



**International treaty examination
of the Agreement between the
Government of New Zealand
and the Government of the
British Virgin Islands for the
Exchange of Information
Relating to Taxes and of the
Agreement between the
Government of New Zealand
and the Government of the
British Virgin Islands for the
Allocation of Taxing Rights with
Respect to Certain Income of
Individuals**

Report of the Finance and Expenditure
Committee

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International treaty examination of the Agreement between the Government of New Zealand and the Government of the British Virgin Islands for the Exchange of Information Relating to Taxes and of the Agreement between the Government of New Zealand and the Government of the British Virgin Islands for the Allocation of Taxing Rights with Respect to Certain Income of Individuals

Recommendation

The Finance and Expenditure Committee recommends that the House take note of its report.

The Finance and Expenditure Committee has conducted an international treaty examination of the Agreement between the Government of New Zealand and the Government of the British Virgin Islands for the Exchange of Information Relating to Taxes and of the Agreement between the Government of New Zealand and the Government of the British Virgin Islands for the Allocation of Taxing Rights with Respect to Certain Income of Individuals, and has no matters to bring to the attention of the House.

The national interest analysis for the treaties is appended to this report.

Appendix A

Committee procedure

The committee met on 21 and 28 April 2010 to consider the agreements.

Committee members

Craig Foss (Chairperson)

Amy Adams

David Bennett

John Boscawen

Brendon Burns

Hon David Cunliffe

Aaron Gilmore

Raymond Huo

Rahui Katene

Peseta Sam Lotu-Iiga

Stuart Nash

Dr Russel Norman

Appendix B

Agreement between the Government of New Zealand and the Government of the British Virgin Islands for the Exchange of Information Relating to Taxes

Agreement between the Government of New Zealand and the Government of the British Virgin Islands for the Allocation of Taxing Rights with Respect to Certain Income of Individuals

National Interest Analysis

Executive Summary

1 The Agreement Between The Government Of New Zealand And The Government Of The British Virgin Islands For The Exchange Of Information Relating To Taxes (“the TIEA”) was signed with the British Virgin Islands (“BVI”) in Washington on 13 August 2009. The TIEA will enable tax officials from New Zealand and BVI (“the Parties”) to request information from each other (such as tax records, business books and accounts, bank information, and ownership information) for the purpose of detecting and preventing tax avoidance and evasion. Access to this previously unobtainable information will enhance Inland Revenue’s ability to detect and prevent tax avoidance and tax evasion. Any reduction in tax avoidance or tax evasion will be beneficial to New Zealand in financial, fiscal and economic terms.

2 The Agreement Between The Government Of New Zealand And The Government Of The British Virgin Islands For The Allocation Of Taxing Rights With Respect To Certain Income Of Individuals (“the Supplementary Agreement”) has been signed with BVI at the same time as the TIEA. Although the TIEA applies on a reciprocal basis, the nature of BVI’s tax system means that it will derive less benefit from the TIEA than will New Zealand. The Supplementary Agreement was therefore offered by New Zealand to ensure that BVI receives some reciprocal benefit from entering into exchange of information arrangements with New Zealand. The TIEA and the Supplementary Agreement should be considered as elements of a “package deal”. New Zealand will not gain any direct benefit from the entry into force of the Supplementary Agreement. However, the Supplementary Agreement is needed to support, and will indirectly benefit New Zealand through its support for the conclusion of the TIEA. In any case, there will be few, if any, negative financial, fiscal and economic implications for New Zealand from the entry into force of the Supplementary Agreement.

3 The TIEA is based on a model produced in 2002 by the Organisation for Economic Cooperation and Development (“the OECD”). The TIEA provides a comprehensive set of rules to support the exchange of information. In particular, it requires the Parties to maintain strict confidentiality in relation to any information received pursuant to a request. Such information may only be disclosed to authorised persons and may only be used for

specified purposes (principally the administration and enforcement of the domestic tax laws of the respective Party). A copy of the TIEA is attached as Annex A.

4 The Supplementary Agreement contains a selected number of articles based on those that typically appear in New Zealand’s double tax agreements (“DTAs”). The articles allocate taxing rights in a limited number of circumstances (in respect of government service and students). A copy of the Supplementary Agreements is attached as Annex B.

