The Treasury

Foreign Trust Inquiry Information Release

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www.treasury.govt.nz/publications/reviews-consultation/foreign-trust-disclosure-rules

Key to sections of the Official Information Act 1982 under which information has been withheld.

Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

<table>
<thead>
<tr>
<th>Reference</th>
<th>Description</th>
<th>Section(s)</th>
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<tr>
<td>[1]</td>
<td>to prevent prejudice to the security or defence of New Zealand or the international relations of the government</td>
<td>6(a)</td>
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<td>[2]</td>
<td>to protect the privacy of natural persons, including deceased people</td>
<td>9(2)(a)</td>
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<td>[3]</td>
<td>to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials</td>
<td>9(2)(f)(iv)</td>
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<td>[4]</td>
<td>to maintain the effective conduct of public affairs through the free and frank expression of opinions</td>
<td>9(2)(g)(i)</td>
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<td>[5]</td>
<td>that the making available of the information requested would be contrary to the provisions of a specified enactment [the Tax Administration Act 1994]</td>
<td>18(c)(i)</td>
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Where information has been withheld, a numbered reference to the applicable section of the Official Information Act has been made, as listed above. For example, a [2] appearing where information has been withheld in a release document refers to section 9(2)(a).

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9 and section 18 of the Official Information Act.
Tax policy report: Foreign Trusts Rules

Date: 12 December 2014  
Priority: Medium  
Security Level: In Confidence  
Report No: T2014/2190  
IR2014/620

Action sought

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<th>Action Sought</th>
<th>Deadline</th>
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<tr>
<td>Minister of Finance</td>
<td>Agree to the recommendations in this report</td>
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<tr>
<td>Minister of Revenue</td>
<td>Agree to the recommendations in this report</td>
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Contact for telephone discussion (if required)

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<tr>
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<th>Position</th>
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12 December 2014

Minister of Finance
Minister of Revenue

Foreign Trusts Rules

1. In a recent report giving an expected timeline for BEPS related work (refer to IR2014/531), we signalled that our foreign trust rules could be improved. This report proposes that officials discuss with Ministers the merits of a review of the current rules for taxing foreign trusts.

2. The rules were introduced in 1988, as part of a wider package of international tax reforms. We believe that the rules reflect good policy. However, they do depart from international norms. Most countries’ tax trusts on the basis of the residence of the trustee (which was New Zealand’s previous approach). However, from 1988, New Zealand’s rules for the taxation of trusts are based on the residence of the settlor. The difference between the two approaches creates an arbitrage opportunity (see paragraph 4 below).

3. New Zealand’s approach of taxing a trust if the settlor is a New Zealand resident — regardless of the residence of the trustees — is principled. The general idea is that even though the trustees have legal ownership of the assets, the settlor is really the economic “power behind the throne” because they set up the trust by transferring the assets to the trust and appointing the trustees. They really control who the beneficiaries are and the terms of the trust deed. Taxation based on the settlor’s residence makes it difficult for New Zealand residents to hide their assets offshore.

4. However, from this starting point it naturally follows that a trust with a foreign settlor is a foreign trust even when the trustees are resident in New Zealand. A foreign trust that derives foreign sourced income will not be taxed in New Zealand on that income (assuming no New Zealand resident beneficiaries). That income might also be free from tax in the foreign settlor’s home jurisdiction because New Zealand’s approach to taxing trusts differs from the international norm.

5. There is now a foreign trust industry in New Zealand that allows non-resident settlors to accumulate assets and income in a foreign trust with no New Zealand tax. Advisors/firms help foreigners establish and manage foreign trusts for a fee.

6. This has attracted criticism internationally — along the lines that we are a tax haven in this respect.

7. Over the last ten years, we have improved some of the regulation of the industry to ensure we can provide information to our treaty partners – especially Australia by requiring foreign trusts to be registered. Even so, there is a concern that our regulation is not good enough. Also, it is difficult to enforce compliance with the rules.

8. We are not a tax haven, because tax havens are all about secrecy. We exchange information under our tax treaties, and have disclosure and record-keeping requirements in place that currently support the need to meet treaty requests for information about foreign trusts. (Note, however, that the rules are more robust concerning exchange of information on foreign trusts with Australia, than for exchange of information with other jurisdictions.)

9. Having said this, the perception that we might be a tax haven are damaging to New Zealand’s “clean” international reputation. This can only get worse in view of future developments by the OECD on BEPS, harmful tax practices, beneficial ownership and AEOI. In particular, although the OECD’s Forum on Harmful Tax Practices (FHTP) and Global Forum on Transparency and Exchange of Information for Tax Purposes have previously scrutinised our foreign trusts rules, and identified no issues with the rules, the FHTP is currently redefining what the OECD sees as an unacceptable tax regime, and New Zealand will be subject to future review on the basis of the redefined criteria.

10. In light of that we have concerns about the following:

- The adequacy of our disclosure and record-keeping requirements – particularly in light of expanding obligations to exchange information now and in the future as a result of FATCA, AEOI, and the multilateral agreement for exchange of information and assistance.

- Our ability to realistically bring the regime up to the appropriate standard in a way that is enforceable and ensures compliance;

- The increased cost to Inland Revenue in policing a new set of rules – especially when there is no New Zealand tax to be collected.

11. The overall value of the industry to New Zealand economy should be weighed against these concerns. This is inherently difficult to measure, especially the value generated indirectly. However, our best estimates are that:

- There are about 8,000 foreign trusts with a New Zealand resident trustee that are currently active. This figure is based on the information disclosed to Inland Revenue under statutory disclosure requirements, but we understand that this figure may be a significant underestimate because of the existence of structures whose purpose is to defeat the statutory disclosure requirements.

- The value of the fees collected in respect of foreign trusts, plus employment income for 3rd party employees and principals for each foreign trust provider
entity, amounts to approximately $24 million per annum, on average. This figure has been calculated from Inland Revenue data. (Other report estimates of fee income resulting from the industry range from $20 million per annum\(^1\) to $50 million per annum.\(^2\))

- The contribution to the New Zealand tax take, in terms of income tax on fee income, goods and services tax, and PAYE paid on behalf of 3rd party employees and principals for each foreign trust provider entity, is around $3 million per annum, on average. This figure has been calculated from Inland Revenue data.

12. The next step is for us to discuss with you the merits of adding a review of foreign trusts to our work programme.

**Recommended action**

We recommend that you:

1. **Note** that in a recent publically released report giving an expected timeline for BEPS related work (refer to IR2014/531), we signalled that our foreign trust rules could be improved.

   Noted

2. **Agree** to discuss with officials early next year whether a project to review the rules for taxing foreign trusts should be added to the tax policy work programme.

   Agreed/not agreed

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Treasury

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Inland Revenue

**Hon Bill English**  
Minister of Finance

**Hon Todd McClay**  
Minister of Revenue

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\(^1\) IFSDG, “Exporting Financial Services: A Report from the International Funds Services Development Group” (IFSDG, 2011) at 47. Cabinet established the IFSDG in March 2010 to look at financial services opportunities for New Zealand. The estimate is said to be from industry sources in 2009.