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NEW ZEALAND COUNCIL OF TRADE UNIONS
Te Kauae Kaimahi

**Submission of the
New Zealand Council of Trade Unions
Te Kauae Kaimahi**

to the

**Government Inquiry into Foreign Trust Disclosure
Rules**

P O Box 6645
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1. Introduction

- 1.1. This submission is made on behalf of the 31 unions affiliated to the New Zealand Council of Trade Unions Te Kauae Kaimahi (CTU). With 320,000 members, the CTU is one of the largest democratic organisations in New Zealand.
- 1.2. The CTU acknowledges Te Tiriti o Waitangi as the founding document of Aotearoa New Zealand and formally acknowledges this through Te Rūnanga o Ngā Kaimahi Māori o Aotearoa (Te Rūnanga) the Māori arm of Te Kauae Kaimahi (CTU) which represents approximately 60,000 Māori workers.
- 1.3. Thank you for your invitation to make a submission to this inquiry.
- 1.4. We see the issues at stake in this inquiry being primarily ethical: they are about the morality of aggressive tax avoidance, tax evasion, money laundering and other criminal behaviour and New Zealand's response to these, they are about fairness and they are about New Zealand's reputation. While they involve Foreign Trusts they are wider than that, including "look through" companies, secrecy and public scrutiny.
- 1.5. We are therefore very concerned that this inquiry's terms of reference and constitution are too narrow. However we make this submission because of the importance of the issues to working people in New Zealand and indeed around the world. The international union movement has for many years been active in raising its concerns about tax evasion, tax avoidance and money laundering.
- 1.6. While resolving the issues at stake requires 'technical' knowledge of tax and other laws and processes, the technical details should not be the primary focus of the inquiry. The objective should be to ensure New Zealand's self-respect and its ethical

position in the international community. The technical details are solely means to that end.

- 1.7. We observe at the outset that while there is a legal distinction between tax evasion (which is unlawful) and tax avoidance, the actual and moral distinction is much more blurred. Wealthy individuals and corporations seek advice on how to pay less tax. Their advisers propose ways to do that which are sometimes ruled illegal by the courts. Avoidance is therefore frequently hovering on the edge of evasion and sometimes crosses the line. It is commonly agreed that the most extreme forms of 'avoidance', often taking advantage of loopholes resulting from differing tax rules in different countries such as through transfer pricing and trusts, are tantamount to evasion because they can lead to almost complete avoidance of any tax and fail to contribute to the revenues of countries in which the individual or corporation is active. In a moral sense, these contrivances and evasion both occupy the same ground: they lead to some of the richest, most ruthless and most powerful individuals and corporations paying much less than the share of tax that society expects and has decided to be fair. We refer to this below as 'tax abuse', which should be understood to include both legal and illegal behaviour. Having the resources to hire the best tax lawyers and accountants and to pursue cases through administrative oversight and the courts to the highest level does not make such actions fair: on the contrary, it embodies unfairness and preservation of privilege.

2. Our concerns

- 2.1. Famous US jurist Oliver Wendell Holmes said "Taxes are the price we pay for a civilized society". Working people rely on a capable state that not only provides physical infrastructure and protection, but augments their 'market' incomes with a social wage: education, health, income when they are out of work or in retirement, protection of the environment and redistribution of income. This becomes even more important with high income and wealth inequalities in New Zealand and throughout the world.
- 2.2. To provide these services and social security, the state must raise revenue through taxes. The way this is done is important in its own right for a number of reasons. Firstly it can be a powerful way to redistribute income. Secondly it must be seen to be fair. That doesn't mean that everyone pays the same, but that there is general consent given to the process and principles for setting what is to be paid. A democratic system is the principal way to achieve this but it will be sustainable only

if it is seen to be carried out fairly and effectively. Thirdly, despite being enforceable by law, it requires the consent of the population because no enforcement authority can continue to collect enough revenue indefinitely in the face of widespread resistance and noncompliance. Widespread noncompliance by some undermines the willingness of others to comply.

