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Minister of Revenue

Minister of Tertiary Education, Skills and Employment

More tools to improve overseas-based borrower compliance

Executive summary

During the joint Ministers' meeting on Tuesday 25 May 2012 officials were asked to report back on whether any further policies or tools are required to increase the rate of compliance amongst overseas-based borrowers.

The overseas-based borrower compliance initiative (the initiative) commenced as a one year project in October 2010 and was scaled up in August 2011 for a further three years. This paper firstly reviews the work already completed and the components still in the pipeline.

This review then sets the scene for our analysis of the drivers of non-compliance and the challenges we face in addressing that non-compliance.

A lack of awareness of their obligations, and an indifferent attitude towards those obligations, remains the key driver behind borrowers shifting from high compliance while in New Zealand to poor compliance while overseas.

The lack of quality contact details continues to make it difficult to educate borrowers or take enforcement action. Once borrowers are contacted approximately 70% comply but further tools and levers would help to improve compliance without the need for expensive legal action.

To lift borrower awareness we recommend developing a communications strategy targeting borrowers before they leave New Zealand.

To improve the quality of contact information we recommend working with the Department of Internal Affairs (Internal Affairs) to establish a long-term data match for contact information from passport renewal applications.
[2]

[2]

Border interventions would apply to the most resistant borrowers. Given Inland Revenue already has tools at its disposal for such non-complaint borrowers, restricting travel would apply narrowly with the main benefit being that of signalling to borrowers that there are potentially serious consequences for non-compliance.
[2]

Further details on this package are supplied in the latter sections of this paper along with information on options that have either not been recommended or were considered out of scope.

Recommended action

We recommend that you:

- a) **Note** the work completed to date by the initiative, the work that is in the pipeline, and the effect this work is expected to have on overseas-based borrower compliance.

Noted

Noted

- b) **Note** that the lack of awareness of and attitude towards their obligations remains the key drivers of non-compliance; the lack of quality contact information and current set of compliance tools is the primary impediment in addressing this non-compliance.

Noted

Noted

- c) **Agree** that Inland Revenue report back on a range of packages for a communications strategy targeting borrowers before they leave New Zealand.

Agreed/Not Agreed

Agreed/Not Agreed

- d) **Agree** that Inland Revenue work with Internal Affairs to establish a long-term data match for contact information from passport applications.

Agreed/Not Agreed

Agreed/Not Agreed

[2]

[2]

Agreed/Not Agreed

Agreed/Not Agreed

[2]

Noted

Noted

[1]

Senior Policy Advisor
Policy Advice Division

Hon Peter Dunne
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Hon Steven Joyce
Minister for Tertiary Education,
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Background

1. In the years leading up to 2010 Inland Revenue had been struggling to collect loan repayments from overseas-based borrowers. These borrowers were able to default without repercussion, creating serious equity problems in the Student Loan Scheme. Overseas-based borrowers were able to avoid their repayment obligations because they were outside New Zealand's tax system while New Zealand-based borrowers were not.
2. In August 2010 Cabinet agreed that Inland Revenue should self-fund a year-long initiative in Australia using a commercial debt recovery approach to target overseas-based borrowers in default. At the time, based on independent private sector advice, the initiative was expected to break-even - a 1:1 return on investment. The primary benefits of the initiative would stem from an overall lift in compliance rates from borrowers who would observe Inland Revenue taking action against defaulters.
3. The initiative commenced at the end of October 2010 and by 30 June 2011 \$3.5 million of payments had been received at a cost of \$573,000 – a return on investment of 6.1:1. In addition to the monetary return the initiative had generated widespread, positive public and media interest. In August 2011 Cabinet agreed to fund a \$12.44 million scale up of the initiative which would run for three years and target borrowers in Australia and the United Kingdom. A return on investment of 3:1 was expected, recognising that more expensive interventions, such as legal action, would likely bring the rate down from 6.1:1.
4. The cumulative return on investment from the start of the initiative in October 2010 through to 31 July 2012 is 11.4:1 or \$11.40 received for every \$1 spent.
5. During the joint Ministers' meeting on Tuesday 25 May 2012 officials were asked to report back on whether any further policies or tools are required to increase the rate of compliance amongst overseas-based borrowers. This paper considers the work already completed or in the pipeline; revisits the drivers of non-compliance and the factors that impede addressing that non-compliance in light of the experience to date; and recommends a package of options.

