Inland Revenue
Te Tari Taake

Communications & Inquiry
Whakawhiti Kōrero me te Pakirehua

National Research and Evaluation Unit
Te Wāhanga ā-motu mo te Rangahau me Aromātai

DEMAND FOR AGGRESSIVE TAX PLANNING

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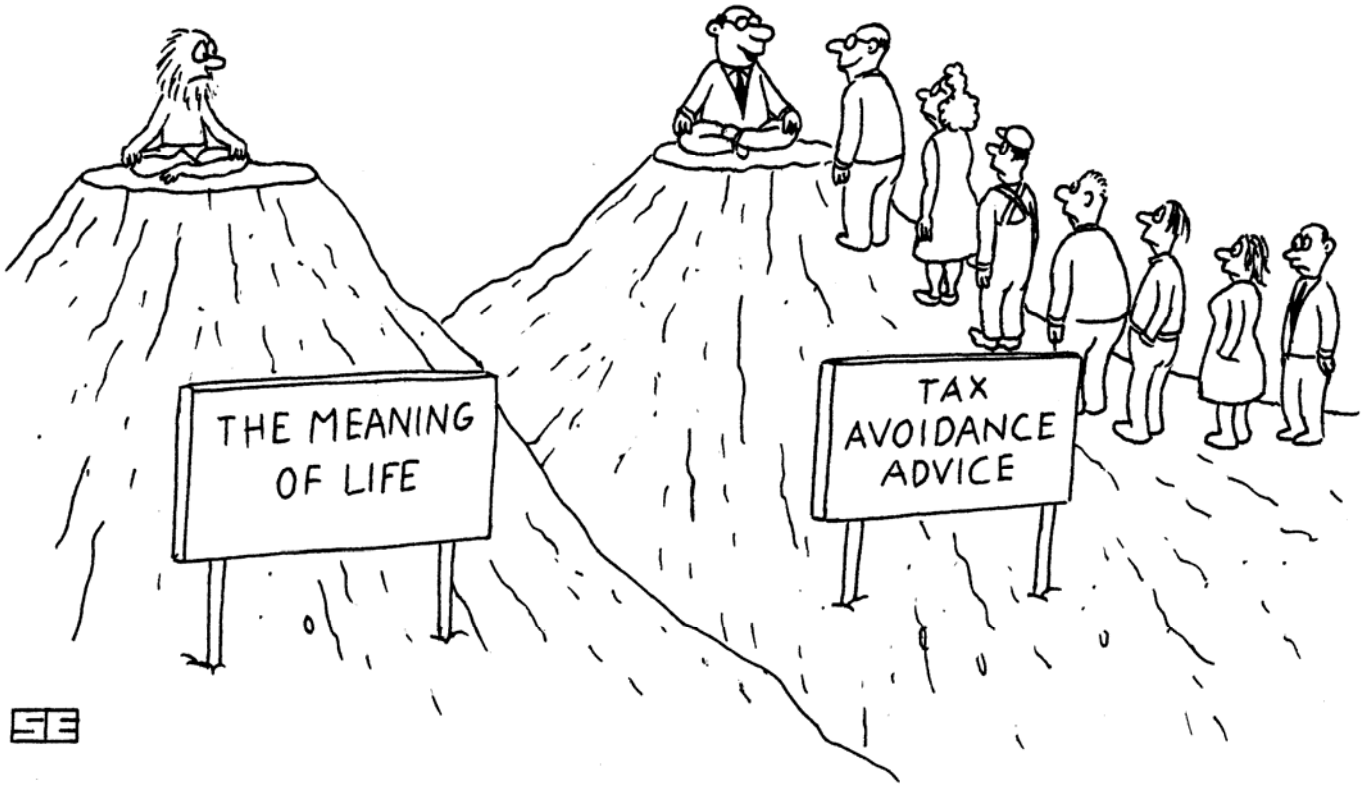
Background

- Aggressive Tax Planning (ATP)
  - is about following the letter of the law but not its spirit
  - generally reducing income or inflating expenses
  - often involves contrived arrangements for little economic sense

- Tax administrations all over the world are working to respond to ATP
  - undermines the public trust in the tax system
  - creates inequalities and reduces tax revenues

Objective

- Investigate the factors and attitudes behind customers' demand for ATP



Method

- ATP risk cases identified by investigators

- Qualitative interviews with Inland Revenue staff (x8), ATP risk customers (x22) and tax agents (x20) to; identify ATP characteristics, and understand each perspective

- Statistical analysis
  1. Latent Class Analysis (LCA) – Customer Profiling
     - for finding subtypes of latent classes from multivariate categorical data.