- 2.3. Widespread tax abuse undermines all of these pillars of effective raising of revenue. It undermines our “civilized society”. Especially when tax abuse is carried out by the rich and powerful, it weakens the redistributive power of taxation. A tax system cannot be fair when tax cannot be collected from a privileged section of society. Finally, when people see others getting away with evasion and gross avoidance they are less likely to comply themselves and the system breaks down.
- 2.4. It is therefore a moral issue, impacting on fairness, use and misuse of political and economic power, and social cohesion.
- 2.5. Tax abuse is not simply a national matter. All countries face the same problem to varying degrees. It follows that it is immoral for New Zealand to aid and abet immoral acts in other countries whether or not particular forms of tax abuse impact directly on New Zealand’s revenue. In criminal law, a person aiding or abetting a crime is considered as culpable as a person committing the crime itself. The same is true in a moral sense, whether or not an immoral activity is strictly criminal or unlawful. The question of whether Foreign Trusts damage New Zealand’s tax base is therefore only a part of the issue. If, as seems clear, they are used by individuals or entities from other countries to undermine their own tax systems we have a moral responsibility to prevent it. If as well they are used for money laundering or other criminal activities our responsibility intensifies.
- 2.6. Allowing this abuse of other tax systems to continue makes us a tax haven. As tax expert Professor Michael Littlewood of the University of Auckland Law School writes (Littlewood, 2016, p. 3):

There is no agreed definition of “tax haven” but a workable definition for present purposes is that a tax haven is any country that wilfully allows itself to be used as a means of avoiding other countries’ taxes (meaning a fortiori that any country that deliberately sets out to allow itself to be used as a means of avoiding other countries’ taxes is also a tax haven). By this definition, New Zealand is plainly a tax haven.

- 2.7. It is now well documented that multinational corporations including Apple, Google, Facebook and the Australian banks have organised themselves for wholesale tax avoidance, if not evasion, in New Zealand and elsewhere¹. The revenue losses in New Zealand are almost certainly in the hundreds of millions of dollars annually and probably in the billions. These are economic losses to New Zealand as well as being losses to public revenue. There are some steps that the New Zealand government could take to reduce that attack on New Zealand's revenue, and Australia has taken more than New Zealand. However there are some that can only be carried out with international cooperation. The OECD BEPS process is prominent among such programmes against tax abuse.
- 2.8. New Zealand's influence in such forums depends on its reputation. We cannot credibly call on other countries to help us prevent tax abuse in New Zealand if we are at the same time aiding and abetting the gouging of their revenue bases. In addition, tolerating such abuse undermines trust in New Zealand's legal and administrative systems. Accepting such abuse on the basis that it makes money for a small group of lawyers and accountants gives the impression that our principles and morality are for sale. That is bad for New Zealand's social cohesion and in the long run bad for us economically because it discourages good business practices, longer term investment and longer term thinking.
- 2.9. If the question were whether systems set up in New Zealand aided oppression, torture, child abuse or other abusive behaviour we would hope and expect that there would be no hesitation in preventing those systems continuing. It would be obscene if the fact that they made money for businesses in New Zealand was raised as a defence. That should be the case even if their abusive behaviour had no direct impact within New Zealand, and even if they were acting legally in the countries where they were occurring. It should be no different with tax abuse.
- 2.10. We therefore submit that there is a clear case that the Foreign Trust regime should be prevented from allowing tax abuse, money laundering or other illegal activities to occur. If these activities cannot be prevented in any other way, the Foreign Trust regime should be closed down. However we consider other possibilities below.
- 2.11. Similarly, 'look through' companies should be prevented from providing opportunities for international tax avoidance.

¹ See for example the series of articles in the New Zealand Herald by Max Nippert on 18 March 2016 at http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11607279.

3. The role of Foreign Trusts

- 3.1. There are at least two ways in which Foreign Trusts are obnoxious.

Secrecy

- 3.2. Firstly, the cloak of secrecy that they provide to settlors (those who “transfer value” to the trust, such as by way of funds or assets, but also in other ways) and to beneficiaries (those who receive income from the trust) can be used to hide activities including tax abuse, money-laundering and other criminal activities. Tax abuse is a frequent use of ‘secrecy jurisdictions’ as the Tax Justice Network describes them² but not the only use.
- 3.3. Secrecy makes it difficult or impossible for tax and law enforcement authorities to track individuals or entities.
- 3.4. Disclosure requirements of Foreign Trusts are so minimal as to be almost useless. As Littlewood (2016, pp. 11–12) describes it

