IMPLICATIONS OF THE PANAMA PAPERS FOR THE NEW ZEALAND FOREIGN TRUSTS REGIME

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This article discusses the implications of the Panama Papers for the legal requirements concerning the disclosure of information and documents relating to offshore financial planning under the New Zealand foreign trust regime. It first identifies the nature of New Zealand foreign trusts (NZFTs) through an outline of our laws of trusts and foreign taxation. It then focusses on the current requirements for disclosure of information relating to NZFTs to authorities in New Zealand and in foreign jurisdictions, the reasoning of the Inquiry into NZFTs, and the Government's response to the Inquiry's recommendations. Finally, it briefly places the Report's conclusions in the context of the submissions it received and the wider international shift to greater transparency of financial information.

I INTRODUCTION

The fact that digital files containing 11.5 million internal documents from the Panama law firm Mossack Fonseca had been passed on to journalists at the Suddeutsche Zeitung,1 was one of the major news stories in early 2016. After receiving the data, the journalists began a detailed, and still ongoing, collaborative investigation with other journalists worldwide under the umbrella of the International Consortium of Investigative Journalists ('ICIJ').2 In New Zealand, journalists released stories detailing how New Zealand legal structures were

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implicated in offshore financial schemes that were possibly linked to criminal activity or tax evasion. The Government soon announced an inquiry into the New Zealand foreign trust regime, the report of which (the Report) criticised the current regulatory regime and recommended significant changes to the disclosure and recording obligations.3 The Government has accepted most of the Report's recommendations,4 with the statutory measures necessary to implement these recommendations being introduced to Parliament in the Taxation (Business Tax, Exchange of Information, and Remedial Matters) Bill. This is the major immediate implication of the Panama Papers for New Zealand law.

This article discusses the legal implications of the Panama Papers for the New Zealand foreign trust regime. It first highlights the criticisms that were voiced about New Zealand's role in illegitimate offshore financial arrangements and the response to these criticisms. Then, after briefly outlining the legal nature of New Zealand foreign trusts (NZFTs), its major focus is a discussion of the Inquiry's Report and recommendations concerning the current and proposed requirements for disclosure of information relating to NZFTs to authorities in New Zealand and in foreign jurisdictions. The article also places the Report's conclusions in the context of the submissions it received and the wider international shift to greater transparency of financial information, and briefly discusses the proposed legislation that has been introduced by the Government to implement the changes.

II NEW ZEALAND'S ROLE IN THE PANAMA PAPERS SCANDAL

Many of the earliest stories arising from the Panama Papers disclosure concerned the revelations that prominent politicians and public officials hold wealth in secretive offshore structures,5 raising suspicions of political corruption. The identification of persons on Mossack Fonseca's client list who had already been blacklisted by governments for their links to crime, corruption, and terrorism was also widely

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reported. Another key part of the scandal was the probable use of offshore financial centres for tax avoidance and evasion.

New Zealand was implicated in the Panama Papers as soon as the story broke. Indeed the Papers arrived just weeks after unrelated news coverage concerning the use of New Zealand trusts and companies in alleged corruption in Malta and a number of oil-producing countries. But the major focus of New Zealand media interest was the possible use of the NZFT regime for the purposes of tax avoidance or evasion. This was not a new concern: there had been criticism of the use of the NZFT regime in the print and television media in 2012. But the Panama Papers painted a more vivid picture of overseas (often Latin American) wealth being held though New Zealand trusts as a safe, secret and tax-free structure for the assets. One trust provider stated that "Trusts are considered sacred cows in New Zealand law and if properly structured cannot be set aside by a court, by a government, by a wife, by a creditor or by any inheritance disputes. They are the legal Fort Knox of asset protection". While the Government initially defended the present system of

