

# **Inland Revenue response to Payments NZ consultation on payments for the next generation**

April 2025



Inland Revenue is supportive of the need for modernisation of the payment's capability in New Zealand. We generally support the approach and the headline benefits as outlined in the consultation document. Our responses cover a range of considerations and ideas for the future of the payment's ecosystem in New Zealand. None of them are to be construed as indicative of a specific choice that Inland Revenue has made with respect to how we may invest in payments systems in the future, nor any commitment as to what tax administration in New Zealand may look like in the years to come.

A well-functioning revenue ecosystem hinges on a payments system that

1. Minimises friction for citizens and businesses to make and receive payments
2. Is safe and secure - minimises the potential for fraud and errors
3. Creates greater certainty in the payment (made to the right target for the payer and received on time by the receiver)
4. Enables more choices for all parties to a payment transaction
5. Permits traceability, auditability and transparency, while complying with privacy rights and respecting privacy rights of all parties
6. Is reliable, available, fault tolerant, able to provide service during force majeure events (offline payments) and resilient
7. Allows the possibility to embed payments within natural business systems
8. Accommodates additional value creation within the payment channel
9. Enables broader participation in the payment's ecosystem
10. Promotes financial inclusion, specifically digital financial inclusion
11. Is efficient and cost effective to operate
12. Is flexible and able to adapt to changing technology and standards

We note that there has been recent progress on delivering new payment system functionality such as the introduction of confirmation of payee and the deployment of open banking-based solutions. We will be keen to work with the industry to play a role in the development of next generation payments capability.

#### 1. **Role of Government in modernising payments**

- a. Government agencies are significant customers of the payments system and are focused on maximising the efficiency and effectiveness of their services to customers including payments.
- b. A trusted payments system is integral to delivery of government services. The role of government and the regulator is to ensure stability (critical for a functioning tax system) but also to foster innovation. Our observations of the experience in other jurisdictions would lead us to the view that New Zealand has fallen behind our peers in the payments arena in terms of providing greater choice and functionality to payments users. The experience of the HMRC in the UK is an example of how Open Banking can be leveraged to provide greater convenience to consumers.
- c. Inland Revenue is one of the largest recipients of payments in New Zealand, both in the government sector as well as the private sector. Inland Revenue made \$42bn in outward payments (c.14m transactions) and received \$152bn in payments (c.14m transactions) in the 2024 year. We touch every citizen and business in the country as well as many customers located outside of NZ's borders.

- d. Many payments events have an element of tax involved in them. This may be GST collected on a sale, or RWT withheld on an interest payment or PAYE collected on a salary payment. The payment of that tax to Inland Revenue, accompanied by accurate information and data related to that payment, is critical to the Government being able to collect revenue. Likewise, an equally large volume of payments is driven by social policy products such as student loans, KiwiSaver, child support etc.
- e. In addition, refunds and disbursements made by IR need to be accurate (paid to the correct account), timely, and notified to give the recipient certainty that they have received what they are due.
- f. It is imperative that any design for modernising the payments infrastructure should take into consideration the needs of Inland Revenue and other Government agencies. The following points are a snapshot of some of the concerns and opportunities we see in the payments space.

## 2. **Ease/ convenience of payments**

- a. The current payments infrastructure does not provide sufficient choice for consumers. It should be possible for a customer to make a payment to Inland Revenue from the application (*natural system*) of their choice and using a source of funds of their choice (card, bank account, digital wallet etc.). We see it as simplifying the option to pay with your own money and from your *natural environment*.
- b. Likewise, it should be possible for a customer to receive a payment from us, be it a tax refund or a social policy related payment, direct to a destination of their choice.
- c. The possibility of a CBDC – digital cash – creates immense potential to fulfil some of the need for a frictionless payment mechanism and should be an integral part of design considerations.
- d. Cross-border payments are still too expensive, cumbersome and time consuming. Inland Revenue collects large volumes of tax and social policy payments from overseas based parties. Simplifying the ability to make a cross-border payment and reducing the cost to do so would facilitate compliance for our customers. As the collector of a student loan book with overseas based borrowers, any means to make cross-border payments simpler, quicker and less expensive would be welcome.
- e. Accessibility and inclusion for all citizens is critical to a government agency. Growing the ease of making payments can grow financial inclusion and digital financial inclusion<sup>1</sup>. As a government agency, this is important to us as it aligns with our organisational goal of improving Oranga for all New Zealanders. We must also ensure that in our desire to deliver a next generation payments platform, we do not leave the previous generation behind.

