

RESPONSIBILITY BEFORE RUIN: A PRE-EMPTIVE FIX FOR NZ'S PHOENIX PROBLEM

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Research Note

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Executive Summary

New Zealand faces a systemic loss of hundreds of millions of dollars in corporate tax revenue due to weaknesses in its corporate governance framework.

The immediate issue is not that the law absolves directors of liability but that enforcing it is too costly and cumbersome in practice. When companies are struck off the register, Inland Revenue or other creditors must first fund restoration and liquidation before any claim against directors can begin. In “no-asset” cases, this chain of steps is rarely undertaken.

This enforcement friction has real-world consequences. It enables so-called phoenix activity, where failed firms re-emerge debt-free, and it allows “zombie companies” to use unpaid GST and PAYE as interest-free working capital. Compliant businesses are unfairly undercut, while the taxpayer bears the burden through repeated write-offs.

Past attempts at reform have failed because they addressed symptoms rather than the enforcement barrier itself. Inland Revenue’s status as a preferential creditor is often an illusion when no assets remain. Existing director liability rules demand expensive litigation that is rarely viable in practice.

A fundamental shift is required from a reactive to a proactive system of accountability. Directors should not be punished for the failure of their business but for failing to act responsibly once insolvency occurs. A statutory duty to act at the first sign of default would prevent debts from mounting and protect public revenue.

Such a framework would require directors to remedy collected tax defaults or place the company into formal insolvency within a defined timeframe. Those who act would have a safe harbour. Only those who fail to act would face personal liability.

Adopting this model would protect public revenue, ensure market fairness and shift the focus from punishing business failure to enforcing responsibility.

1. Introduction

1.1 *The vanishing tax bill*

Every year in New Zealand, hundreds of millions of dollars in tax revenue – funds intended for public services – effectively vanish. This is not the result of a sophisticated scheme but of a quiet, systemic problem that occurs when a company gets into financial trouble. Owners can often walk away from significant tax debts by allowing their business to be removed from the official Companies Register, leaving the taxpayer to bear the loss.

There are two distinct ways for a company to cease existing. The first is a formal liquidation: a controlled, legally required process where an independent professional investigates the company's failure and ensures any remaining value is paid to creditors in a set order.

The second, and far more problematic, path is an administrative strike-off. This is a passive process where the government removes a company from the register, typically because its directors have stopped filing mandatory paperwork.¹ This route involves no investigation and is often used as a deliberate abandonment strategy.

The core of this practice involves the misuse of taxes collected on behalf of the Crown. When a business charges GST or deducts PAYE from an employee's wages, it acts as a conduit for public revenue. While GST is technically a liability of the supplier rather than a trust fund in the strict legal sense, the economic reality is that these funds represent money collected from the public intended for the Government. However, a company in financial distress will often use these funds as a source of interest-free working capital to stay afloat. This creates so-called "zombie companies" that are technically insolvent but continue to trade, giving them an unfair competitive advantage. They can operate with artificially low overheads, allowing them to undercut honest competitors who are meeting their full tax obligations. This not only harms the Crown but distorts the entire market by penalising fair play.²

This strategy often culminates in illegal "phoenix activity" – where a new business rises from the ashes of the old one, carrying on the same trade but leaving its debts behind. The scale of this issue is significant: in the 2023–24 financial year alone, the Inland Revenue Department (IRD) was forced to write off \$694.5 million in tax debt, much of it lost through this very process.³

1.2 *A history of failed fixes*

This research note will explain why this problem persists. It will show that New Zealand's attempts to fix it have consistently addressed the symptoms rather than the root cause. The government has given the IRD Priority status to collect its money in a collapse, but this is of little use when there are no assets left to claim.⁴ It has also passed specific laws to stop phoenix companies, but these have proven easy for determined operators to sidestep.⁵

The core issue is that New Zealand has focused on trying to solve the problem *after* a company has already failed. This note will look to international examples for a better way forward. It will examine the aggressive system used in Australia, which many consider to be draconian.⁶ Then, it will turn to Germany, which has an effective and balanced solution. By focusing on holding directors accountable *before* a company collapses, the German system smartly prevents the problem from developing in the first place.

This paper will argue that by adopting the principles of the German model, New Zealand can finally address its uncollected tax problem, create a fairer market for honest businesses, and ensure that when a company fails, its tax obligations do not simply disappear.

2. The architecture of avoidance: defining the New Zealand problem

2.1 Quantifying the deficit

The problem of tax evasion through corporate failure is not theoretical; it is a measurable and rapidly growing financial liability for the country. As of June 2024, New Zealand's total overdue tax debt reached an alarming \$7.94 billion. The primary source of this deficit is the corporate sector, which accounted for \$4.8 billion of the total, a figure that had surged from \$3.4 billion just one year prior.⁷

A closer look at this corporate debt reveals that the issue is concentrated in the non-payment of GST and PAYE. These are effectively "pass-through" taxes that businesses collect or withhold on behalf of the Crown. This is a critical indicator of severe financial distress, as it shows that companies are using government funds as unauthorised working capital to stay afloat. The scale of this specific problem is immense, with businesses in the 2025 tax year alone failing to remit over \$1.471 billion of these collected taxes.⁸

This debt is not spread evenly across the economy. It is heavily focused in sectors facing significant economic headwinds, particularly the construction industry. By 2025, construction firms accounted for approximately \$1 billion in outstanding tax obligations. Other heavily impacted sectors include Rental, Hiring and Real Estate Services (around \$500 million) and Accommodation and Food Services (\$325 million), reflecting widespread stress linked to the property market downturn and rising interest rates.⁹

Ultimately, a substantial portion of this debt will never be recovered. While IRD is legally required to write off debt after a formal liquidation confirms there are no assets, this is only part of the story.¹⁰ A more telling figure is the amount IRD already deems impossible to retrieve. One analysis of the overdue tax book showed that a pool of \$1.1 billion was already classified as non-collectable, representing revenue that is effectively lost to the taxpayer, even before the final write-off occurs.

