



International treaty examination of the Agreement between the Government of New Zealand and the Government of the Commonwealth of Dominica on the Exchange of Information with Respect to Taxes and Tax Matters

Report of the Finance and Expenditure
Committee

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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 Commonwealth of Dominica on the Exchange of Information with Respect to Taxes and Tax Matters and has no matters to bring to the attention of the House.

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

Appendix A

Committee procedure

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

Committee members

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Amy Adams

David Bennett

John Boscawen

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Appendix B

Agreement between the Government of New Zealand and the Government of the Commonwealth of Dominica on the Exchange of Information with Respect to Taxes and Tax Matters

National Interest Analysis

Executive Summary

1 On 16 March 2010 New Zealand signed the Agreement between the Government of New Zealand and the Government of the Commonwealth of Dominica on the Exchange of Information with Respect to Taxes and Tax Matters (“the TIEA”).

2 The TIEA establishes a mechanism by which tax officials from New Zealand and Dominica (“the Parties”) can request information from each other (such as business books and accounts, bank information, and information on the ownership of legal entities) 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. New Zealand already has a network of 35 double tax agreements (“DTAs”) in place with key trading and investment partners which provide for exchange of information arrangements similar to those which are established under the TIEA. TIEAs are designed to be used to establish exchange of information arrangements with jurisdictions where DTAs may not be appropriate, such as with low-tax jurisdictions. Dominica is a low-tax jurisdiction, and is also an important international finance centre. New Zealand, to date, has signed a total of 13 TIEAs.

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 that support the exchange of information. These rules ensure that requested information will be obtained and provided in a timely and effective manner. However, the rules also ensure that information may not be requested or used indiscriminately. Information requests may only be made in prescribed circumstances, and information received pursuant to a request may only be disclosed to authorised persons and used by those persons for authorised purposes (principally, the administration and enforcement of the domestic tax laws of the respective Party.) The text of the TIEA is attached as Annex A.

4 A key measure offered by New Zealand to encourage Dominica to enter into the TIEA is found in Article 11 of the TIEA. This Article constitutes an obligation on the Parties not to impose “prejudicial or restrictive measures based on harmful tax practices” on each other. This obligation relates to the OECD Harmful Tax Practices initiative, in which the prospect of OECD member countries imposing sanctions on or taking other defensive measures against jurisdictions identified as having harmful tax practices has previously been raised. The key identifier of harmful tax practices is whether a jurisdiction

engages in effective exchange of information on tax matters. Given that the TIEA provides for full exchange of information on tax matters with Dominica, it would be inappropriate for New Zealand to impose any such measures on Dominica while the TIEA is in force. The provision was included in recognition of this, but was expressed as a reciprocal obligation on both Parties.

Nature and timing of proposed binding treaty action

5 It is proposed that the TIEA be brought into force for New Zealand following completion of the Parliamentary treaty examination process in accordance with Standing Orders 388 to 391. It is expected that this process will be completed by the end of 2010.

6 Subsequent to completion of the Parliamentary treaty examination process, the TIEA can then be incorporated into domestic legislation by Order in Council pursuant to section BH 1 of the Income Tax Act 2007. Section BH 1 authorises the giving of overriding effect to DTAs by Order in Council.¹ Despite the reference to DTAs, the Agreements to which the section relates are those that have been negotiated for any one or more of the purposes listed in the section. The facilitation of exchange of information is a listed purpose. Therefore, the TIEA falls within the ambit of section BH 1.

7 Upon the promulgation of the Order in Council, the TIEA can then be brought into force, in accordance with Article 13 of the TIEA through an exchange of diplomatic notes that confirms the completion of the respective constitutional and legal requirements for entry into force of the TIEA by each Party. The TIEA comes into force on the date of the last notification, and takes effect for taxable periods beginning on or after 1 January following entry into force or, where there is no taxable period, for all charges to tax arising on or after 1 January following entry into force. New Zealand will ensure that the arrangement referred to in paragraph 18 is concluded before its notification is sent.