[2]

The initiative to date

7. Moving from the New Zealand-based borrower regime, that mostly works invisibly behind the scenes through the PAYE system, to the overseas-based borrower regime, which requires an active exchange of assessments and payments, would be challenging for a borrower at the best of times. For many borrowers leaving New Zealand their loan obligations are not high on their priority list and the need to keep Inland Revenue informed of their contact details is frequently forgotten.

9. Since its commencement in October 2010, the initiative has focussed on a programme of debt prevention and recovery including direct and indirect campaigns, legal action and improving payment methods.

10. Direct campaigns have been successful in recovering arrears from borrowers who have been located either through their existing contact details or through track and trace activities.

11. Indirect campaigns have focussed on providing education and encouraging compliance in the wider borrower population through online advertising via news websites such as www.stuff.co.nz as well as Facebook and Google. These have resulted in increased collections from borrowers who have responded to campaign messages without needing to be directly contacted.

12. Legal action is underway against a group of borrowers who have refused to comply following contact through the direct campaigns. In July 2011 a group of 45 borrowers were notified that legal proceedings would commence if payments were not received. At the time of writing only 17 borrowers remain non-compliant, the rest either clearing their arrears or coming to an arrangement.

13. Payment methods for overseas-based borrowers have been expanded and borrowers now have straightforward, cost-free options available to meet their obligations. Payments can now be made online and over the telephone via debit or credit card and through Orbit Remit, a payment company with Australia and the United Kingdom coverage in particular, which does not pass any additional costs on to their customers.

In the pipeline

14. Some components of the initiative, as well as some policy changes from Budget 2011 and Budget 2012, have yet to be implemented but will have a positive impact on overseas-based borrower compliance. These items are briefly outlined below so that they can inform any consideration of further policy change.

In the shorter term (the next 3 months)

Further payment options	<p>Negotiations are underway with other international money transfer organisations which will provide more options for borrowers seeking to pay their obligations.</p> <p>In addition, Inland Revenue is currently finalising an “online direct debit” payment option through WestPac Australia. This option utilises an existing service, but will allow Inland Revenue staff to set up online direct debit arrangement with the borrower while on the phone. This service is for borrowers in Australia only.</p>
Legal action	Legal action commenced in July 2011 continues with 17 cases at

	<p>various stages of proceedings. Once judgment is obtained in New Zealand the judgment will be transferred through the High Court to an equivalent court in Australia to commence debt recovery.</p> <p>Contracts are being finalised with private-sector providers to undertake the management of the legal cases transferred to Australia and the subsequent debt recovery actions. This may include asset seizure and bankruptcy.</p>
Private sector debt collection	An open Request for Proposal is being finalised, and will be placed on the Government Electronic Tender Service to invite private sector debt collection agencies to engage in the provision of debt services, primarily in Australia and the United Kingdom, but also with global coverage as required. Once in place, this will enhance Inland Revenue's ability to track and trace as well as undertake debt collection activities in the borrower's country of residence.
Private sector track and trace	Discussions with two private sector agencies are underway to determine the cost of contracting out the track and trace activities needed to locate a further 6,300 borrowers believed to be resident in Australia.

In the medium term (the next 3 to 9 months)

Customs data match	A new data match with Customs is being developed which will locate borrowers in serious default as they enter the country. Information from arrival cards will be used to contact borrowers while they are in New Zealand and initiate debt recovery action. This will be particularly useful for borrowers who have permanently left New Zealand but who periodically return due to family ties etc.
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In the longer term (more than 9 months)

Alternate contact person	<p>Borrowers leaving New Zealand and applying for a repayment holiday now have to supply a New Zealand-based contact person. For the 2013 academic year onwards students wishing to borrow from the Student Loan Scheme will also need to provide a contact person.</p> <p>In the event the borrower defaults and cannot be located, the contact person can be asked to either talk to the borrower or provide the borrower's contact details. While these changes will take time to filter through they are expected to improve the compliance of borrowers travelling overseas in the future.</p>
Government wide payment service	Inland Revenue, the Ministry of Justice and the Ministry of Social Development have started exploratory work to test the feasibility of a government wide approach for the supply of overseas payment services.