2.2 The two paths of corporate demise

At the heart of New Zealand's uncollected tax problem lies the critical difference between the two ways a company can cease to exist. The path a company takes determines whether its directors are held to account or are allowed to walk away from their obligations, leaving creditors – including the taxpayer – empty-handed.

The first path is formal liquidation. This is the proper and orderly process for winding up a company, especially an insolvent one. A licensed and independent liquidator is appointed to take control of the business, investigate the reasons for its failure, and scrutinise the conduct of its directors.¹¹ The liquidator's job is to sell any remaining assets and distribute the proceeds to creditors according to a strict legal hierarchy.

In this process, the IRD holds a preferential status for unpaid GST and PAYE, meaning its claim is prioritised over those of general unsecured creditors like suppliers.¹² While this does not guarantee payment, the process ensures transparency and a formal investigation into the company's affairs.

The second, far more problematic path is an administrative strike-off. This is a passive process that directors can exploit to achieve a low-cost, low-scrutiny exit. If a company fails to meet basic administrative duties, most commonly the filing of its annual return, the Registrar of Companies can assume it is no longer in business and initiate proceedings to remove it from the register.¹³

Directors of a failing company can trigger this deliberately by simply ceasing all compliance and abandoning the corporate shell. This abandonment strategy completely bypasses the investigative

rigour of a formal liquidation. There is no independent practitioner appointed, no automatic inquiry into the company's failure, and no review of the directors' conduct.¹⁴

A critical enforcement weakness makes this second path so damaging. For directors to *voluntarily* apply to have their company removed under section 318(1)(d) of the Companies Act, they must confirm the company has ceased trading and settled all its liabilities. Crucially, the application must include a written 'no-objection' notice from the Commissioner of Inland Revenue.¹⁵ However, this vital safeguard does not apply when the Registrar initiates the strike-off *involuntarily* due to non-compliance. This allows directors to sidestep any engagement with the IRD.

This weakness is the primary enabler of illegal phoenix activity. A director can transfer all valuable assets from their failing, debt-laden company to a new, clean entity. They then abandon the original company, leaving behind its liabilities, including substantial tax arrears. By waiting for the Registrar to inevitably strike the company off for non-compliance, they dispose of the indebted corporate shell without triggering an investigation that could unwind the asset transfer.

This presents creditors like the IRD with a difficult choice: they can object to the removal, but this merely keeps an assetless company on the register. The alternative is to undertake a costly and time-consuming legal process to have the company restored and then liquidated, a gamble that is often not worth the expense. The phoenix operator relies on this calculated creditor inertia to make their escape.

3. A history of incomplete reform: why New Zealand's measures have failed

3.1 *The illusion of priority*

On paper, New Zealand law gives the Inland Revenue Department a significant advantage in recovering unpaid taxes from a failed company. For unpaid GST and PAYE, the IRD is granted the status of a preferential creditor. This is intended to give the tax authority a head start, allowing it to claim its share of a liquidated company's assets before general trade creditors, such as suppliers, receive anything.

In reality, this legal advantage is often an illusion. While the law grants the Inland Revenue Department (IRD) and employees priority over secured creditors (such as banks) for proceeds from accounts receivable and inventory, this priority is only effective if such assets actually exist at the time of liquidation.¹⁶

This is where the system consistently fails. In a large proportion of liquidations, particularly those involving smaller businesses, the company's assets – including its inventory and receivables – have been depleted long before the liquidator is appointed. Consequently, the IRD's preferential status becomes worthless. It has priority over a pool of money that no longer exists.

The problem extends beyond the Crown's losses. IRD's preferential status actively harms other creditors, particularly trade suppliers who extend credit without knowing that substantial tax arrears will rank ahead of them in any liquidation. A supplier deciding whether to extend credit to a struggling company has no way of knowing that IRD debts stretching back months or years will take priority over their invoices. If that information were visible, many suppliers would refuse to trade on credit. The preferential regime thus creates a hidden liability that catches unsecured creditors unawares, while giving IRD a false sense of security that discourages timely enforcement. The result is that IRD's inaction in pursuing overdue tax shifts losses onto trade creditors who had no means of assessing the risk.

This creates an "enforcement paradox". The IRD is one of the most active initiators of liquidations in the country, often forcing non-compliant companies into a formal insolvency process as a last resort. Yet, this very act of enforcement is frequently the trigger for the final, irreversible write-off of the tax

debt. The formal liquidation process confirms the absence of assets, leaving the IRD legally compelled to extinguish the debt, having recovered nothing.¹⁷

3.2 Flawed deterrents: ineffective personal liability rules

New Zealand law does contain specific provisions designed to hold directors personally responsible for a company's debts, but in practice, these tools have proven to be largely ineffective. They represent another area where the rules seem strict on paper but fail to deliver accountability in the real world, particularly when it comes to unpaid taxes.

The two main legal avenues are general duties under company law and a specific anti-avoidance rule in tax law. The Companies Act 1993 imposes a duty on directors to avoid reckless trading – that is, carrying on the business in a manner likely to create a substantial risk of serious loss to creditors.¹⁸

While allowing a company to trade for an extended period while knowingly accumulating large tax arrears can be a clear breach of this duty, proving it in court presents a high legal hurdle. A liquidator must convince a judge that the director's actions were objectively unreasonable, not just an optimistic but ultimately failed attempt to save the business.¹⁹

A more targeted provision, section HD15 of the Income Tax Act 2007, allows IRD to “pierce the corporate veil” and make directors personally liable for tax debts in cases of asset stripping.²⁰ However, this rule is also limited by a high evidentiary burden, as it requires proof of a specific purpose to defeat the tax liability. This makes it suitable for deliberate, orchestrated schemes but not for the more common scenario of a business simply collapsing under financial pressure.²¹

The most significant reason these rules fail, however, is not their wording but the practical impossibility of enforcing them. Any legal action against a director must typically be initiated and funded by the company's liquidator. In the frequent “no-asset” liquidations, where the company has no funds left, the liquidator has no money to pursue the complex and costly High Court litigation required to hold a director accountable.