## 3. **Real-time payments and digital interactions**

- a. Data Rich payments - The advent of the ISO 20022 standard in the high value payments environment has unlocked the ability for a payment to carry more information along with the payment. This is critical to reducing reconciliation effort due to mis-directed payments and the ability to include value added features within the payment. The current limit of 3 lines of reference information for retail payments is highly restrictive.
- b. Payments splitting - We can envisage a future in which a payment made to Inland Revenue contains all the tax related information within it (data rich transactions), thus obviating the need for a separate “information return” to be filed.

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<sup>1</sup> This distinction is important. One may be financially included (possess a bank account) but may struggle to access it as digital technology can create a hurdle to surmount.

An example to explain this concept is in the way tax is withheld by banks on an interest payment. The tax is withheld at the time the interest is paid to the customer. However, the payment of the tax to IR is a separate event at the end of the month and accompanied by an information return. In a future world, the original interest payment could be “split” at source and the tax payment could be made simultaneously along with the related income information to identify and allocate the income to the taxpayer.

- c. Real-time digital payments has its place in a digital world that is driving more real-time interactions. While being able to make payments to citizens in a timely manner can benefit the recipient especially in emergency situations, we are cognisant that any such functionality is not without its costs – potentially the need to have our operations/systems running on weekends to deal with potential customer interactions.

#### 4. **Transparency and traceability of transactions**

- a. Being able to confirm that a social policy payment or tax refund has been made to the intended recipient is important. Today, a payment to a bank account can be confirmed using appropriate bank records such as account statements. Likewise, a customer can prove a payment to Inland Revenue by examining their bank account statement. Will such traceability continue to be available in a future that may be dominated by payments using instruments like a digital currency?
- b. Modernisation of payments systems may result in disintermediation of the banking system. Peer to Peer (P2P) payments via digital wallets may prevail – effectively acting as digital cash. Such mechanisms may have an effect of circumventing controls and the ability to control aspects like money laundering and evasion of tax obligations. Any design must take into account such requirements.
- c. It is important that, while future payment channels afford privacy to the user, it does not provide anonymity of transactions and that rich data be attached to payments to meet the needs of the various parties with an interest in the transaction.
- d. Inland Revenue has broad powers to collect information that is necessary or relevant for administration or enforcement purposes of the tax and social policy system, including collection of information from 3<sup>rd</sup> parties. We exercise these powers where allowed by law and only after significant consideration, but they remain an important instrument in tracking non-compliance and recovering debt. The future payments system for New Zealand should account for such a need in its design.

#### 5. **Fraud/error prevention**

- a. In order for Inland Revenue to refund or make disbursements to citizens, it is necessary to hold accurate target account information. This prevents misdirected payments and can also help to reduce the potential for fraud. An issue that occurs is that individuals or businesses change their bank accounts and fail to update the information we hold. The ability to pay to a **proxy identifier** such as a mobile number or an email address may be an alternative that could overcome such a drawback of the current system. Such a design would also need to incorporate controls to ensure it is secure and cannot be misused.
- b. The ability to ensure that an account number provided to us actually belongs to the identified taxpayer is important. Banks have recently released functionality referred to as Confirmation of Payee and have also developed open banking APIs that aids this process - account validation. Such functionality is welcome and must become common place, easily accessible, and should create the ability to ensure that a payment is made to the correct recipient.

- c. Payment's notifications are an important component of a payment transaction, giving all parties to the transaction, the certainty that a payment has indeed been made. This is also important as a tool in preventing fraudulent transactions, alerting a participant to a potential fraudulent access to their account.