8 Radio New Zealand "New Zealand caught up in Panama data leak" (4 April 2016) Radio New Zealand <www.radionz.co.nz>; Hamish Fletcher "Panama Papers: Leak leaves stain on New Zealand's name" New Zealand Herald (online ed, 9 April 2016).
9 Rob Stock "Unaoil bribery scandal: New Zealand shell company linked to Unaoil scandal" (31 March 2016) Stuff <www.stuff.co.nz>; Jacob Borg "No mention of 'estate planning' in Mizzi's New Zealand trust; minister sues: 'character assassination'" Times of Malta (online ed, 21 May 2016).
10 "Panama papers: Mossack Fonseca 'bragged about lax New Zealand tax rules'" New Zealand Herald (online ed, April 11 2016); Patrick O'Meara "Panama Papers put NZ laws under scrutiny" (4 April 2016) Radio New Zealand <www.radionz.co.nz>.
11 Chalkie (Tim Hunter) "NZ foreign trusts among global tax havens" (22 August 2012) Stuff <www.stuff.co.nz>; Terry Baucher "Tax sleuth Terry Baucher looks at the curious world of foreign tax trusts and how they are a legitimate means of tax avoidance for non-residents" (12 October 2012) Interest.co.nz <www.interest.co.nz>.
12 Gyles Beckford et al "NZ at heart of Panama money-go-round" (9 May 2016) Radio New Zealand <www.radionz.co.nz>.
13 Gareth Vaughan, Denise McNabb and Richard Smith "US$7 billion fraudster Allen Stanford, the 'outside wife', 'favourable tax laws,' and 'the legal Fort Knox of asset protection' - New Zealand foreign trusts" (27 June 2016) Interest.co.nz <www.interest.co.nz> quoting from the promotional website of Trust New Zealand, which is part of Equity Trust International Ltd.
taxation of foreign trusts, it soon saw fit to set up an inquiry tasked with assessing the accuracy of the criticisms that had been levied. The inquiry was undertaken by John Shewan, an experienced New Zealand taxation expert. Some commentators criticised the selection of a commercial tax practitioner to review the adequacy of our tax rules, the suggestion essentially being that this was like the poacher turning gamekeeper. But, as further detailed below, the report that Mr Shewan produced was fairly critical of the current rules, finding that they were inadequate and recommending significant changes to the disclosure requirements for foreign trust information. This satisfied at least some critics of the existing regime. Most significantly, the Report clearly persuaded the Government that action was necessary, the latter quickly stating that it would put in place most of the changes proposed.

This attention on the NZFT regime provided a useful learning opportunity for the general public: the law relating to foreign trusts was probably not a dinner table topic before the Panama Papers hit the media. Subsequently, there were a number of informative news articles and blog posts explaining the workings of the regime and its possible failings to the layperson, with academic tax experts such as Craig

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14 Jane Patterson "Overseas trust activities not NZ's concern – minister" (5 April 2016) Radio New Zealand <www.radionz.co.nz>; "Utterly incorrect’ - Prime Minister John Key denies Panama Papers are evidence NZ is a tax haven" New Zealand Herald (online ed, 9 May 2016); Ron Pol "Ron Pol compares one part of NZ's foreign trusts regime to a criminal getaway car manufacturing industry and asks whether the PM will take action or double-down on offshore trusts" (8 May 2016) Interest.co.nz <www.interest.co.nz>.

15 Radio New Zealand "NZ to review foreign trust laws – Key" (11 April 2016) <www.radionz.co.nz>.


17 Ron Pol "Ron Pol explores barriers and opportunities facing the Shewan 'review' of NZ foreign trusts" (16 June 2016) Interest.co.nz <www.interest.co.nz>.

18 Isaac Davison "Review: Existing foreign trust disclosure rules inadequate" New Zealand Herald (online ed, 27 June 2016).

19 Ron Pol "Ron Pol cheers John Shewan's report on foreign trust disclosure, says with him exercising the nuclear option the government's choices are now stark" (28 June 2016) Interest.co.nz <www.interest.co.nz>.