Section 59B [of the Tax Administration Act 1994] provides that a New Zealand-resident trustee of a foreign trust must supply certain information to the Commissioner of Inland Revenue. The principal requirement is that the trustee must disclose to the Commissioner “the name or other identifying particulars (for example, the date of the settlement on the trust) that relate to the foreign trust”. This is so badly drafted that one suspects it was deliberate. If Parliament’s intention had been to require the trustee to disclose the name of the *settlor*, it could easily have said so – but it did not. Presumably, then, Parliament did not intend to require the trustee to disclose the name of the settlor. For example, the settlor might be John Smith and he might call his trust the Abracadabra Trust. If the trustee discloses to the Commissioner that it is the trustee of the Abracadabra Trust, and nothing more, that would appear to satisfy s 59B. Another example: the trust might be established by Jack, who settles \$100 on the trustee. Jill then settles a further \$25 million on the trustee. The trustee discloses to the IRD that it is the trustee of a trust established by John. Again, that would seem to satisfy s 59B.

All the trustee is obliged to supply is the name or other identifying particulars (for example, the date of the settlement on the trust) that relate to the foreign trust. The trustee is generally not required to supply any information at all as to the following:

1. the name of the settlor;

² <http://www.taxjustice.net/faq/>

2. the country of residence of the settlor;
3. the names of the beneficiaries;
4. the country of residence of the beneficiaries;
5. the assets held by the trust;
6. the country in which the assets are situated;
7. the value of the assets;
8. the amount of income generated by the assets;
9. to whom, if anyone, the income is distributed.

- 3.5. Littlewood notes that there is a slightly more stringent requirement for Australian resident settlors, namely that the Australian residency should be declared to the Inland Revenue Department (IRD) by the trustee. IRD then informs the Australian Tax Office of this fact and the other (vestigial) information provided.
- 3.6. The trustee is required to hold certain information which may be helpful to authorities in tracking down settlors and beneficiaries (though only “if known” to the trustee).
- 3.7. However authorities in other countries can only access this by asking IRD to require the trustee to provide it. The overseas authorities must first know that the trust exists, where it is located, and that it is of interest to them. That is unlikely.
- 3.8. This effective wall of secrecy protects tax abuse, money laundering and criminal behaviour and encourages the use of Foreign Trusts for those purposes.

Tax loop-holes

- 3.9. Secondly the structure of New Zealand's Foreign Trusts provides at least one tax loophole. In New Zealand law, the tax-residency of the settlor (along with the source of the income) determines whether income is taxable. To simplify, only if the settlor is New Zealand resident is overseas income taxed. However in most overseas jurisdictions, the tax-residency of the trustee determines tax status. Therefore a settlor from one of those jurisdictions can gain tax-free or low-tax status by using a New Zealand Foreign Trust with a New Zealand-resident trustee (see for example Littlewood, 2016, pp. 7–9).

4. Solutions

- 4.1. It has been asserted that there are some benefits to offering Foreign Trusts which are real ones that are not connected to tax abuse or illegal activities. We have yet to hear a convincing case being made for this other than that they provide income to some lawyers and accountants. Unless that case can be made we would support abolishing them.
- 4.2. However if there is a valid case for their continuing existence we and the rest of the New Zealand public need to be assured that there are robust protections against their abuse. These should include at least an end to their secrecy and an end to their ability to provide tax loopholes. Both of these protections are necessary. If the secrecy is removed but they can still provide tax loopholes we have solved only half the problem. If we remove the tax loopholes but retain secrecy then their use for illegal activities or tax abuse which is protected by secrecy has not been prevented.
- 4.3. Regarding an end to secrecy, a public register of Foreign Trusts should be established, much as we have public registers of companies and incorporated societies. The information provided through those registers should include the names and addresses of all settlors, trustees and beneficiaries, ultimate settlors and beneficiaries, annual returns and sets of financial accounts which include the assets held by the trust, their value and where they are situated, the income they generate, to whom that income is distributed, and any other distributions made (such as of capital).
- 4.4. Trustees should also be required to obtain, verify and retain adequate, accurate and current information on the beneficial ownership and control of trusts. They should be required to make that information available to the appropriate government authorities on request. We note that in October 2013 the Mutual Evaluation of New Zealand by the international Financial Action Task Force (FATF) under the auspices of the OECD found that New Zealand was non-compliant on this matter. It found that “it cannot be determined that information on the ultimate beneficial owners is accessible and/or up-to-date in all cases” (Financial Action Task Force, 2013, p. 42). The New Zealand Government undertook to implement the FATF recommendations in a statement to the Corruption Summit in London this month.³