Problem definition revisited

15. The non-compliance of overseas-based borrowers still stems from a **lack of awareness** of, and an indifferent attitude towards, their obligations. The **lack of quality contact details** continues to make it difficult to educate borrowers or take enforcement action. Once borrowers are contacted

Inland Revenue's experience is that approximately 70% comply but **further tools and levers** would help to improve compliance without the need for expensive legal action.

Lack of awareness

16. Debt prevention is always preferable to debt recovery and Inland Revenue's ultimate aim is to have as high a proportion as possible of overseas-based borrowers complying with their obligations from the point they leave the country.

17. While Inland Revenue will continue to target overseas-based borrowers through a range of channels, there needs to be a comprehensive communications strategy aimed at borrowers while they are in New Zealand. Such a strategy would:

- prevent non-compliance by educating borrowers before they go overseas;
- reach New Zealand family and friends of borrowers already away; and
- encourage borrowers to remain compliant.

18. A successful communications strategy that informs borrowers of their obligations and the systems and processes supporting them as they travel, would not only increase the rate of compliance but also improve the quality of contact details, the take up of the repayment holiday and the provision of alternate contact persons.

Lack of quality contact details

19. The key impediment to collecting loans from overseas-based borrowers when the original scaling-up initiative began in 2010 was the lack of quality contact information. This continues to be the case.

20. Inland Revenue needs reliable and sustainable sources of contact information, either from external data sources or through leverage that encourages overseas-based borrowers to provide their details.

21. Inland Revenue has been tracing overseas-based borrowers by dedicating its own staff to researching their whereabouts. While delivering some success, tracing overseas-based borrowers is not Inland Revenue's comparative advantage given its role as a tax collection agency. For this reason Inland Revenue will be introducing a customs data match and engaging private tracing agencies to supplement its own efforts.

22. The most effective addition to this set of tracing tools would be an established source of contact information from the Department of Internal Affairs for overseas-based borrowers that renew their passports. From the initial testing Inland Revenue believes this will provide a reliable and efficient source of information long-term.

[2]

Further tools and levers

23. Once contact is successfully made, the borrower needs to be persuaded to make payment or come to an arrangement. Currently approximately 70% of overseas-based borrowers in default become compliant once they are contacted.

24. At the moment, Inland Revenue's key leverage is suited to targeting those of the remaining 30% of borrowers that continuously resist paying.

25. Legal action is effective against resistant borrowers (of the 45 cases taken only 17 have resisted paying until the court stage). However, this approach is time consuming and expensive. A case can be brought against an overseas-based borrower simply to affect their credit rating (e.g. if their assets are insufficient to cover their arrears), but the costs of this approach appear to outweigh the benefits.

26.

[2]

27. Inland Revenue is in the process of engaging overseas private debt collection agencies to provide Inland Revenue with a compliance option that does not require as much effort and expense as legal action.

28. Measures that act as a strong deterrent to a wider group of borrowers and that do not commit significant Inland Revenue resources would complement the department's existing tools.

[2]

29. Border interventions would apply to the most resistant borrowers. Given Inland Revenue already has tools at its disposal for such non-complaint borrowers, restricting travel would apply narrowly with the main benefit being that of signalling to borrowers that there are potentially serious consequences for non-compliance.

[2]

30. In summary, Inland Revenue proposes to:

- recommend to Ministers that Inland Revenue report back on a range of packages for a communications strategy targeting borrowers before they leave New Zealand;
- investigate alternative sources of contact information using of section 17 of the TAA;
- recommend to Ministers that Inland Revenue work with Internal Affairs to establish a long-term data match for contact information from passport applications;

[2]

31. Further details on this package are supplied below along with information on options that have either not been recommended or were considered out of scope.

Addressing the lack of awareness

A preventative communications strategy

32. The long term health of the overseas-based borrower regime is best protected by ensuring compliance from those about to go overseas so that progressively more and more borrowers meet their obligations from the get go. Preventing non-compliance starts at home as the best opportunity to reach the borrower is before they leave New Zealand.

33. Research from Colmar Brunton highlighted the positive impact of borrower's New Zealand-based networks in overseas-based borrower compliance. This suggests that a New Zealand-based communications campaign could also influence borrower behaviour both directly before they leave and indirectly through their social networks in New Zealand.