20 The Government's announcement is noted above n 4. See also Isaac Davison "Government to make sweeping changes to foreign trusts in wake of Panama Papers" New Zealand Herald (online ed, 13 July 2016); Jane Patterson "Govt accepts Shewan's foreign trust advice" (13 July 2016) Radio New Zealand <www.radionz.co.nz>.

21 Terry Baucher "Terry Baucher argues now is a good time to address unintended consequences through a full review of the tax rules for trusts" (13 June 2016) Interest.co.nz <www.interest.co.nz>; Deborah Russell "Foreign trusts 101: a plain English introduction amid the
Elliffe, Michael Littlewood, and Deborah Russell explaining the regime to the media and public.\(^{22}\) Professor Littlewood released a clear and concise analysis on a free research depository,\(^{23}\) as well as providing a detailed submission to the Government Inquiry.\(^{24}\) Further in-depth discussion of the history and rules of the taxation of foreign trusts is also publicly available in a series of articles by Professor John Prebble, who was a member of the consultative committee that advised the government at the creation of the current foreign trusts regime.\(^{25}\) Now it is released, the Inquiry's Report provides another concise and lucid presentation of the basic features of the regime,\(^{26}\) and the information and submissions on which the Report's conclusions are based is collected on a Treasury webpage.\(^{27}\) Given these alternative sources of information about the NZFTs regime, it is appropriate to merely restate the basics here to provide the context of the proposals for change.

### III THE NEW ZEALAND FOREIGN TRUST REGIME

#### A The Legal Nature of a New Zealand Foreign Trust

The legal nature of a NZFT is that, in essence, it is a trust created according to the general law of trusts, but to which special rules of taxation apply under the Income Tax Act 2007 due to the lack of connection to New Zealand of the settlor, beneficiaries, and income of the trust.\(^{28}\) As such, NZFTs are mainly of use only to persons who are not New Zealand tax residents, who use the trust to pay less tax in
the jurisdiction where they are a tax resident (or for other purposes, without incurring New Zealand tax liability).²⁹

A NZFT is created by the settlor (the person who 'settles' the property on the trust) as a tool for managing her wealth. In any trust, the settlor seeks to provide her property for the benefit of beneficiaries, not by giving them absolute ownership of the property but by transferring it to a trustee who will manage the property for the benefit of the beneficiaries.³⁰ To benefit from the NZFT regime, the settlor will be a person who is not tax resident in New Zealand, and is in that sense 'foreign'.³¹ She arranges for her property rights to be transferred into the ownership of another person, the trustee – who is based in New Zealand.

The trustee may be an individual or a company. They will have a title to the trust property, which will usually be an asset that is held in a foreign jurisdiction, either directly or structured through New Zealand entities or an overseas company. The asset may be an active investment such as a company or a passive investment such as shares or bonds, but one of the keys to not being liable to New Zealand taxation is that the income from those investments is characterised as to have a foreign source (rather than having a New Zealand source).

Finally, to prevent New Zealand taxation on the income of the trust there must be no distribution to any beneficiary who is a New Zealand tax resident.³² This is really just part of the general policy to tax residents' worldwide income and not to tax non-residents' income.³³ The combination of foreign source and no New Zealand settlor or beneficiaries receiving distributions means that no New Zealand tax is payable.³⁴

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²⁹  *Inquiry Report* at 4.10-4.18; Littlewood, above n 23, at 1-3.
³⁰  There are myriad textbook discussions of the nature of trusts – which have the same basic structure throughout the common law world – but one important text is James Penner *The Law of Trusts* (10 ed, Oxford University Press, Oxford, 2016).
³⁴  For further discussion, see Elliffe *International and Cross-Border Taxation in New Zealand*, above n 33, at 101-107 and 145-149.
The basic structure of a NZFT was represented in the following diagram provided in the Inquiry's Report:\textsuperscript{35}

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\textbf{B The Origins and Uses of the NZFT Regime}