³ https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/522722/New_Zealand.pdf

- 4.5. The information should also be made available proactively to any international registers established for the purpose of stamping out tax abuse, money laundering and criminal behaviour and in agreements to exchange information on tax, corruption, money laundering and crime.
- 4.6. We do not consider that simply providing such information to a government authority (such as the IRD) is sufficient because it does not resolve the problem that the victims of abusive behaviour may not know of their existence, location or identity. The Foreign Trusts must be open to scrutiny and search by individuals, journalists and overseas authorities responsible for enforcement⁴. In any case, we have not heard any convincing case why the Foreign Trusts (or domestic trusts) should have any less requirements for openness than companies and incorporated societies which have searchable online registers.
- 4.7. It has been asserted in the media that the secrecy surrounding Foreign Trusts may be a protection for people whose safety or assets are threatened such as by an oppressive regime. We have not been presented with any evidence that this is at all a significant use of the trusts. To the extent that it is a real problem, a procedure and authority could be set up for such people to apply to have such details as would compromise their safety withheld from public scrutiny (but not withheld from New Zealand authorities). However a case would also need to be made that New Zealand had a responsibility for providing such facilities. It is not of itself a reason for continuing to allow Foreign Trusts.
- 4.8. Regarding removing the tax loopholes, at the least the well-known one described above at 3.9 should be removed. Littlewood (p.16) considers that the crucial aspect is that in 1988 “a New Zealand-resident trustee was exempted from tax on income derived from outside New Zealand, so long as the income was not distributed to a New Zealand-resident beneficiary”. He states that

It would be possible, indeed straightforward, to withdraw the exemption while leaving the [resident settlor] rule unchanged.

That could be done by simply repealing ss CW 54 and HC 26 of the Income Tax Act 2007. The result would be that a New Zealand-resident trustee would be subject to tax

⁴ The London Anti-corruption Summit, attended by New Zealand stated: “We support the role that the media, including investigative journalists, the business community, and civil society can play in complementing and reinforcing corruption reporting systems including effective monitoring and follow up.” The Summit also covered tax matters. See p.4 <https://www.gov.uk/government/publications/anti-corruption-summit-communicue>

on income derived from outside New Zealand, even where the income was distributed to a non-resident beneficiary. That would effectively bring the problem to an end.

- 4.9. Another approach might be to subject the trustee to tax where the settlor is from a jurisdiction where the trustee is subject to tax.
- 4.10. However careful scrutiny of the rules is required to determine whether other loopholes exist. If an assurance cannot be given that all foreseeable loopholes have been plugged then Foreign Trusts should be abolished. If the Foreign Trusts continue then IRD should be funded to apply special scrutiny to their activities.

5. Conclusion

- 5.1. The behaviour of those involved in Foreign Trusts is primarily a moral and reputational issue, not a technical tax one. Neither is tax abuse the only issue: so are money-laundering and illegal activities.
- 5.2. Unless a strong case can be made that the Foreign Trusts perform a socially useful purpose and that we can prevent their use for anti-social purposes in New Zealand and globally, they should be abolished.
- 5.3. However we consider an alternative solution of making them as open as companies and incorporated societies, including proactively making their details available to international public registers, and removing the tax loopholes they provide as long as these can be accomplished effectively.
- 5.4. The current situation cannot continue.
- 5.5. We are available to discuss this submission further if requested.

6. References

- Financial Action Task Force. (2013). *2nd Follow-up Report: Mutual Evaluation of New Zealand*. Paris, France: Financial Action Task Force. Retrieved from <http://www.fatf-gafi.org/publications/mutualevaluations/documents/fur-new-zealand-2013.html>
- Littlewood, M. (2016). *Using New Zealand as a tax haven: How is it done? Could it be stopped? Should it be stopped?* (Working Paper No. 1 of 2016). Auckland, N.Z.: University of Auckland. Retrieved from http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2761993