The IRD itself does not typically fund these actions, as any money recovered would first be used to pay the liquidator's and lawyers' fees, creating a poor return on investment for the Crown. This creates the central “enforcement paradox”: the very cases where director misconduct is most likely to have occurred – no-asset company failures – are precisely the ones where there are no resources available to investigate or prosecute that misconduct.²²

Some relief may come from forthcoming reforms. The Companies Amendment Bill is expected to give unsecured creditors priority over secured creditors for proceeds recovered through director insolvent trading litigation. This would remove a key disincentive for liquidators to pursue claims where the secured creditor is aligned with the directors. The Supreme Court's decision in *Mainzeal* has already signalled, without strictly ruling on the point, that such recoveries should benefit unsecured creditors. Statutory confirmation would be welcome, but it does not address the underlying problem: these claims still depend on a funded liquidator willing to run complex litigation.

The landmark Supreme Court case of *Debut Homes* perfectly illustrates this gap between theory and reality. In that case, a director knowingly continued to trade his insolvent company, prioritising other creditors while accumulating over \$450,000 in unpaid GST owed to the IRD.²³ The Court found him personally liable, setting a powerful legal precedent.

Yet, the practical impact of this decision has been minimal. The law may be strong on paper, but the systemic reliance on unfunded liquidators to enforce it means that in the vast majority of cases, it remains a deterrent that is never actually deployed.

3.3 *The phoenix law and its limitations*

To combat the most blatant forms of corporate rebirth, New Zealand law includes specific anti-phoenixing provisions. However, these regulations are not a blanket ban; they govern a specific, and legal, restructuring process. A director of a failed company is prohibited from being involved in the management of a new “phoenix company” for five years if that new company uses a same or similar name.²⁴ A director who breaches this rule can be made personally liable for all the debts of the new company.²⁵

When first introduced, these provisions were heralded as the solution to the problem of directors walking away from debts only to start again with a clean slate. However, the entire regime is built on a fatal flaw that makes it a toothless deterrent against the most common form of abuse. The legislation’s power hinges entirely on its narrow definition of a phoenix company based on its name.²⁶

This creates a trivially simple method of circumvention. A director wishing to engage in illegal phoenix activity can fully comply with the letter of the law while flagrantly violating its spirit. They simply need to register their new company under a completely different and unrelated name.

For example, a director of the failed Genius Construction Limited can transfer the business and its assets to a new company named Superior Building Solutions Limited. Because the new name is not similar to the old one, the new entity is not a phoenix company as defined by the Act. Consequently, the five-year ban on the director’s involvement does not apply. They are free to continue the exact same business, often with the same assets, staff, and customers, having successfully shed the tax and other debts of the old company without breaching the specific anti-phoenixing provisions.²⁷

This legislative focus on a superficial element like branding, rather than the substantive economic act of transferring a business to abandon its debts, renders the provisions largely symbolic and explains why phoenix activity continues to be a persistent and unresolved problem.

3.4 *Existing but underutilised powers*

In addition to the flawed phoenix rules, the IRD holds other enforcement tools. It can report debts to credit agencies and issue garnishee notices to divert funds from a company’s bank accounts. While effective in isolation, these are blunt, reactive instruments that often precipitate a company’s immediate collapse rather than encouraging early, responsible governance.

The Department’s specific powers to pursue directors have also proven insufficient.

The Tax Administration Act 1994 contains “Knowledge Offences,” which make it a criminal offence for a person to knowingly apply PAYE deductions for any purpose other than payment to the Commissioner.²⁸ The penalties are severe, including up to five years imprisonment and a \$50,000 fine.²⁹ However, these provisions are very rarely prosecuted and do not serve as a meaningful deterrent in the vast majority of cases.

The IRD can also, as a creditor, pursue directors for breaches of their duties under the Companies Act. A high-profile example is the case of *Commissioner of Inland Revenue v Clooney Restaurant Limited*, where the IRD successfully sued a director for, among other things, breaching his duties by transferring the assets of his old companies to a new one, leaving behind significant tax liabilities.³⁰

While such cases prove that liability can be established, they require the IRD to commit to lengthy and expensive High Court litigation. This is not a viable or efficient solution to a systemic problem involving thousands of companies and hundreds of millions of dollars annually. These powers are reactive, costly, and only deployed in exceptional circumstances, leaving the core problem of widespread, low-level non-compliance unaddressed.

4. A comparative lens: international approaches to director accountability

4.1 The 'draconian' alternative: Australia's Director Penalty Notice (DPN) regime

In stark contrast to New Zealand's reactive and court-dependent system, Australia employs a proactive, aggressive, and highly effective administrative regime to ensure directors are held accountable for unpaid company taxes. This framework, known as the Director Penalty Notice (DPN) regime, allows the Australian Taxation Office (ATO) to bypass the formal liquidation process entirely and make company directors personally liable for certain tax debts.³¹

The system targets the non-payment of taxes that are collected or held on behalf of others: Pay As You Go (PAYG) withholding, the Goods and Services Tax (GST), and the Superannuation Guarantee Charge (SGC).

The power of the DPN regime lies in its sophisticated two-tiered structure, which creates powerful incentives for directors to maintain compliance, even when their company is in financial distress.