Despite some assertions that it is a loophole created specifically to help the wealthy avoid taxation, as the Report observes the NZFT regime is better seen as the by-product of a legitimate policy choice in international taxation.\textsuperscript{36} The rationale for this regime is based on the view that a trustee is, in economic terms, merely an agent for the settlor, achieving the settlor's purposes in a way that the settlor (for practical or legal reasons) could not.\textsuperscript{37} From the perspective of New Zealand taxation, there was a concern that foreign trusts established in other jurisdictions by New Zealand settlors would erode the tax base unless their income was taxed.\textsuperscript{38} If we view the settlor as a person who has set up an offshore structure to hold wealth that may have

\textsuperscript{35} The diagram is Figure 2 of the \textit{Inquiry Report} at [4.29].

\textsuperscript{36} \textit{Inquiry Report} at [4.18]. See generally the analysis of John Prebble in the articles cited above n 25.


otherwise been invested – and its income taxed – in New Zealand, then it makes sense to attribute the income to the settlor for tax purposes, unless that income is clearly not going to find its way into the hands of the settlor. However, as the Report observed:39

the old trust tax rules made it relatively easy for New Zealand residents to escape tax on their offshore income. This could be achieved by establishing a trust offshore and settling investment assets on it. The trustee, who would be a non-resident of New Zealand, would invest the funds and accumulate income. No New Zealand tax would be payable on the income except where it was distributed within six months of the trust’s tax year end to beneficiaries resident in New Zealand. Distributions after that time were capital, and not taxable. Unsurprisingly, distributions of income were rare.

On the other hand, if a foreign settlor invests wealth in foreign assets so as to generate income overseas, and that income is regarded either as accruing to them or the trust’s beneficiaries (being persons are not otherwise liable for income tax in New Zealand), then it seems consistent to not tax that income in New Zealand.40 The New Zealand resident trustee should not be taxed on this income, as they cannot use it for their own benefit. As the Consultative Committee argued in 1988, "this is the appropriate treatment since such income has no definite connection with New Zealand apart from the existence here of the trust administrator … who will … have no beneficial interest in the income.”41

The non-taxation of foreign trusts in New Zealand makes them an attractive option for people who wish to take advantage of the trust structure – for example those who come from civil law countries that do not recognise the trust. Simply by transferring ownership to the New Zealand trustee along with the requisite payment and paperwork, the settlor can utilise the trust institution. The reasons for setting up a trust that the promoters of NZFTs gave to prospective clients include protecting the property from government confiscation, claims from former spouses / partners, forced heirship claims, and claims from creditors.42 These basic features and consequences of the common law trust were the benefits identified in the submission

39 Inquiry Report at [4.13].
41 Cited in the Inquiry Report at [4.17].
42 Inquiry Report at [4.25]-[4.36].
on behalf of the New Zealand branch of the Society of Trust and Estate Practitioners.\textsuperscript{43} It stated that:\textsuperscript{44}

Whilst foreign trusts might sound exotic to many, they are in broad terms no different in many respects to New Zealand domestic trusts. Clients use them for privacy, controlled succession of assets to future generations, and some measure of asset protection.

Similarly, the submission from trusts provider TGT Legal identified the benefits sought by their clients in setting up NZFT’s as relating to its nature as a trust, rather than tax benefits or secrecy:\textsuperscript{45}

Individuals and families will often have significant businesses and other assets in a number of jurisdictions around the world and with family members, spanning several generations, may live in different parts of the world. For these families the establishment of a trust provides a central location from which the relevant assets can be administered and managed. Moreover the use of the trust enables the benefit of these assets to be enjoyed by successive generations without title having to change hands.