8 New Zealand policy, once an exchange of information arrangement has been established with another jurisdiction, is to approve that jurisdiction for the purposes of the venture capital exemption at section CW 12 of the Income Tax Act 2007. (Qualifying foreign investors from approved territories are exempt from paying income tax on any gains derived from the sale of shares in qualifying venture capital investment into New Zealand.) Approval of a jurisdiction for the purposes of section CW 12 requires the making of an additional Order in Council. This will be attended to after the TIEA enters into force.

9 The TIEAs will not apply to Tokelau, the Cook Islands or Niue

Reasons for New Zealand taking the treaty action

10 New Zealand domestic law specifically prohibits Inland Revenue from divulging information it holds to foreign jurisdictions, except when authorised by a tax treaty.²

¹ That is, the Order in Council may specify that the provisions of the agreement will have effect notwithstanding any provision of the Inland Revenue Acts, the Official Information Act 1982 or the Privacy Act 1993 – although only in relation to tax matters.

² Sections 81 and 88 of Tax Administration Act 1994 refer. The term “double tax agreement”, as used in section 88 (by virtue of its legislative definition) is also applicable to TIEAs.

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.

11 The most common type of tax treaty in which exchange of information provisions feature are DTAs. New Zealand currently has 35 DTAs in force. However, DTAs are typically only concluded between trading and investment partners with broadly similar tax systems. To cater for other situations, the OECD, in 2002 produced a model TIEA (with a comprehensive commentary) that provides solely for the exchange of information on tax matters. The OECD also, in 2000, published a list of low-tax international finance centres with which member countries are encouraged to negotiate TIEAs, based on the OECD model TIEA.³ The 2000 list includes Dominica.

12 New Zealand signed its first TIEA, with the Netherlands Antilles, on 1 March 2007. A second TIEA, with Bermuda, was signed on 16 April 2009. A further 11 TIEAs have since been signed. This brings the total number of TIEAs signed by New Zealand to 13. Each new TIEA concluded further expands New Zealand's network of exchange of information arrangements and reduces the tax evasion and avoidance options available to New Zealand residents.

13 The TIEA with Dominica provides a comprehensive set of rules to support the exchange of information. These rules are designed to ensure that requested information is obtained and provided in a timely and effective manner. The TIEA, however, also ensures that information is not to be requested or used indiscriminately. Requested information must be “foreseeably relevant” to the tax affairs of a particular person or entity (the OECD commentary clarifies that this means the Parties are not at liberty to engage in “fishing expeditions”). In addition, information received pursuant to a request may only be disclosed to authorised persons and may only be used by those persons for authorised purposes (principally, the administration and enforcement of the domestic tax laws of the Parties.)

14 Interference from bank secrecy and domestic tax interest rules is specifically prohibited as an obstacle to effective information exchange.⁴ Otherwise, rights and safeguards secured to residents of either jurisdiction by domestic law or administrative practice remain in effect. In particular, as noted above, the Parties are required to maintain strict confidentiality in relation to any information received pursuant to a request.

15 The text of the TIEA is attached as Annex A.

³ The 2000 OECD report “Towards Global Tax Co-operation: Progress in Identifying and Eliminating Harmful Tax Practices” refers.

⁴ This is a key aspect of the TIEA. Access to bank information on transactions and savings assists tax administrations in determining whether a person has correctly declared their income. Bank secrecy rules prevent the disclosure of bank information, and therefore facilitate tax evasion. TIEAs override any such domestic bank secrecy rules with an explicit treaty obligation to provide bank information. Domestic Tax Interest rules prohibit a jurisdiction from complying with a request for information if that jurisdiction itself does not itself need that information for tax purposes. TIEAs therefore also override any domestic tax interest rules with an explicit treaty obligation to provide information regardless of whether or not there is a domestic interest.