5 Both the TIEA and Supplementary Agreement are further supplemented by a less-than-treaty status Memorandum of Understanding Between The New Zealand Revenue Department And The Ministry Of Finance Of The British Virgin Islands Concerning The Interpretation Or Application Of The Agreement Between The Government Of New Zealand And Government Of The British Virgin Islands For The Exchange Of Information Relating The Taxes (“the Understanding”). The Understanding sets out the shared understandings on matters relating to the interpretation and operation of the TIEA and Supplementary Agreement.

Date and nature of proposed binding treaty action

6 Before the TIEA and the Supplementary Agreement are brought into force for New Zealand they first must be submitted to the House for Parliamentary treaty examination, in accordance with Standing Orders 388 to 391. Following completion of the Parliamentary treaty examination process it is proposed that the two agreements be incorporated into domestic legislation by Orders in Council. The Understanding has a less-than-treaty status and is not required to be submitted for parliamentary treaty examination.

7 The two agreements can then be brought into force, in accordance with Article 14 of the TIEA and Article 8 of the Supplementary Agreement, through an exchange of diplomatic notes that confirm that the Parties have completed their constitutional and legal procedures for entry into force.

8 Each agreement will enter into force on the date of the later of the two diplomatic notes. New Zealand officials will manage the procedures to ensure that both agreements enter into force on the same date.

Reasons for New Zealand taking the treaty action

The TIEA

9 New Zealand domestic law specifically prohibits Inland Revenue from divulging information it holds to foreign jurisdictions, except when authorised by a tax treaty.¹ Other countries generally follow the same principle. Therefore, to assist in the detection and prevention of tax avoidance and tax evasion, most developed countries are building networks of treaties that allow for the exchange of information on tax matters.

10 The most common type of tax treaty in which exchange of information provisions feature are double tax agreements (“DTAs”). New Zealand currently has 35 DTAs in force. However, DTAs are typically only concluded between trading and investment

¹ Sections 81 and 88 of Tax Administration Act 1994 refer.

partners with broadly similar tax systems. To cater for other situations, the OECD, in 2002, produced a model TIEA that provides solely for the exchange of information on tax matters.

11 The OECD model TIEA provides a comprehensive set of rules to support the exchange of information. These rules are designed to ensure that requested information is provided in a timely and effective manner. Interference from bank secrecy and domestic tax interest rules are specifically prohibited as an obstacle to effective information exchange. Otherwise, rights and safeguards secured to residents of either jurisdiction by domestic law or administrative practice remain in effect. The Parties are required to maintain strict confidentiality in relation to any information received pursuant to a request. Such information may only be disclosed to authorised persons and may only be used for specified purposes (principally the administration and enforcement of the domestic tax laws of the respective Party).

12 New Zealand is currently negotiating a number of TIEAs based on the OECD model TIEA. The first New Zealand TIEA to arise from those negotiations was with the Netherlands Antilles, signed on 1 March 2007. Negotiations for a TIEA with BVI have now also concluded. Each new TIEA represents a further step forward for New Zealand in terms of extending its network of exchange of information arrangements.

The Supplementary Agreement

13 Although the TIEA applies on a reciprocal basis, BVI only has a limited tax system (consisting primarily of payroll taxes). BVI therefore has little need to seek information on tax matters from other countries. New Zealand, by contrast, imposes income tax on the worldwide income of its tax residents, and so has a keen interest in ensuring that it can obtain information on the income earning activities of those tax residents in foreign jurisdictions. Accordingly, New Zealand has a much greater interest in concluding a TIEA than BVI, and can expect to derive greater benefits from the TIEA than will BVI.

14 To encourage BVI to conclude the TIEA, and following the approach adopted by other OECD member countries in TIEA negotiations, New Zealand offered to enter into an additional agreement with BVI that would allocate taxing rights in a limited number of circumstances.

15 Prior to the advent of TIEAs New Zealand had previously only entered into arrangements for the allocation of taxing rights in its DTAs. As noted above, however, DTAs are typically concluded between trading and investment partners with broadly similar tax systems, where the concession of taxing rights is reciprocal. That is, New Zealand may give up a taxing right but the other country will also give up a taxing right in reciprocal circumstances. In financial terms, these reciprocal reductions often tend to offset each other (for example, reduced tax in the other jurisdiction can result in a reduced foreign tax credit against the New Zealand tax liability). However, given BVI's limited tax system, entering into a DTA with BVI would mean New Zealand giving up taxing rights with little, if any, reciprocity.

