)

Financial year ending 30 June 2014	
Contact records received from DIA	380,539
Contact records not matched to a corresponding Inland Revenue record for:	372,567
<ul style="list-style-type: none"> • overseas-based child support debtors • overseas-based child support non-debtors who do not appear to have up to date contact information • overseas-based student loan defaulters. 	
Contact records matched to corresponding Inland Revenue records for:	7,874
<ul style="list-style-type: none"> • overseas-based child support debtors • overseas-based child support non-debtors who do not appear to have up to date contact information • overseas-based student loan defaulters. 	
Ongoing programme operating costs	\$1,700 ³³
Individuals successfully contacted ³⁴ using contact records matched to:	
<ul style="list-style-type: none"> • overseas-based child support debtors • overseas-based child support non-debtors who do not appear to have up to date contact information • overseas-based student loan defaulters. 	937 73 2,310
Payments received from individuals as a result of successful contact with:	
<ul style="list-style-type: none"> • overseas-based child support debtors (201 payments) • overseas-based student loan defaulters (1501 payments). 	\$357,181 \$6.7 million
Percentage of individuals who have addressed ³⁵ their debt as a result of being successfully contacted by Inland Revenue:	
<ul style="list-style-type: none"> • overseas-based child support debtors • overseas-based student loan defaulters. 	23% 43%

³³ Approximate annual incidental administrative charge.

³⁴ We have made attempts to contact all 7,874 matched individuals, 3,320 have passed our three point identity verification process.

³⁵ Individual no longer has payments that are overdue.

In July 2014, the operation of this information sharing agreement was independently reviewed. The review has identified a number of improvement opportunities and we are currently taking the necessary steps to improve our processes.

A copy of the approved information sharing agreement is available to view on our website, www.ird.govt.nz

Privacy breaches

Our customers have concerns that when we share their information it may be disclosed inappropriately. We take privacy very seriously and we regularly review our systems and processes to prevent privacy breaches.

Following a potential privacy breach, Inland Revenue takes immediate steps to contain or limit it. This includes designating an appropriate individual to lead the initial investigation and determine who needs to be notified.

An appropriate evaluation takes place to determine what personal information was involved, the cause and extent of the breach, who was affected by the breach and whether those affected might be harmed.

When considering harm to individuals, Inland Revenue adheres to Part 8 section 66 of the Privacy Act 1993 (the Act), which sets out the strict circumstances under which interference and harm to individuals should be taken into account. In any case where there may be doubt, the Privacy Officer will discuss the case with the Office of the Privacy Commissioner.

We identified 287 instances (152 in the same period in 2012–13) where people's privacy may have been breached. Follow-up investigations established that in fact 241 (118 in the same period in 2012–13) had occurred.

These affected the privacy of 2,143 people. No interference or harm to any individual (with reference to section 66 of the Act) occurred as a result of these breaches. Five instances accounted for 86% of affected people. These are outlined in the table below.

FIGURE 14 – INSTANCES OF PRIVACY BREACHES

Detail	Number of affected people
One instance where Inland Revenue staff information was released to the PSA	1,616
Customer email addresses were visible in an external email sent (rather than being blind carbon copied)	140
Account statements were sent to the wrong tax agent	47
Customer details were sent to the wrong tax agent	25
Customer details for daily counter appointments were given to a single customer	16

The main cause of breaches is through staff manually handling correspondence (223 instances). We are taking measures to avoid these errors by reviewing handling processes, educating staff and regular performance reporting.

Capability and EEO

FIGURE 15 – EEO STATISTICS

	2011–12	2012–13	2013–14
Percentage of female staff	64%	64%	64%
Percentage of female team leaders	62%	63%	60%
Percentage of female managers	43%	45%	46%

FIGURE 16 – STAFF TURNOVER AND FTES

	2011–12	2012–13	2013–14
Staff turnover	11.8%	10.6% ³⁶	9.6%
Staff FTEs	5,301	5,475	5,641

³⁶ Figure recalculated for greater precision.

FIGURE 17 – PROPERTY INFORMATION (AT 30 JUNE)³⁷

	2012	2013	2014
Accommodation area (m ²)	100,736	101,678	93,439
Other area (m ²)	927	927	1,113
Total area leases (m ²)	101,663	102,605	94,552
Vacant accommodation (m ²)	5,571	1,003	0
Vacant m ² as a % of total m ²	5.5%	1%	0%
Average space per person (m ²)	17.4	17.9	15.5
Annual rental per person	\$5,760	\$5,727	\$5,410
Utility costs per person	\$823	\$799	\$773
Total occupancy cost per person	\$6,583	\$6,526	\$6,184

FIGURE 18 – EXPENDITURE ON CONSULTANTS AND CONTRACTORS

	2011–12	2012–13	2013–14
Total expenditure on consultants and contractors (\$000)	\$47,305	\$52,907	\$59,191
% of total operating expenditure	7.0%	8.1%	8.5%
% of total capital and operating expenditure	6.5%	7.5%	7.9%

FIGURE 19 – BREAKDOWN OF EXPENDITURE ON CONSULTANTS AND CONTRACTORS

	2011–12 Actual \$000	2012–13 Actual \$000	2013–14 Actual \$000
Information technology	14,023	17,882	20,481
Specialist advice and project management	26,552	29,151	31,436
HR and change management services	938	778	2,225
Tax issues	1,473	669	1,179
Property	1,964	2,074	2,023
Research	1,448	1,113	1,325
Communications	156	343	123
Other	751	897	399
Total	47,305	52,907	59,191

³⁷ Data in the table is calculated using staff headcount.

Evaluating our work programmes

We measure our effectiveness through evaluating our work programmes. The findings help us understand the factors that contribute to their success or why they are not working as intended. This year, we evaluated the effect of KiwiSaver on savings and remuneration, and considered this in relation to government costs. We published an evaluation report on the seven years' evaluation of KiwiSaver.

We evaluated how the new ways of repaying student loan obligations improved student loan repayment and debt levels.

We are evaluating Better Public Services Result 10 initiatives.

Our evaluation reports are available at:
www.ird.govt.nz/aboutir/reports/research/