  2. Canonical discriminant function analysis
     - Confirmation of Clusters determined through LCA
     - To find rules for classifying objects given a set of pre-classified objects.

ATP Individual Customers - Profile	%	Wider population (Individual)
• Male	80%	50%
• 45+ years of age	90%	43%
• Auckland location	60%	35%
• Self-employed	64%	8%
• Professional/technical	20%	7%
• Financial/insurance services	20%	3%
• Rental/hiring/real estate	19%	1%
• On-time filing of tax	50%	60%
• On-time payment of tax	60%	85%
• Income $60,000+	63%	10%
• Expense claims $10,000+	24%	1%

ATP Business Customers - Profile	%	Wider population (Business)
• Business age 10-20 years	67%	29%
• Auckland location	60%	34%
• Finance/insurance services	22%	3%
• Rental/hiring/real estate	18%	1%
• Professional/scientific/technical	17%	7%
• On-time filing of tax return	66%	72%
• On-time payment of tax	82%	84%
• Business turnover $500,000+	29%	3%
• Profit (i) $60,000+	30%	6%
• Profit (ii) $500,000+	11%	1%
• Expense claims $250,000+	32%	22%

Role of Tax Agents

More than 89% of ATP Individual customers had a tax agent

More than 80% of ATP Business customers had a tax agent

"The current tax law is over the heads of most clients and also for many accountants." (Tax agent)

ATP customer-tax agent relationship types

1. Customer keeps agent at a distance

"They don't want to reveal information to the agent, won't give the facts, not transparent." (IR staff)

2. Customer proactive with agent

"[The customer] wanted 10% off the tax bill, they didn't care how." (IR staff)

3. Customer leaves everything to the agent

"Inland Revenue defines this as tax avoidance and thinks we should know better, but we trusted our accountant." (Customer)

4. Customer reactive to agent

"Agents consider avoidance and come up with two or three commercial reasons and say 'we should get over the line'." (IR staff)