16 For this reason, the Supplementary Agreement has been limited to a selected number of DTA articles chosen because they will result in minimal fiscal cost to New Zealand and will not provide a commercial advantage to individuals or entities operating in BVI:

- Pursuant to Article 5 of the Supplementary Agreement, remuneration paid by the Government of one jurisdiction to an individual in respect of services rendered to that Government will be exempt from income tax in the other jurisdiction. However, this rule does not apply if the individual is a tax resident of that other jurisdiction (unless the individual became resident solely by reason of the rendering of those services). The Article will therefore only apply when a BVI Government official comes to New Zealand in an official capacity. Such visits are likely to be minimal. In any case, New Zealand generally does not tax salaries and wages earned in New Zealand where the visit is for less than 90 days.
- Pursuant to Article 6 of the Supplementary Agreement, where a student or business apprentice who is a tax resident of one jurisdiction is temporarily present in the other jurisdiction solely for the purpose of their education or training, payments which they receive from outside that other jurisdiction for their maintenance, education or training will be exempt from income tax in that other jurisdiction. As New Zealand generally does not tax payments of this type, the Article will have few implications.

17 Article 7 of the Supplementary Agreement provides that information may be exchanged for the purposes of carrying out the provisions of the Supplementary Agreement using the mechanism established by the TIEA. This is an important clarification to ensure that where the respective tax authorities need to communicate with each other for any purpose of the Supplementary Agreement, they can do so without violating their domestic secrecy laws that otherwise protects tax matters.

18 Given that the Supplementary Agreement has been negotiated primarily for the purposes of securing and supporting the TIEA, Article 9 of the Supplementary Agreement explicitly provides that the provisions of the Supplementary Agreement will only have effect once the TIEA has entered into force (in practice, New Zealand officials will ensure that both the TIEA and Supplementary Agreement enter into force on the same date).

The Understanding

19 The TIEA and Supplementary Agreement are supplemented by a less-than-treaty status instrument that clarifies a number of areas of joint understanding between the authorities in each country that will be administering the Agreements (that is, between the New Zealand Inland Revenue and BVI's Ministry of Finance). The clarifications generally concern administrative issues pertaining to the interpretation and operation of the Agreements.

Consideration of other options

20 New Zealand's objective in negotiations was to secure effective exchange of information arrangements with BVI. The only other possible treaty mechanism for entering into such arrangements with BVI would be as part of a DTA. However, DTAs are designed to be concluded between trading and investment partners with broadly similar tax systems. As noted above, the fact that DTAs allocate taxing rights means that New Zealand would stand to lose revenue if it were to enter into a DTA with BVI.

21 The entering into of the Supplementary Agreement is the "trade off" for BVI agreeing to enter into exchange of information arrangements with New Zealand. The

TIEA and the Supplementary Agreement constitute a package deal. Neither agreement can be entered into without the other.

Advantages and disadvantages to New Zealand of the treaty action

22 The TIEA will enable New Zealand tax officials to request tax records, business books and accounts, bank information, and ownership information from BVI. Access to this previously unobtainable information will enhance Inland Revenue’s ability to detect and prevent tax avoidance and tax evasion. Any reduction in tax avoidance or tax evasion will be beneficial to New Zealand in financial, fiscal and economic terms.

23 BVI is unlikely to raise many (if any) requests for information from New Zealand. However, if requests for information are received from BVI, New Zealand will incur administrative costs in obtaining and providing the requested information. However, streamlined and effective mechanisms for dealing with exchange of information requests have already been established in relation to New Zealand’s existing 37 DTAs and TIEAs. The administrative costs of responding to requests from BVI will only be marginal. Experience gained from the exchange of information arrangements already in place under New Zealand’s existing tax treaties indicates that the benefits arising from the enhanced ability to reduce tax avoidance and evasion outweigh any of the costs that arise.