The first tier is the "21-Day DPN". This notice is issued when a company has lodged its tax returns on time but has failed to pay the liability. Upon receiving this notice, directors have a 21-day "safe harbour" to avoid personal liability. They can do so by causing the company to pay the debt, appoint a voluntary administrator, or begin the process of putting the company into liquidation. This powerfully incentivises directors to formally address insolvency rather than ignore mounting debts.³²

The second, far more punitive tier is the "Lockdown DPN". The most punitive 'lockdown' penalty – where personal liability is inescapable – applies if directors fail to lodge returns within three months of the due date. In this scenario, the directors become automatically and irrevocably personally liable for the tax debt. The 21-day safe harbour disappears. Placing the company into administration or liquidation provides no escape; the only way for the director to cancel this personal liability is to pay the debt in full.

This framework is more than a simple debt collection tool; it is an instrument of corporate governance. The lockdown provision forces directors to maintain a basic level of compliance – lodging returns – to avoid personal financial ruin.

This prevents "zombie companies" from trading for years while accumulating hidden tax debts. It also gives the ATO the power to pursue a director's personal assets, such as their house or wages, to satisfy the company's debt, regardless of whether the company itself has any funds left.³³ The liability is imposed through an administrative notice from the ATO, not a court order, making it a swift and efficient enforcement mechanism.

It is this power to impose an absolute and inescapable personal liability through an administrative process that leads many to view the Australian system as draconian, but it has proven to be extremely effective.³⁴

4.2 The 'pre-emptive' solution: the German director liability model

The German approach to corporate tax debt offers a fundamentally different and more sophisticated solution. At first glance, the system appears far more lenient than that of New Zealand or Australia. In a German insolvency, the tax authority (*Finanzamt*) has no special priority; it is treated as an ordinary unsecured creditor, standing in line equally with all other suppliers and general creditors.³⁵ This is a deliberate philosophical choice based on the principle of equal treatment for all creditors.

However, this lack of formal priority is counterbalanced by one of the world's most stringent and unforgiving personal liability regimes for a company's managing directors (*Geschäftsführer*). This liability, known as *Geschäftsführerhaftung*, is not a post-insolvency remedy but a pre-emptive tool that forces compliance *before* a company's collapse, effectively serving as the state's primary enforcement mechanism.³⁶

The power of the German system comes from a set of interlocking duties that create a perilous situation for the director of any company in financial distress.

First, a director has a strict, non-delegable, and urgent duty to file for insolvency without delay – typically within a maximum of three weeks – from the moment the company becomes illiquid (unable to pay its debts) or over-indebted.³⁷ Failing to file on time is not just a breach of duty; it is a criminal offence and also triggers personal civil liability for damages.³⁸ This rule alone makes the New Zealand-style abandonment strategy an impossibly risky proposition for a German director.

Second, German law creates what is known as the “tax liability trap”. A director is held personally liable for any corporate taxes (such as VAT and wage tax) that go unpaid due to their intentional or grossly negligent breach of duty. At the same time, once a company is “insolvency ripe”, the director is also personally liable for *any* payments made from the company's accounts.³⁹

German courts have resolved this conflict in a way that heavily favours the tax authority. A director is deemed to have acted with gross negligence if, when funds are insufficient to pay all creditors, they choose to pay other creditors like suppliers but fail to pay the tax office.

To avoid personal financial ruin, the director's only rational and legally safe course of action is to use available funds to pay all creditors, including the *Finanzamt*, on a proportionate basis.⁴⁰ This creates a powerful “backdoor priority”. While the insolvency law preaches equality, the severe personal liability rules coerce directors into prioritising tax payments to protect their own assets.

Crucially, this system is not designed to punish business failure, but to enforce responsible management in a crisis. A director who correctly identifies the moment of insolvency and fulfils their legal duty by filing the paperwork on time is generally protected from this personal liability. The liability is a consequence of the *failure to act responsibly*, not of the insolvency itself.

This pre-emptive model provides two profound advantages over the New Zealand system. First, it prevents the build-up of large, unrecoverable tax debts. Because directors are compelled to confront insolvency the moment it occurs, they cannot continue to trade for months or years while accumulating massive arrears. Second, it ensures market fairness. The system quickly and efficiently removes non-viable “zombie companies” from the market, preventing them from using unpaid taxes as a form of state-sponsored subsidy to unfairly undercut their compliant and solvent competitors.

The practical implications of these different regimes are set out in Appendix 4, which provides worked scenarios showing how common cases unfold in New Zealand, Australia and Germany.

5. A pathway to accountability: a German-inspired model for New Zealand

5.1 *Why the German model is preferable*

An analysis of the New Zealand, Australian, and German systems reveals that the German model offers a demonstrably superior and more balanced pathway for reform. Its strength lies in its pre-emptive focus, which addresses the root cause of the problem, unlike New Zealand's reactive and ultimately ineffective measures.

New Zealand's framework – from its illusory preferential creditor status to its unenforceable director liability rules – only comes into play after a company has already failed. By this point, the tax debt is typically large and unrecoverable.

The German system, in contrast, is proactive. By placing a strict and personal duty on directors to file for insolvency at the first sign of distress, it forces a resolution before a company can trade for months or years while accumulating unpayable tax arrears.⁴¹ It stops the financial bleeding before it becomes fatal for the Crown's revenue.

Compared to the Australian model, the German approach is more nuanced and less draconian. While Australia's Director Penalty Notice regime is undeniably effective, its power to impose automatic and inescapable personal liability through an administrative notice can be seen as a blunt instrument.⁴² The German system is more sophisticated because it provides a clear "safe harbour" for honest directors. Liability is not triggered by the business failure itself, but by the director's personal failure to follow a clear and timely legal process. A director who acts responsibly and files for insolvency as required is protected from personal liability for the company's tax debts.⁴³

This makes the German model preferable on all fronts. It achieves the primary goals of protecting public funds and ensuring market fairness more effectively than New Zealand's framework, while striking a more sophisticated balance between director accountability and fairness than the Australian alternative. It punishes irresponsibility, not just failure.