34. As outlined in paragraph 7 borrowers often do not have to make any effort to comply in New Zealand, whereas they must take specific actions to comply whilst overseas. Shifting borrowers from a passive state to an active state requires a significant change in behaviour. This kind of shift is only achievable via a dedicated communications strategy.

35. If Ministers approve further work in this area officials will report back with a range of packages for such a communications strategy.

Addressing the lack of contact details

Receiving contact details from passport applications

36. Borrowers applying for passport renewals provide their contact details to Internal Affairs. These contact details are likely to be extremely accurate as the applicant is relying on them to receive their passport or to respond to any questions that arise during the renewal process.

37. Earlier this year Inland Revenue made a request to Internal Affairs under section 17 of the TAA for the details of all passport renewal applications made in the last three months. This request was made so that the passport renewal process could be evaluated as an on-going source of contact information and would enable collection activity to commence.

38. The records were received in early July and were matched against Inland Revenue's files to identify those applicants with student loans. Of the 134,000 renewal applications received over the three month period, 15,927 were identified as student loan borrowers. Preliminary analysis shows that 2,938 are overseas-based borrowers, with approximately 50% (1,424) having an overdue repayment obligation. These borrowers have total loan balances of \$83 million, of which over \$10 million is in default.

39. These details will now be used by the debt recovery teams to test the quality of the information received. While the information is likely to have been accurate at the time it was supplied it is up to three months old and some borrowers may have moved on in the intervening period.

40. Nevertheless, these initial results suggest that the passport renewal process will be a valuable on-going source of contact details. If Ministers approve further work in this area officials will consult with Internal Affairs and the Office of the Privacy Commissioner to scope the cost and impact of a permanent information sharing agreement.

Section 17 requests

41. Section 17 of the TAA provides Inland Revenue with broad powers to request information from individuals, businesses, non-profit organisations and Government agencies for the purposes of administering and enforcing the Inland Revenue Acts¹. These requests can be made narrowly, such as a request to a bank for the notes relating to a specific meeting between a taxpayer and their bank manager, or broadly, such as a request to Internal Affairs for a list of recent immigrants for the purposes of targeting advice.

[2]

Developing further tools and levers

[2]

Border interventions

48. We have previously reported on proposals to impose travel restrictions on borrowers with significant levels of default (PAD2010/324 – *Overseas-based borrowers – powers to assist compliance*; and PAD2011/52 - *Student loan scheme* [2] *border related proposals* refer).

49. Overseas-based borrowers may still retain a connection with New Zealand, such as friends, family, sporting or business interests, which will lead them to return to New Zealand from time to time.

¹ The Inland Revenue Acts comprises the legislation administered by Inland Revenue and includes the Student Loan Scheme Act 2011.

50. The Student Loan Scheme Amendment Bill 2012 will legislate for a new information match between Inland Revenue and the New Zealand Customs Service to identify borrowers in serious default as they cross the border. When targeted borrowers enter New Zealand the information from their arrival card will be used by Inland Revenue to initiate contact with the borrower.

51. Some borrowers, once contacted, will refuse to comply. These borrowers may feel that all they need do is keep their heads down, wait for their flight out of the country, and once again be out of reach.

52. Introducing some kind of travel restriction, such as a power of arrest, would send a clear message to all borrowers that non-compliance is unacceptable and would provide greater leverage over those who temporarily return to New Zealand.

53. While a serious step, raising Bill of Rights concerns relating to freedom of movement, there is an equivalent existing power under the Child Support Act 1991. Officials recommend public and inter-agency consultation prior to the introduction of an arrest power or other travel restrictions.

[2]

55. If Ministers request further work in this area officials will consult with the New Zealand Customs Service, the Ministry of Justice and the Police to identify the costs and impacts of enforcing and communicating travel restrictions.

[2]

[2]

Credit ratings in Australia

61. In order to undertake legal action in Australia, such as asset seizure or bankruptcy, Inland Revenue must obtain judgment in New Zealand and then have that judgment transferred through the

High Court to an equivalent court in Australia. After the judgment is lodged in Australia the debt becomes recognised under Australian law and can affect the borrower's credit rating in Australia.

62. This would have a direct effect on defaulters applying for credit and, with the necessary publicity, an indirect effect on borrowers more widely who wish to maintain their credit rating. This may be a useful tool for borrowers who refuse to engage but whose debts or assets make full legal action unattractive. Inland Revenue will explore whether lodging judgments in Australia in order to affect credit ratings is a useful compliance tool.