However, equally as attractive it seems, at least from these promotional materials, is the ability to keep the existence and nature of the trust secret due to the lack of disclosure that was required to establish a foreign trust. Indeed, when one considers that the trust property of the NZFT is likely to be held in a ‘tax haven’ jurisdiction where the trust is a recognised legal institution and there is no taxation of trust income, the suspicion arises that it is not in fact the trust institution itself that is important to some settlors – rather it is the additional layer of secrecy that it provides without tax consequences in New Zealand. This structuring of asset ownership through multiple layers based in different jurisdictions is called ‘laddering’, and is a well-known means of making beneficial ownership harder to identify.\textsuperscript{46} The example of the use of foreign trusts by Australians 'drying up' when further disclosures were introduced for trusts with Australian settlors provides further anecdotal evidence of

\begin{itemize}
\item \textsuperscript{43} John Hart “STEP NZ Branch Submission” <www.treasury.govt.nz> at [6] and [9].
\item \textsuperscript{44} At [9].
\item \textsuperscript{45} TGT Legal Submission <www.treasury.govt.nz>.
\end{itemize}
the importance of secrecy.\textsuperscript{47} With this evident desire for secrecy comes the charges of New Zealand being a tax haven where people can hide their wealth from their jurisdiction of tax residence.

This 'tax haven' concern has been on the agenda of the Inland Revenue (IR) for many years, as documents released in relation to the Inquiry demonstrate. Indeed, despite the increased disclosure and record-keeping requirements being introduced in 2006, the IR has continued to be worried about the international pressures concerning the NZFT regime. A 2014 IR tax policy report noted international perceptions that New Zealand was a tax haven in this respect, which were "damaging to New Zealand's "clean" international reputation''.\textsuperscript{48} That the NZFT regime may be seen in this light was also the conclusion of Professor Littlewood, whose submission stated that:\textsuperscript{49}

New Zealand law allows non-residents to use trusts established in New Zealand to avoid the tax they would otherwise have to pay in their home country. … [A] tax haven is "a jurisdiction that allows itself to be used by non-residents as a means of avoiding the tax that they would otherwise have to pay in their home countries". By this definition, New Zealand is plainly a tax haven.

As can be seen from the analysis of other tax law experts and IR officials mentioned above, this is not a unique view. Indeed, the use of the NZFT regime for tax haven purposes was seen by one Treasury tax policy official as a likely effect of the changes in our international tax law policy before they were introduced.\textsuperscript{50}

\textbf{C Balancing NZ Tax Policy with International Tax Co-operation}

As in many areas of law and policy, there can be a number of normative views taken towards the adequacy of current arrangements compared to other possibilities – and these views are driven by wider ideological and economic assumptions.\textsuperscript{51}

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\textsuperscript{47} Inquiry Report at Appendix 4, [18].
\textsuperscript{49} Michael Littlewood “Submission”, above n 24, at [8] and [9].
\textsuperscript{50} See Simon Boyce "Submission to the Foreign Trust Disclosure Inquiry" at 1 <www.treasury.govt.nz>.
Professor Elliffe encapsulates the basic divergence in perspective on the NZFT regime:

This regime could potentially provide a vehicle for foreigners to use New Zealand trusts in their international tax planning structures. Exemption from New Zealand tax in these circumstances has been seen, variously, as a strong positive for the New Zealand economy on the one hand, and on the other hand, as an irresponsible contribution to international tax evasion.

The fact that there are political questions involved in this area is highlighted by the interesting comments of Professor Littlewood, who after making the aforementioned assertion that New Zealand was plainly a tax haven, made equally clear his view that whether New Zealand should continue to play this role was not a technical legal question, but a political one. In considering that political question, he notes that the effect of any change would be unlikely to lessen the amount of tax evasion in the world, as those using NZFTs for these purposes would simply move their legal structures elsewhere. This is something to ponder given the proposed changes discussed below.

The Inquiry’s Report evidently sought to balance the competing concerns about tax abuse and legitimate offshore planning business. It rejected the suggestion that they had no legitimate use and should be abolished by doing away with the present tax exemption. Based on submissions of New Zealand providers of foreign trust services, it observed that many offshore parties are compliant with their home jurisdiction’s tax rules, and argued that there is:

no reason to alter policy settings to make New Zealand less attractive. Doing so would seem inconsistent with the Government’s commitment to making New Zealand attractive for new investment and being globally recognised as a safe place to invest and undertake business, including financial services.