5.2 *Adapting the principles for New Zealand*

Adopting the German model does not require a direct copy of its legal code. Instead, New Zealand can adapt its core principles to create a framework that is both effective and suited to its own commercial environment. The goal is to shift the focus from post-failure punishment to pre-emptive accountability.

A German-inspired reform package for New Zealand would involve two key changes. First, it would introduce a clear and objective statutory duty for directors to act. The German model relies on a test of "illiquidity" or "over-indebtedness", but legal experience in New Zealand suggests that pinpointing the exact moment of insolvency is often difficult and litigious.⁴⁴ Therefore, this new duty would be triggered automatically by a "bright line" event: when a company fails to remit its collected taxes, such as GST and PAYE, by their due date.

Once this trigger is met, directors would have a strict and defined statutory timeframe to either remedy the tax default or place the company into a formal insolvency process like administration or liquidation.⁴⁵ This timeframe needs to strike a balance. It must be short enough to prevent the accumulation of large, unrecoverable debts, but long enough to be fair to directors.

This is particularly important in New Zealand, where company law does not formally distinguish between the duties of executive and non-executive directors in the way German law does. A timeframe that is too short could deter competent individuals from taking on non-executive director roles.

Therefore, the exact duration should be the subject of legislative consultation, but a period of 30, 60, or 90 days would be appropriate.

Second, this would be paired with a balanced personal liability rule. Directors would become personally liable for the unpaid GST and PAYE, but only if they failed to comply with this new duty to act within the specified timeframe. This creates the crucial “safe harbour” seen in the German system. It means an honest director who confronts the company’s failure and takes the responsible step of initiating a formal insolvency process would be protected from personal liability. The penalty would be reserved for those who choose inaction or who deliberately continue to trade while insolvent, deepening the loss to the Crown.⁴⁶

This proposal does raise a genuine policy question. The Director Liability Notice would give IRD an administrative mechanism to deem directors personally liable – a power no other creditor would possess.

IRD already holds preferential status, superior access to information, and the ability to issue garnishee notices and apply for liquidation. Whether it should also have the power to impose personal liability through an administrative decision, rather than through the courts, is a matter that warrants careful consideration during the legislative process. The judicial review safeguard is intended to address this concern, but the balance between efficient enforcement and procedural fairness will require scrutiny.

A reasonable objection is that New Zealand does not need new legal architecture — it needs the Commissioner to use existing powers more vigorously. Writing in *Stuff* as this paper was being finalised, insolvency practitioner Damien Grant argued that the problem “does not require new laws or fresh capital. Only that the Commissioner’s staff perform the basic level of competence and insist that firms pay what they owe, liquidate promptly those who do not, and hold to account directors who profit from persistent breaches.”⁴⁷ IRD can already prosecute knowledge offences, issue garnishee notices, report to credit agencies and apply for liquidation. If these tools were deployed consistently and promptly, the argument runs, the problem would largely solve itself.

Grant is right that the powers exist. The question is why they go unused. The current system requires IRD to initiate action: to identify non-compliance, pursue the company, fund restoration if necessary, and either litigate or find a liquidator willing to act. Each step costs time and money. The proposed framework reverses this burden. A bright-line trigger creates automatic obligations for directors. The enforcement question shifts from whether IRD will act to whether directors have complied. Administrative notices replace High Court litigation. The system becomes cheaper to operate precisely because it demands less of the regulator at each stage.

This does not eliminate the need for adequate resourcing — issuing and processing Director Liability Notices will require capacity. But it is a different kind of capacity: administrative rather than litigious, routine rather than exceptional. The proposal is not simply another tool for an already-full toolkit. It is a redesign intended to make enforcement viable at scale.

This package would transform New Zealand’s system, creating a powerful incentive for directors to address financial distress early and responsibly.

6. Conclusion

New Zealand’s problem with uncollected corporate tax is not a series of isolated incidents, but the predictable outcome of a systemic flaw. The administrative strike-off process, designed as a simple tool for clearing the companies register, has been co-opted as a low-cost, low-scrutiny exit for directors to

abandon their financial obligations. This has enabled a persistent culture of phoenix activity and left taxpayers bearing the cost of hundreds of millions of dollars in lost revenue each year.⁴⁸

As this note has demonstrated, New Zealand's history of reform has been a story of incomplete and ineffective measures. The legal tools that have been deployed – from granting the IRD preferential creditor status to enacting specific rules against phoenix activity and director misconduct – have consistently proven to be reactive. They are designed to manage the consequences of failure, but they come into play too late in the process, long after a company's assets have been exhausted and the real opportunity for recovery has passed.⁴⁹

The path to meaningful reform lies in shifting from a reactive to a proactive framework. The principles of the German model provide a compelling blueprint for a solution adapted to New Zealand's unique context. By placing the onus of responsibility squarely on directors to act at the first sign of insolvency, it pre-empts the accumulation of unpayable debt. Its genius lies in its balance: it is not a punishment for entrepreneurial failure, but a penalty for the failure to manage that failure responsibly. It provides a clear "safe harbour" for honest directors who follow the rules, while holding those who do not to account.⁵⁰

By adapting these principles, New Zealand can move beyond a framework that tolerates evasion to one that demands accountability. A reform that establishes a clear, statutory timeframe – be it 30, 60 or 90 days – for directors to act on tax defaults, combined with a safe harbour for those who comply, would achieve this. A German-inspired model would not only protect the Crown's revenue but would also foster a fairer and more robust commercial environment by ensuring that non-compliant "zombie companies" cannot gain an unfair advantage over their honest competitors.⁵¹

It is acknowledged that these reforms would have wider implications. The administrative resources required by Inland Revenue to manage a system of Director Liability Notices would need to be carefully scoped and funded – though this is expected to be offset by increased revenue recovery.