Consideration of other options

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

Advantages and disadvantages to New Zealand of the treaty action

Advantages

17 The TIEA will enable New Zealand tax officials to request tax records, business books and accounts, bank information, and ownership information from Dominica. Access to this previously unobtainable information will enhance Inland Revenue’s ability to detect and prevent tax avoidance and tax evasion (the TIEA permits New Zealand to request information in relation to “taxes of every kind and description”. Its likely principal application, however, will be in respect of income taxes). Any reduction in tax avoidance or tax evasion will be beneficial to New Zealand in financial, fiscal and economic terms.

18 The TIEA closely follows the 2002 OECD model TIEA and is subject to the comprehensive commentary produced by the OECD to support consistent interpretation and application of the TIEA provisions.

19 The approval of Dominica for the purposes of the section CW 12 venture capital exemption may result in increased venture capital investment into New Zealand.

Disadvantages

20 Dominica is unlikely to raise many requests for information from New Zealand. If requests for information are received from Dominica, 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 DTAs and TIEAs. The administrative costs of responding to requests from Dominica will therefore only be marginal. Experience gained from administering 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.

21 New Zealand may be required to bear some costs in relation to requests for information that it makes to Dominica. In order to set out a shared understanding of the Parties with respect to costs, as provided for by Article 9, a less-than-treaty status Arrangement will be signed between the two Parties before the TIEA enters into force. The Arrangement will likely set out the parameters where the costs to a request must be borne by the requested Party and when a requesting Party must reimburse the requested Party any costs relating to a request. It is intended that the Arrangement 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.⁵

22 The TIEA contains one article, Article 11, not found in the OECD model TIEA. Article 11 imposes an obligation on the Parties not to impose “prejudicial or restrictive measures based on harmful tax practices” against each other. 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.⁶ The key identifier of harmful tax practices is whether a jurisdiction engages in effective exchange of information on tax matters. Given that the TIEA provides for full exchange of information on tax matters with Dominica, it would be inappropriate for New Zealand to impose any such measures on Dominica while the TIEA is in force. The provision was included in recognition of this, but was expressed as a reciprocal obligation on both Parties.

23 New Zealand and Dominica do not have a strong bilateral relationship/history.

24 On balance, it is in New Zealand’s interests to conclude the TIEA with Dominica and to do so will achieve the Government’s policy objectives set out in the previous section.

Legal 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

25 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 (Article 1). Such information includes information that is relevant to the determination, assessment and collection of taxes, the recovery and enforcement of tax claims, or the investigation or prosecution of criminal tax matters. In the case of Dominica, the TIEA will apply to “taxes of every kind and description” (this also applies to NZ). As noted above, Dominica currently has a very limited tax system, and so is unlikely to make many requests for information from New Zealand.

26 The legal obligations established by the TIEA include the requirement to provide information without regard to whether the conduct being investigated would constitute a crime under the laws of the Requested Party if such conduct occurred in the Requested Party (Article 5). Such an obligation is a feature of the OECD model TIEA, and is intended to counter any domestic law provision of a country that prevents the exchange of information on matters unless they constitute a crime. No such standard exists in New

⁵ In recognition of the possibility that capacity issues in Dominica may mean that, on occasions, they may struggle to find the staff or other resources to comply with a single or multiple requests for information from New Zealand, it is intended that the MOU will provide for the possibility that the two sides will consult each other in such circumstances with a view to finding solutions. For example, where it is vitally important for Inland Revenue to obtain the information, New Zealand may agree to pay a larger share of the costs.

⁶ 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. The G20 Leaders Summit of 2 April 2009 re-raised the prospect of counter-measures against non-complying jurisdictions. The Leaders Statement from that Summit contained the statement that “we stand ready to deploy sanctions to protect our public finances and financial systems”.

Zealand, but they are a common feature of many of the jurisdictions with which New Zealand concludes TIEAs.

27 The TIEA also contemplates the possibility that representatives of the tax administration of the Requesting Party may be allowed to visit the Requested Party to interview individuals and examine records (Article 6). The treaty does not impose any obligation on the Requested Party to agree to such a visit. However, the possibility may prove to be useful in certain cases. For example, New Zealand officials may wish to consider visiting Dominica for the purposes of conducting interviews.