One way of interpreting the Report’s conclusions on the NZFT regime is that while it should continue to exist, New Zealand should deal with the consequences of that

52 Elliffe *International and Cross-Border Taxation in New Zealand*, above n 33, at 103, citing for the positive view the Ministry of Economic Development *Exporting Financial Services: A Report from the International Funds Services Development Group* (February 2011), and on the negative side a statement from Green Party leader Russel Norman from 2012.

53 Littlewood “Submission”, above n 49, at [14].

54 At [16].

55 *Inquiry Report* at [4.33].
taxation choice for our international partners and should no longer allow itself to be used as a tax haven for foreign tax residents: 56

New Zealand should not be or be seen as a country that effectively facilitates evasion through having disclosure and reporting requirements that are sufficiently weak to cause offshore parties to conclude that detection is highly improbable.

Thus, the Report ultimately concluded that the rules of the current regime "are not fit for purpose in the context of preserving New Zealand's reputation as a country that cooperates with other jurisdictions to counter money laundering and aggressive tax practices." 57 Based on a review of IR files, it was "reasonable to conclude" that NZFTs were being used to hide illicit wealth and to avoid or evade taxation in foreign jurisdictions. 58

But the Report was equally clear that changes to the NZFT regime as required a delicate balance: 59

Dealing with this issue requires a balancing of interests. On the one hand, there are offshore parties who want to use New Zealand as a genuine safe haven for the holding of family wealth. Their interest is consistent with government policy that encourages and welcomes offshore investment and a vibrant financial services sector. On the other hand, from both a global and local reputational and ethical perspective, New Zealand needs to protect against the risk of unwitting facilitation of money laundering, tax evasion and other illicit activities.

The Report's proposals seek to deter any exploitation of these 'tax haven' aspects of the NZFT, as well as combating any use that is being made for criminal or money laundering purposes, without taking away their use for legitimate wealth management purposes.

D Current Disclosure Requirements

In order to understand the way that the proposals do this, it is necessary to consider current disclosure requirements. In a nutshell, all that must be disclosed to the IR on the establishment of the trust is the name of the trust, the name and contact details of the New Zealand trustee, and whether the settlor of the trust is Australian. 60

We can get a sense of the adequacy of the current levels of disclosure that exist for

56 Inquiry Report at [4.34].
57 Inquiry Report at [1.2].
58 Inquiry Report at [1.6].
59 Inquiry Report at [10.8].
60 Tax Administration Act 1994, s 59B.
NZFTs by considering the way that they are promoted to clients, with one advertisement stating that "One of the principal benefits of New Zealand foreign trusts is the limited reporting requirements and compliance obligations". This is because, as Professor Littlewood argued, the disclosure regime as "almost completely useless" due to the lack of information gathered. Similarly, Professor Elliffe comments that:

The reality is that information held by the New Zealand Inland Revenue is unlikely to be specific enough to be helpful to a foreign revenue authority unless they already have a significant amount of information about their non-compliant taxpayer. … Countries outside of Australia may struggle to identify situations where the New Zealand foreign trust regime is being used by their residents because it is doubtful whether the New Zealand Inland Revenue would have access to the information to be able to appropriately respond to their query.

It is remarkable that these comments are directed towards disclosure and record-keeping requirements that were introduced in response to earlier criticisms of the inadequacy of disclosures concerning NZFTs. Prior to 2006, NZFTs were not required to provide any information to IR or to keep financial records for New Zealand tax purposes. IR itself identified problems in this situation, with a 2004 policy report stating that: "there is a risk that New Zealand may be unable to supply its double tax agreement (DTA) partners with information relating to certain foreign trusts if requested." Indeed, it was the concern of the Australian tax officials that NZFTs were causing problems for the collection of tax in that jurisdiction that was the catalyst for action on further disclosure. The existing disclosure requirements sought to remedy that situation.