Finally, while this proposal focuses on accountability, it should ideally be accompanied by a simplified, lower-cost business rehabilitation regime for SMEs, ensuring that viable businesses have a pathway to recovery that is currently lacking in our insolvency settings. These proposals should also be considered alongside the Law Commission's current work on director liability, which is examining the policy basis for personal liability across a range of contexts. Engagement with that process would help ensure coherence across New Zealand's corporate governance framework.

Ultimately, however, this proposal is more than a technical fix; it represents a fundamental shift in philosophy. It moves New Zealand from a reactive framework that chases debts to a proactive one that demands accountability, strengthening both the integrity of the tax system and the principle of fair play in the market.

Appendix 1: Principles for Legislative Design

1. The Trigger Mechanism

The new duty should not rely on a complex assessment of “insolvency” or “illiquidity”, which can be subjective and difficult to determine in real-time. Instead, it should be triggered by a “bright line” event: the default on specific tax obligations (GST and PAYE) collected on behalf of the Crown.

2. The Duty to Act

Upon triggering the default, directors must be subject to a strict, non-delegable statutory duty to take one of two actions within a defined period (proposed as 30, 60, or 90 days):

- Remedy the default by paying the outstanding tax; or
- Place the company into a formal insolvency process (Voluntary Administration or Liquidation).

3. The Safe Harbour

To encourage responsible behaviour rather than immediate resignation, directors who comply with the duty to act within the statutory timeframe must be granted a “safe harbour” from personal liability for the tax debt.

4. The Penalty for Inaction

Personal liability for the unpaid GST and PAYE should attach only to those directors who fail to take either of the required actions within the timeframe. This liability ensures that directors cannot simply abandon a company (the “strike-off” strategy) to escape debts owed to the Crown.

Appendix 2: Draft Regulatory Impact Statement (RIS)

Director Accountability for Collected Taxes Bill

1. Problem Definition

The issue

- Each year, hundreds of millions of dollars in GST and PAYE collected on behalf of the Crown are not remitted.
- In 2023–24, Inland Revenue (IRD) wrote off \$694.5 million in uncollected tax debt. A significant portion was lost through strike-off companies abandoned by directors without entering liquidation.
- As of June 2024, overdue tax debt stood at \$7.94 billion, of which \$4.8 billion was owed by companies, primarily in GST and PAYE arrears.
- These are effectively “collected taxes” (or pass-through taxes) – funds deducted from employees or charged to consumers – that should never form part of working capital.
- The current system allows directors to avoid liability by walking away from insolvent companies, enabling phoenix activity and creating “zombie companies” that unfairly undercut compliant competitors.

Why existing measures are inadequate

- IRD preferential creditor status is illusory: in many liquidations there are no assets to distribute.
- Director liability under reckless trading or tax avoidance provisions requires costly litigation that is rarely viable in “no-asset” cases.
- Anti-phoenix company provisions are easily circumvented by changing company names.

2. Objectives

- Protect public revenue by ensuring GST and PAYE are remitted.
- Prevent directors from misusing taxes as working capital.
- Create a fairer business environment by removing the advantage of zombie companies.
- Balance accountability with safe harbour protections for responsible directors.

3. Options Considered

Option 1: Status quo

- No change to existing law.
- IRD continues to bear large write-offs.
- Market distortions persist.
- Not consistent with international best practice.

Option 2: Australian model (Director Penalty Notice regime)

- Automatic, inescapable personal liability for directors through administrative notice.
- Effective deterrent but widely viewed as draconian.
- May discourage risk-taking and entrepreneurship.

Option 3: German-inspired model (preferred)

- Proactive director duty to act within a fixed statutory timeframe (e.g., 30, 60, or 90 days) of tax default.
- Safe harbour if directors remedy default or initiate insolvency.
- Personal liability for directors who fail to act.
- Balanced approach that punishes irresponsibility, not failure.

4. Preferred Option

The Government proposes adopting a German-inspired model via the *Director Accountability for Collected Taxes Bill*. This option:

- Is proactive rather than reactive.
- Aligns with international best practice while preserving fairness.
- Provides clarity and deterrence through a standalone statute.
- Establishes IRD enforcement via Director Liability Notices with judicial review safeguards.

5. Implementation

- Standalone Act, commencing within 6 months of Royal assent.
- Transitional period of 6 months to allow companies to update compliance systems.
- IRD responsible for issuing Director Liability Notices.
- Education campaign for directors and professional advisers to raise awareness.

6. Impacts

Fiscal

- Significant reduction in annual tax write-offs.
- More consistent revenue for Crown accounts.
- Administrative costs for IRD to issue notices, offset by savings in enforcement.

Business

- Honest businesses benefit from fairer competition.
- Non-viable companies forced to exit earlier.
- Some increased compliance pressure on directors, particularly in SMEs.

Legal

- Clearer statutory duty replaces vague reckless trading standard for tax defaults.
- Stronger enforcement tools reduce reliance on costly litigation.

7. Consultation

- Inland Revenue and MBIE consulted on legislative design.
- Feedback from insolvency practitioners and business groups highlighted support for clarity, but concern about overreach.
- To address fairness concerns, the Bill includes a robust safe harbour and proposes a flexible timeframe (30, 60, or 90 days) to be determined after consultation, providing a reasonable period for directors to act.

8. Risks and Mitigation

Risk	Mitigation
Directors may resign quickly at first sign of default, leaving companies leaderless	Safe harbour applies only if directors take responsible steps, not abandonment
IRD overuse of Director Liability Notices	Judicial review safeguard
SMEs lack awareness of new duties	Education campaign by Companies Office and IRD

9. Monitoring and Evaluation

- IRD to report annually on:
 - Number of Director Liability Notices issued
 - Amount of tax debt recovered
 - Estimated reduction in write-offs compared with baseline
- Review after 3 years to assess effectiveness and compliance costs.

10. Conclusion

The German-inspired model, implemented through the *Director Accountability for Collected Taxes Act*, offers a balanced, effective and fair reform. It protects Crown revenue, strengthens market integrity, and ensures that responsibility is borne by those who fail to act, not by taxpayers.