ATP Customer segmentation - Individuals

Clusters

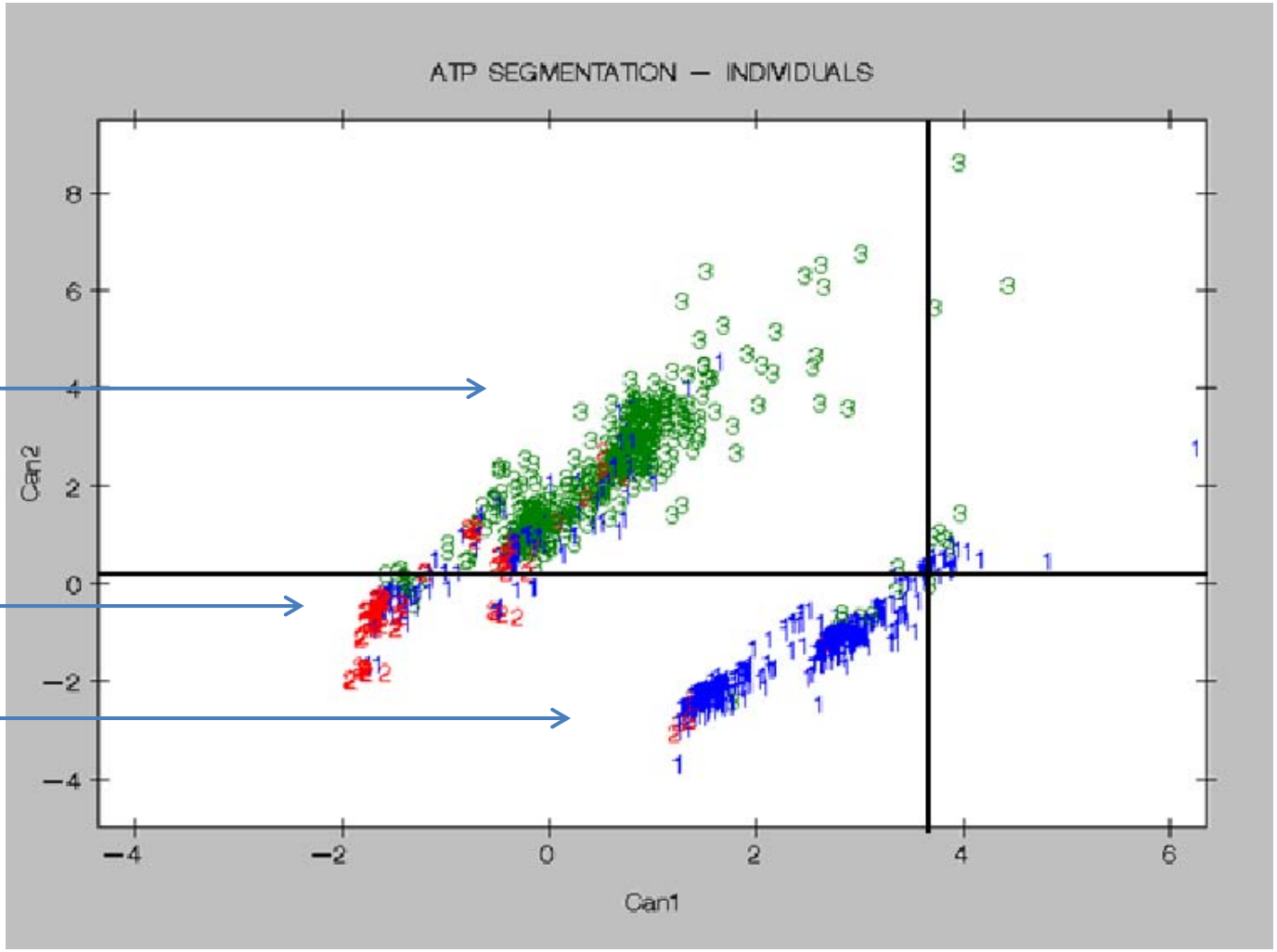
3 = ATP Risk cluster

2 = 'Opportunist' cluster

1 = Non-ATP cluster

'Can' = Canonical variable

Error rate 10%



ATP Customer segmentation – Businesses

Clusters

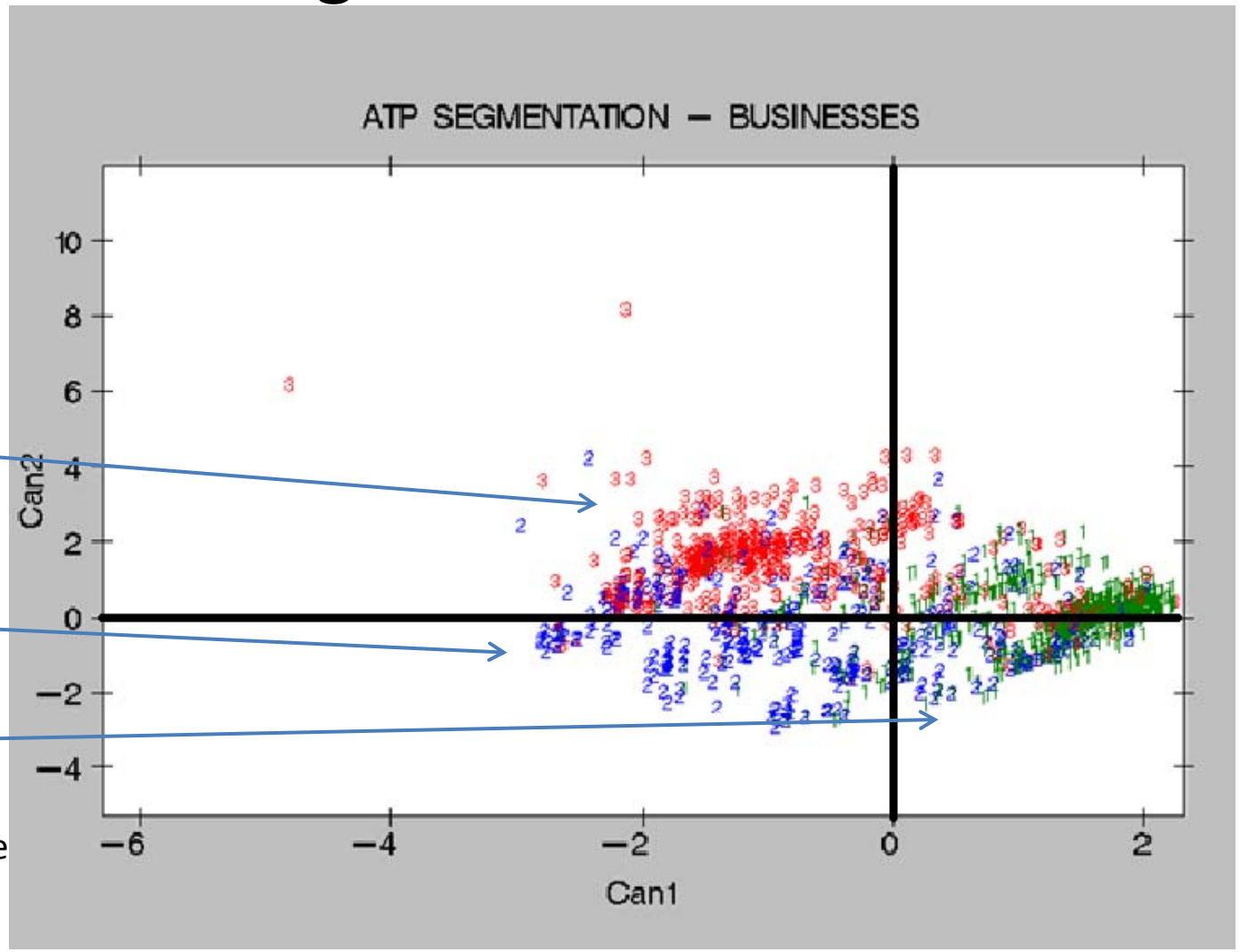
3 = ATP Risk cluster

2 = 'Opportunist' cluster

1 = Non-ATP cluster

'Can' = Canonical variable

Error rate 19%



Discriminators of ATP

	Primary Discriminators	Secondary Discriminators	Minor Discriminators
Individual customers	Lower administrative compliance Linked to tax agents	Annual income after expenses Individual age Liabilities Professional services	Travel expense claims Real estate and financial services Tax credit claims Donations paid
Business customers	Lower administrative compliance Business growth Linked to tax agents	Business age Liabilities	Auckland Finance and insurance services Annual turnover

ATP on a tax planning spectrum

1. Customers with minimal tax planning opportunity

2. Customers with conservative tax planning attitudes

3. Customers keen to minimise tax

(a) Focussed on legal correctness

- Transactions have both commercial reasons and tax advantages
- Expect tax law to be specific

(b) Focussed on ATP

"I'd say we have 5 - 10% of clients who like to take more of a risk in business activities, 40 – 50% want to keep IR happy and the rest are happy to do some sort of tax minimisation but without going too far so that IR will come back and have a go at them." (Tax agent)

Tax Morale has two levels

Social responsibility
to pay tax

HIGH

"It's essentially not our money, it's the government's money." (Customer)

Meeting the **intent** of the tax legislation

LOW

"I don't believe I should be paying more tax than I have to. I have successful businesses that pay a lot of tax. Why should I pay more?" (Customer)

Final comments: 1 – Responsibility for ATP

- People expect their tax planning to be judged according to written legislation – not happy with the 'spirit of the law'

- People expect their tax agent to get their taxes right, and may not feel responsible for their ATP risk

2 - Identifiable characteristics

- ATP Individual customers stand out – high use of tax agents, professional occupations, use of expense claims

- ATP business customers are harder to distinguish – slightly lower compliance rate and slightly higher use of tax agents

- Segmentation indicates a secondary group of 'opportunists' who need the same attention for ATP