24 New Zealand may be required to bear some costs in relation to requests for information that it makes to BVI. The Understanding referred to in paragraph 19 above sets out the shared understanding of the Parties with respect to costs, as is required by Article 10 of the TIEA. “Ordinary” costs of complying with a request will be borne by the requested Party, but “extraordinary costs” (such as the cost of hiring translators or interpreters) will be reimbursed by the requesting Party. However, prior consultation will be required if extraordinary costs appear likely to exceed US\$500. This will ensure that New Zealand will only progress information requests giving rise to significant reimbursement costs if the need to obtain the information justifies the expenditure.

25 The TIEA is largely based on the 2002 OECD model TIEA. A key difference from the OECD model, however, is that the TIEA includes, at Article 11, an obligation on each jurisdiction not to impose “prejudicial or restrictive measures based on harmful tax practices”. This obligation relates to the OECD Harmful Tax Practices initiative, in which the prospect of OECD member countries taking defensive measures to restrain the harmful tax practices of other countries has previously been raised.² New Zealand does not currently impose any such measures and, given that the TIEA provides for full exchange of information on tax matters with BVI, would not contemplate introducing such measures with respect to BVI while the TIEA is in force. The provision was included in recognition of this, but was expressed as a reciprocal obligation on both Parties.

26 The Supplementary Agreement was negotiated primarily for the purpose of securing a TIEA with BVI. New Zealand is not expected to derive any direct benefit from the Supplementary Agreement. The Supplementary Agreement will, however, indirectly benefit New Zealand by means of the TIEA. As noted above, the revenue implications for

² The 1998 OECD report “Harmful Tax Competition: An Emerging Global Issue” and 2000 OECD report “Towards Global Tax Co-operation: Progress in Identifying and Eliminating Harmful Tax Practices” refer.

New Zealand of the Supplementary Agreement entering into force are expected to be minimal, and will be outweighed by the benefits New Zealand stands to gain from BVI concluding the TIEA.

27 On balance, it is in New Zealand's interests to conclude the TIEA and the Supplementary Agreement with BVI.

28 If BVI ever unilaterally terminates the TIEA, the Supplementary Agreement would also terminate and New Zealand would likely terminate the Understanding. Similarly, if New Zealand ever unilaterally terminates the Supplementary Agreement, BVI could be expected to terminate the TIEA.

Obligations which will be imposed on New Zealand by the treaty action, the position of reservations to the treaty, and an outline of any dispute settlement mechanisms

The TIEA

29 The TIEA places a reciprocal obligation on each Party to provide, upon request, information that is relevant to the administration and enforcement of specified taxes. In the case of BVI, the specified taxes are "such taxes as may from time to time, be imposed by law". As noted above, BVI currently has a very limited tax system, primarily consisting of payroll taxes, and so is unlikely to make many requests for information from New Zealand.

30 The Parties are required to maintain strict confidentiality in relation to any information received pursuant to a request. Such information may only be disclosed to authorised persons and may only be used for specified purposes (principally the administration and enforcement of the domestic tax laws of the respective Party).

31 In the Understanding, the respective tax authorities set out their shared understanding of how incidents of costs incurred in providing assistance will be addressed: the requesting Party is to reimburse the requested Party for "extraordinary costs" (such as the cost of engaging an interpreter or translator) incurred in responding to the request. Otherwise costs are to be borne by the requested Party. Prior consultation will be required if extraordinary costs appear likely to exceed US\$500.

32 Both Parties are constrained from imposing "prejudicial or restrictive measures based on harmful tax practices" (the Understanding sets out the shared understanding of how this phrase will be interpreted). As noted above, New Zealand does not currently impose any such measures and, given that the TIEA provides for full exchange of information on tax matters with BVI, would not contemplate introducing such measures with respect to BVI while the TIEA is in force.

33 Reservations are not provided for under the TIEA.

34 Article 13 of the TIEA provides that any difficulties or doubts arising as to the interpretation or application of the TIEA are to be resolved, if possible, by mutual agreement between the competent authorities (for New Zealand, the Commissioner of

Inland Revenue or his or her authorised representative). The Parties may also agree on other forms of dispute resolution.

The Supplementary Agreement

35 The Supplementary Agreement imposes obligations on New Zealand to limit its taxing rights in certain limited circumstances. These circumstances are described in paragraph 16 above. At present the practical implications for New Zealand are effectively nil.