Appendix 3: Draft Cabinet Paper

Purpose

This paper seeks Cabinet agreement to introduce the *Director Accountability for Collected Taxes Bill*. The Bill creates a new statutory duty for directors to act promptly when GST or PAYE defaults occur. It provides a safe harbour for responsible directors and imposes personal liability only on those who fail to act.

Problem

Each year, Inland Revenue writes off hundreds of millions of dollars in uncollected GST and PAYE. These are monies collected from consumers and employees on behalf of the Crown. In 2023–24 alone, \$694.5 million was written off, much of it from companies abandoned without liquidation. As of June 2024, overdue tax debt stood at \$7.94 billion, of which \$4.8 billion was owed by companies, largely in GST and PAYE.

The immediate issue is not that directors are legally immune. Duties already exist under the Companies Act, and companies can be restored for scrutiny. The real weakness lies in the cost and delay of activating enforcement. To pursue a claim, creditors must fund restoration, liquidation, and often litigation. In no-asset failures—the very cases most likely to involve misconduct—these steps are rarely taken.

This enforcement friction has significant consequences. It allows directors to walk away from failing companies, leaving unpaid GST and PAYE behind. Some firms re-emerge in new guises (“phoenixing”), while others trade on as “zombies”, using taxes as interest-free working capital. Both distort competition, undercut compliant businesses, and shift losses onto taxpayers.

Existing remedies, including reckless trading provisions and anti-phoenix rules, have proven ineffective because they are too slow, too expensive, and too rarely invoked. Without reform, the problem will persist.

Objectives

The reform aims to:

- protect Crown revenue by reducing uncollectable GST and PAYE debt
- prevent phoenix activity and discourage “zombie” trading funded by unpaid collected taxes
- ensure fair competition so compliant businesses are not undercut
- balance accountability with fairness by providing a clear safe harbour for directors who act responsibly.

Options Considered

Status quo

Under current arrangements, Inland Revenue continues to bear large write-offs. Directors can abandon companies that owe GST and PAYE, leaving creditors to fund costly restorations and liquidations. Remedies exist in theory but are rarely pursued in no-asset cases. Zombie companies persist, and phoenix activity remains attractive.

Australian model – Director Penalty Notice regime

This regime imposes automatic and inescapable personal liability on directors through administrative notice. It has proven effective in securing tax compliance. However, it is widely criticised as draconian, with the potential to discourage entrepreneurship and risk-taking.

German-inspired model (preferred)

This option imposes a proactive duty on directors to act within a fixed statutory timeframe (e.g., 30, 60, or 90 days) once collected taxes defaults occur. Directors must either remedy the default or commence formal insolvency. A safe harbour protects those who act responsibly. Personal liability attaches only where directors fail to act. This balances deterrence with fairness and addresses the enforcement friction at the core of New Zealand's current problem.

Proposal

Cabinet is invited to agree to the introduction of the *Director Accountability for Collected Taxes Bill*. The Bill would:

- establish a statutory duty for directors to remedy GST or PAYE defaults or place the company into formal insolvency within a fixed statutory timeframe (e.g., 30, 60, or 90 days)
- provide a safe harbour for directors who take these responsible steps, ensuring that liability does not punish ordinary business failure
- impose joint and several personal liability on directors who fail to act, making accountability automatic and reducing reliance on costly restorations and litigation
- empower Inland Revenue to issue enforceable Director Liability Notices, with the safeguard of judicial review
- create a proportionate criminal offence for wilful non-compliance, punishable by fines or director disqualification.

This approach moves New Zealand from a reactive enforcement model to a proactive accountability framework. It reduces the high transaction costs that currently prevent effective scrutiny of directors, protects public revenue, and levels the playing field for compliant businesses.

Implementation

The Bill will be enacted as a standalone statute, the *Director Accountability for Collected Taxes Bill*.

- The Act will commence within 6 months of Royal assent.
- Transitional provisions will allow companies a further 6 months to update compliance systems.
- Inland Revenue will administer the regime and issue Director Liability Notices, subject to judicial review.
- The Companies Office and Inland Revenue will run an awareness campaign to ensure directors understand their duties and the scope of the safe harbour.
- Professional advisers, insolvency practitioners, and business groups will be engaged to promote compliance and highlight the benefits of early action.

Impacts

Fiscal

- A material reduction in annual write-offs of GST and PAYE debt.
- More predictable Crown revenue, as enforcement no longer depends on costly restorations or liquidations.

Business

- A level playing field for compliant firms, as phoenix operators and zombie companies lose the ability to trade on using unpaid collected taxes.
- Some additional compliance pressure on directors, particularly in SMEs, mitigated by the safe harbour for those who act responsibly.
- Greater certainty and clarity for directors compared with the vague and litigation-heavy reckless trading standard.

Legal

- A clear statutory duty replaces reliance on case-law-driven remedies.
- Automatic liability for directors who fail to act reduces reliance on liquidators or creditors funding court proceedings.
- The judicial review safeguard ensures proportionate use of Inland Revenue's new powers.

Risks and Mitigation

Risk	Mitigation
Directors resign rather than act	The safe harbour applies only where directors take responsible steps to remedy defaults or commence insolvency. Abandoning a company does not provide protection.
IRD overuse of enforcement powers	All Director Liability Notices are subject to judicial review. This safeguard ensures proportionate use of the regime and provides directors with legal recourse.
Lack of awareness among SMEs	Inland Revenue and the Companies Office will run a targeted education campaign, supported by professional advisers. The focus will be on clarity, practical guidance, and reassurance about the scope of the safe harbour.
Reform may be perceived as discouraging entrepreneurship	The duty targets irresponsibility, not business failure. Directors who act responsibly remain protected. This balances deterrence with fairness and avoids penalising ordinary risk-taking.