28 The Parties are required to maintain strict confidentiality in relation to any information received pursuant to a request (Article 8). 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).

29 Both Parties are constrained from imposing “prejudicial or restrictive measures based on harmful tax practices” (Article 11). New Zealand does not currently impose any such measures and, given that the TIEA provides for full exchange of information on tax matters with Dominica, would not contemplate introducing such measures with respect to Dominica while the TIEA is in force.

30 Reservations are not provided for under the TIEA.

31 Article 12 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; for Dominica, the Minister of Finance or the Minister’s authorised representative). The Parties may also decide upon other forms of dispute resolution.

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

32 Subject to the completion of the Parliamentary treaty examination process, the TIEA will be implemented into New Zealand domestic law by Order in Council in accordance with section BH 1 of the Income Tax Act 2007. It is expected that this process will be completed by the end of 2010.

33 Section BH 1 of the Income Tax Act 2007 enables TIEAs to be given effect by Order in Council. Section BH 1 provides that TIEAs will then override the Inland Revenue Acts, the Official Information Act 1982, and the Privacy Act 1993. The override of the Acts is necessary to give effect to the terms of a TIEA, given that the TIEA requires New Zealand to provide information it holds to foreign jurisdictions which is forbidden under those Acts. The Official Information Act is overridden to ensure that communications with other states during TIEA negotiations are not disclosed. The Privacy Act is overridden to ensure that information can be exchanged regarding natural persons under the exchange of information provisions of the TIEA.

34 After the Order in Council have entered into force, New Zealand will notify Dominica by diplomatic note that all of its domestic constitutional and legal procedures for

entry into force of the TIEA are complete. Dominica will likewise notify New Zealand by diplomatic note when it has completed its domestic constitutional and legal procedures for entry into force of the TIEA. The TIEA will enter into force on the date of the last notification (Article 13). The provisions of the TIEA will apply prospectively (for example, this means that the TIEA provisions cannot then be used to obtain information predating entry into force).

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

35 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

36 New Zealand is likely to raise more requests for information than Dominica but, if requests for information are received from Dominica, New Zealand will incur administrative costs in complying with those information requests (Article 9). 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 and TIEA network. The administrative costs of responding to requests from Dominica are therefore expected to be marginal.

37 In addition, New Zealand will likely be required to reimburse Dominica for extraordinary costs (such as the cost of hiring translators or interpreters) that may arise from a New Zealand request made under the TIEA. It is intended that the Arrangement described above will set out the parameters where New Zealand will be required to reimburse Dominica for information requests it makes. It is intended that 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.

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

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

39 The Ministry of Foreign Affairs and Trade and the Treasury have been consulted on the proposed treaty action. Further, the concept of TIEAs in general has been canvassed in published tax policy work programmes.

Subsequent protocols or amendments to the treaty and their likely effects

40 No future amendments are anticipated. New Zealand will consider any proposed amendments to the TIEA 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

41 Article 14 of the TIEA provides that either Party may terminate the TIEA by giving six 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.

42 Any decision by New Zealand to terminate the TIEA would be subject to the usual domestic approvals and procedures.

Agency disclosure statement

43 The Inland Revenue Department has prepared this extended national interest analysis. It has undertaken an analysis of the issue of implementing a TIEA between New Zealand and Dominica and the legislative and regulatory proposals arising from that implementation and has considered all other possible options in that process. Inland Revenue is of the view that there are no significant constraints, caveats and uncertainties concerning that regulatory analysis.

44 An Order in Council is required to implement the TIEA into New Zealand domestic law.

45 Inland Revenue is of the opinion that the policy options considered will not impair additional costs on businesses during the current economic recession; impair private property rights, market competition, or the incentives on businesses to innovate and invest; or override fundamental common principles (as referenced in Chapter 3 of the Legislation Advisory Committee Guidelines).

46 Inland Revenue notes that the form of this National Interest Analysis is consistent with that of a number of previous National Interest Analyses prepared in relation to other TIEAs concluded by New Zealand.