Options not recommended

63. This section summaries the options that have not been recommended in this paper.

Resources

64. As of July 31 2012 the initiative has a return on investment of 11.4:1 or \$11.40 received for every \$1 spent. One option to build on the success of the initiative would be to increase the funding available to increase the scope of the current activities.

65. Inland Revenue has completed the recruitment and training of 40 additional staff to focus on overseas-based borrower cases and work with private debt collection agencies on debt-recovery activities in Australia and the United Kingdom. The \$12.44 million approved by Cabinet for the three year scale-up of the initiative will also cover up to 10 additional resources to bring the total staff numbers up to 50, if required.

66. These staff primarily undertake both direct debt recovery from borrowers with valid contact details and the tracking and tracing of borrowers who cannot be located. Debt recovery activity offers the highest return on investment as successful actions translate directly into money received. Track and trace activity offers a lower return as successful cases must then be actioned by the debt recovery team before money is received.

67. Presently Inland Revenue has sufficient staff to complete all of the debt recovery actions for borrowers who can be located. Deploying additional staff now would mean investing in less profitable tracking and tracing activity. While the lack of contact information remains the major constraint in improving compliance, we believe this problem is best addressed by identifying and building access to sustainable sources of quality information.

68. In time we expect the number of borrowers with up to date contact information to increase as a result of either the activities currently underway or because we have found a sustainable source of quality information. At this point we cannot accurately estimate the number of staff that would be needed to respond to this expected improvement in information quality.

69. Should staff numbers become an issue in the future we will revisit the allocation of resources within Inland Revenue and, if appropriate, report to Ministers then with options to increase recovery rates.

Changing the structure of the regime

70. This paper has considered options that will improve borrower's compliance with the existing overseas-based borrower regime. Structural changes to the regime (the one-year repayment

holiday, the annual repayment obligations, the imposition of interest) have not been considered as part of this paper.

71. If changes were made to the regime then we would expect that options included in this paper would still improve compliance irrespective of any changes made.

Implementation and funding

72. Inland Revenue's work programme has a number of significant projects currently underway, including major deliverables in 2012 and 2013 for student loans, Budget 2012 and reforms in Child Support in 2013 and 2014. Any additions to the student loans work programme will require further explicit trade-offs as to which initiatives should be deferred, scaled-back or removed from Inland Revenue's work programme. However, resources have been anticipated for the delivery of Budget 2013 initiatives. Those resources will be applied to the wider tax policy initiatives in Budget 2013, not just student loans. Whether those resources are sufficient will depend upon the significance, in particular the systems requirements, of the overall Budget 2013 package.

73. Inland Revenue is also managing significant fiscal pressures over the next few years including investment into transformation initiatives, self-funding other policy initiatives and the escalating costs of supporting aging technology infrastructure. Inland Revenue is not in a position to absorb further operating costs and with the restrictions on the use of depreciation funding [CAB Min (12) 10/3A] on capital costs, Inland Revenue will likely seek funding for both operating and capital costs.

74. As a consequence, Inland Revenue will be subject to the Treasury Better Business Case requirements to provide an opportunity for all implementation options to be extensively considered and evaluated.

75. If Ministers approve further work on the options in this paper Inland Revenue will carry out a feasibility analysis for implementing these changes. This will inform a high level (low confidence) view of the resources and funding required and will in turn determine if the proposed changes will be subject to the Better Business Case requirements.

Overseas child support debt

76. This paper only considers options that would specifically address the non-compliance of overseas-based borrowers. Collecting student loans from overseas-based borrowers is similar in certain respects to collecting child support from non-resident parents: contact details are crucial but often lacking and enforcement is difficult outside of New Zealand.

77. Should Ministers agree to further work on any of the recommendations in this paper, officials will investigate and report on whether those options may also hold value for child support.

Consultation

78. The Ministry of Education, Ministry of Social Development (StudyLink) and the Treasury have been consulted.

79. The Department of Internal Affairs, New Zealand Customs Service and the Ministry of Foreign Affairs and Trade were consulted on [2] border related proposals during the development of the earlier policy papers. Further consultation with these agencies will occur should Ministers agree to further work on these proposals.