Consultation

Inland Revenue, MBIE, the Treasury and the Companies Office were consulted. Insolvency practitioners and business representatives were engaged; they supported stronger accountability but emphasised the need for safe harbour.

Recommendations

It is recommended that Cabinet:

1. **note** that uncollected GST and PAYE debt is a systemic problem costing the Crown hundreds of millions of dollars annually;
2. **agree** to the introduction of the *Director Accountability for Collected Taxes Bill* to establish a statutory duty on **directors** to act promptly when defaults occur;
3. **agree** that directors who comply will have a safe harbour from liability, and those who fail to act will be personally liable;
4. **agree** to empower IRD to issue enforceable Director Liability Notices, subject to judicial review;
5. **agree** that the Bill will commence within 6 months of Royal assent, with a 6-month transitional period for compliance; and
6. **invite** the Minister of Revenue to issue drafting instructions to the Parliamentary Counsel Office and to introduce the Bill to the House.

Appendix 4: Three scenarios – Comparing New Zealand, Australia and Germany

To show how different legal frameworks handle the same underlying behaviour, this appendix sets out three common scenarios. Each example describes how the case would typically play out in New Zealand, then contrasts it with the Australian and German systems.

Scenario 1: Zombie trading on GST and PAYE

A small construction company files its GST and PAYE returns but does not pay the tax due. Instead, it uses the cash to pay suppliers and keep jobs going.

In New Zealand, Inland Revenue is a preferential creditor, but only in theory. If the company collapses, a liquidator must be appointed to investigate and bring claims. When no assets are left to fund this work, nothing happens. If the company is struck off for non-compliance, Inland Revenue would first need to restore it to the register and then apply for liquidation. In practice, the tax debt is usually written off.

In Australia, the Australian Taxation Office issues a Director Penalty Notice within 21 days. The directors must either pay the debt, place the company into voluntary administration or begin liquidation. If they do not act, personal liability attaches automatically. The procedure is administrative, quick and does not require court action.

In Germany, once the company becomes insolvent or over-indebted, directors have a strict duty to file for insolvency within a maximum of about three weeks. Continuing to pay suppliers while not remitting wage tax or VAT after that point exposes directors to personal and even criminal liability. This ensures that the company is forced into formal insolvency quickly and prevents long periods of tax-funded “zombie” trading.

Scenario 2: Non-lodger as phoenix incubator

The same company stops lodging GST and PAYE returns altogether as cash tightens. It continues to trade and begins shifting assets to a new entity.

In New Zealand, non-lodgment can lead to the company being struck off by the Registrar. Inland Revenue can object or later restore the company to the register, but both steps are costly. Director liability claims still depend on a funded liquidator. The absence of enforcement means directors can drift for months or years before any scrutiny occurs.

In Australia, non-lodgment is far riskier. If returns are not lodged within three months, directors face a “lockdown” penalty notice. Personal liability becomes automatic and cannot be avoided even by placing the company into administration or liquidation. The only escape is to pay the tax in full. This removes the incentive to go dark and wait for strike-off.

In Germany, directors who fail to keep proper books or delay filing for insolvency risk both civil and criminal sanctions. If assets have been moved out of the failing company, an insolvency administrator can claw them back through avoidance law. Tax law also allows personal liability if non-payment results from gross negligence or wilful breach. Non-lodgment is therefore not a safe path.

Scenario 3: Asset-strip and restart

The directors of OldCo transfer plant, customer lists and staff to NewCo for inadequate value, leaving OldCo burdened with tax arrears. OldCo is then abandoned.

In New Zealand, Inland Revenue can attempt to use section HD15 of the Income Tax Act to hold directors or related parties liable. However, this requires proof of an intention to defeat tax liabilities and usually depends on a liquidator pursuing the claim after the company is restored. In no-asset cases, these actions are seldom taken.

In Australia, unpaid PAYG, GST and superannuation still trigger director penalty notices regardless of how the phoenixing is structured. The ATO also has a range of dedicated anti-phoenix powers, from director identification numbers to security deposits and recovery of creditor-defeating dispositions. These tools make asset transfers harder to execute and easier to unwind.

In Germany, directors who fail to file for insolvency on time are personally exposed for payments made after insolvency ripeness, including asset transfers. Transactions at undervalue can be clawed back by the insolvency administrator under avoidance law. Tax-representative liability also applies if unpaid wage tax or VAT can be traced to wilful or negligent conduct. Phoenixing is therefore much more likely to rebound on the directors personally.

Summary

These scenarios show why New Zealand's enforcement gap matters. Directors are legally accountable in theory, but in practice the costs of restoration, liquidation and litigation mean that few cases are ever pursued.

Australia overcomes this by attaching liability quickly and administratively.

Germany does so by imposing a strict duty to act early and by exposing directors personally if they delay or make selective payments. Both systems achieve what New Zealand's reactive framework does not – swift and certain accountability.

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- ⁴⁶ Beissenhirtz, “Managing director personally liable for company’s tax obligations,” accessed October 2, 2025, <https://www.beissenhirtz.com/en/managing-director-personally-liable-for-companys-tax-obligations/>.
- ⁴⁷ Damien Grant, “The Ponsonby icon that dined out on unpaid tax,” *Stuff*, 23 November 2025, <https://www.stuff.co.nz/nz-news/360892892/damien-grant-ponsonby-icon-dined-out-unpaid-tax>.
- ⁴⁸ McDonald Vague, “The Risks of Company Strike Off,” accessed October 2, 2025, <https://www.mvp.co.nz/articles/risk-management/the-risks-of-company-strike-off>.
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- ⁵¹ RNZ, “Businesses’ unpaid tax bill - ‘there’s potential for a lot of collateral damage,’” May 29, 2024, <https://www.rnz.co.nz/news/business/569106/businesses-unpaid-tax-bill-there-s-potential-for-a-lot-of-collateral-damage>.

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