36 If New Zealand ever commences taxing maintenance payments derived from outside New Zealand by visiting students, those taxing rights will be constrained in respect of students from BVI who come to New Zealand to study.

37 Reservations are not provided for under the Supplementary Agreement

Measures the Government could or should adopt to implement the treaty action, including the specific reference to implementing the legislation

38 Subject to the completion of the Parliamentary treaty examination process, the TIEA and the Supplementary Agreement will be implemented into New Zealand domestic law in accordance with section BH 1 of the Income Tax Act 2007.

39 Section BH 1 authorises the giving of effect to certain tax agreements under New Zealand domestic law by overriding Regulation. That is, the Governor-General may declare by Order in Council that an agreement to which section BH 1 pertains will (within certain specified limits) override the Inland Revenue Acts, the Official Information Act 1982, and the Privacy Act 1993. This override is necessary to give effect to the terms of the two agreements (it will, for example, enable the TIEA to override New Zealand's secrecy requirements).

40 After the Orders in Council have entered into force, New Zealand will notify BVI by diplomatic note that all of its domestic constitutional and legal procedures for entry into force of the TIEA and the Supplementary Agreement are complete. BVI will likewise notify New Zealand by diplomatic note when it has completed its domestic constitutional and legal procedures for giving effect to the TIEA and the Supplementary Agreement. The TIEA and Supplementary Agreement will enter into force on the date of the last notification. Their provisions will then have effect for income years and charges to tax arising after a period of thirteen months following entry into force.

Economic, social, cultural and environmental costs and effects of the treaty action

41 No social, cultural or environmental effects are anticipated. Any economic effects are expected to be favourable, as noted above.

The costs to New Zealand of compliance with the treaty

42 New Zealand will be required to reimburse BVI for extraordinary costs (such as the cost of hiring translators or interpreters) that may arise from a New Zealand request made under the TIEA. However, the Understanding provides for consultation if extraordinary costs appear likely to exceed US\$500. This will ensure that New Zealand will only progress

information requests giving rise to significant reimbursement costs if the need to obtain the information justifies the expenditure.

43 New Zealand is likely to raise more requests for information than BVI but, to the extent that requests for information are received from BVI, New Zealand will incur administrative costs in complying with those information requests. As noted above, however, streamlined and effective mechanisms for dealing with exchange of information requests have already been established in relation to New Zealand's existing DTA network. The administrative costs of responding to requests from BVI are therefore expected to be marginal.

44 New Zealand may suffer some revenue loss from the limitation of taxing rights (but only, as noted above, if New Zealand ever commences taxing maintenance payments derived from outside New Zealand by visiting students). However, any such revenue loss would be minimal, and would be compensated by favourable financial, fiscal and economic effects of the TIEA.

45 Any costs arising to Inland Revenue as a result of the operation of the TIEA and Supplementary Agreement will be met within existing baselines.

Completed or proposed consultation with the community and parties interested in the treaty action

46 The Ministry of Foreign Affairs and Trade and the Treasury have been consulted and agree with the proposed treaty actions. Further, the concept of TIEAs in general has been canvassed in published policy work programmes.

Subsequent protocols or amendments to the treaty and their likely effects

47 No future amendments are anticipated. New Zealand will consider any proposed amendments to the TIEA and Supplementary Agreement on a case by case basis, and any decision to accept an amendment would be subject to the usual domestic approvals and procedures.

Withdrawal or denunciation provision in the treaty

48 Article 15 of the TIEA provides that either Party may terminate the TIEA by giving three months' written notice through the diplomatic channel. The Parties will remain bound by the Confidentiality provisions contained in Article 8 of the TIEA even after it has been terminated.

49 Article 9 of the Supplementary Agreement provides that either Party may, terminate the Supplementary Agreement by giving written notice through the diplomatic channel. Such termination will become effective, for New Zealand, in the income year beginning on or after 1 April in the calendar year next following that in which the notice of termination is given. For BVI, the termination will become effective in the income year beginning on or after 1 January in the calendar year next following that in which the notice of termination is given.

50 Any decision by New Zealand to terminate the TIEA or Supplementary Agreement would be subject to the usual domestic approvals and procedures.

Adequacy statement

51 The Inland Revenue Department has prepared this extended national interest analysis and has assessed it as adequate and in accordance with the Code of Good Regulatory Practice.