## 6. Whole of system approach

- a. A payments ecosystem is diverse and is a complex one involving multiple players. In New Zealand we believe that the current system is dominated by a small cohort of private sector participants. Any modern payment system must foster innovation and make it easier for the entry of new players that are able to safely deliver innovation to the market. The Fintech sector is very relevant to innovation in the payments system.
- b. Payment's systems should be more closely aligned to business systems and should afford greater choice for the consumer. One of the aspirations for tax administration in New Zealand is to make the tax process as seamless as possible. This would be done by embedding the tax process within the natural business process. A simple way of understanding this is to look at how employers are able to withhold PAYE as part of the regular payroll run. Extending this analogy to other tax processes would enable us to eventually allow a business or an individual to complete a tax transaction from within the natural system of their choice.
- c. The choice of 'natural' system could be as simple as a mobile banking platform for an individual or a point-of-sale platform for a business. In order to remain within the chosen platform, the payment related to a business transaction would need to have a channel or an ability to be made from within such a system. E.g. This may be the ability to make a tax payment from within a mobile banking platform without having to switch to Inland Revenue's portal. Banks could facilitate this by permitting a customer to view a tax liability from a banking platform. At the more complex end of town, e-invoicing is emerging as a way to speed up payments for goods and services and to reduce fraud. Any e-invoicing system will require an associated payments system in order to function successfully. Likewise, we may choose to embed a tax process within such an e-invoicing system. A modernised payment system will take into consideration such an evolution.

## 7. New and emerging technologies to consider

- a. The backbone for digital currencies is a **distributed ledger technology** – commonly referred to as blockchain technology. The importance of blockchain infrastructure and the opportunities it provides cannot be underestimated. It may be possible to use programmable transaction rules and smart contracts in a tax ecosystem to automate processes. Potentially duties and levies could be pre-programmed into a transaction that meet prespecified criteria. This may also allow us to embed a tax process within a natural system e.g. collection of a specific tax type at source when a taxable event occurs or being able to track a taxable event through the blockchain.
- b. Across any payment transaction, identification of the parties involved in the transaction are critical. The ability to uniquely identify the recipient is critical to ensure that payment is made to the right recipient. Emerging technology such as **digital identity** will be relevant to such a problem. This should be placed as a key building block right at the onset of the work on modernising the payment system. Digital identity is also an enabler to ensure that a payment has adhered to any regulation governing the transaction (e.g. age restricted purchases). Digital identity as a technology has many facets to it and we need to ensure that we are not constrained in our thinking, which may be grounded in previous attempts to deploy a federated identity model.
- c. Comparing the New Zealand payments landscape to other jurisdictions reveals that, from a convenience perspective, New Zealand has fallen behind. Our payment options, especially for online transactions, are primarily restricted to card-based options. We note that, in many overseas jurisdictions, the ability to pay from **digital wallets** and the ability

to use **QR codes** to receive a payment are far more prevalent. These offer consumers choices to pay more conveniently and from a device or system of their choice.

- d. **Speed of payments** is relevant in a world where transactions are often conducted in real time. The advent of SBI 365 has gone a long way towards resolving some of these issues. However, this is still not a true real time payment future. Many countries have implemented the ability to make payments in real time.

#### 8. **Inland Revenue's role in the forming of a next gen payment capability**

- a. Inland Revenue will need to connect to the modernised payments ecosystem in a manner that fulfils the requirements and enables opportunities briefly outlined in sections above. The design chosen for an agency of our size (direct participation vs participation through a commercial bank) will be dependent on the design chosen for the modernised payments system. This will in turn determine the amount of change required to our revenue collection, payment disbursements and accounting processes.
- b. We will want to work closely with Payments NZ and the industry to determine the most effective way for Inland Revenue to help shape and participate in the payments ecosystem of the future.
- c. Given the volume of payments we manage and the fact that our processes impact every NZ citizen, we consider ourselves as key to helping drive forward the use of a modernised payments capability.

Yours Sincerely



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