In more detail, the current disclosure requirements are as follows. The existence of NZFTs must be disclosed to the IR by the resident foreign trustee according to s

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61 Inquiry Report at [6.21].
63 Littlewood "Submission", above n 49, at [20].
64 Elliffe International and Cross-Border Taxation in New Zealand, above n 33, at 148-149.
59B of the Tax Administration Act 1994. These requirements, which are set out in the IR disclosure form IR607, only require the name or identifying particulars of the trust, the name and contact details for the resident trustee, and any details concerning qualifying resident trustee status. There is also a yes/no option for disclosing whether the settlor is resident in Australia. This means that there need be no disclosure of the names, addresses, or tax residences of the foreign persons associated with the trust, such as the settlor, non-resident trustee, other controlling person, protector, or beneficiaries. Any changes to this information must be provided within 30 days.

The information that IR holds is not automatically shared with any foreign jurisdiction, with the exception of the information on the IR 607 form being provided to the Australian tax authorities if the form indicates there is an Australian settlor. The Report provides the interesting information that in the past seven years (presumably from around 2010-2016) there have been 142 exchanges of information with foreign tax authorities from 23 countries. This seems to refer only to IR providing information to foreign countries, with IR providing information spontaneously (after identifying a matter that may be of interest to a foreign tax authority) in the bulk of the cases (around 80%), with only around 20% being information requested by foreign tax authorities.

In addition to the disclosure requirements, there are more onerous record-keeping requirements under s 22 of the Tax Administration Act 1994. Information that must be recorded includes the trust deed and other trust documents, the amount and recipient of any distributions, and the name and address of settlors and any beneficiaries who have received a distribution. Accounts that are sufficient for the financial position of the trust to be determined must also be kept. The information provided on the form is not subject to any further check unless the person running the trust is audited by IR. If the foreign trust has been set up and run to plan, there is no tax payable in New Zealand and no need to file any annual tax return. The IR told the Inquiry that requests for such information from NZFTs were met without

68 Inland Revenue "IR607 Foreign Trust Disclosure Form" <www.ird.govt.nz>.
69 Inquiry Report at [6.1].
70 Tax Administration Act 1994, subss 59(2)-(6).
71 Inquiry Report at [6.14].
72 Section 22(7)(d).
73 Section 22(2).
74 Inquiry Report at [6.10].
75 Inquiry Report at [6.10]-[6.13].
difficulty and at generally the same standard for other business taxpayers. There are severe maximum punishments for intentionally breaching the disclosure or record-keeping obligations (up to 5 years imprisonment and/or a fine not exceeding $50,000), but IR reported that these have never been used in respect of NZFTs. If a trustee was convicted and there was no qualifying resident foreign trustee, then the trust would be subject to New Zealand tax on its worldwide income.

The Report’s conclusion about these current disclosure and record-keeping requirements is critical, characterising them as "very light-handed". In sum, it observed that "[a]s a practical matter, although quite extensive records are required to be maintained, very little information about foreign trusts is ever actually provided to IR or to any other government agency." From the perspective of preventing NZFTs being used to avoid or evade tax, most significant is that "[f]oreign tax authorities will typically not know to ask for information about a New Zealand foreign trust that has connections with their jurisdiction because they have no way of knowing that it exists." This was a major deficiency in the view of the Report, for it created the possibility for just the tax haven use that was alleged in the media:

This could lead some parties to take a calculated risk that not reporting income from a New Zealand foreign trust in the tax return in the country of residence of the person who has received it is highly unlikely to ever be detected. Similarly, an aggressive tax structure that results in capital that would otherwise be known to the home tax authority being housed in a New Zealand foreign trust is unlikely to be identified by the offshore tax authority.

As noted above, this is exactly the problem identified by academic tax commentators and media reports relating to the Panama Papers.

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76 Inquiry Report at [6.7].
77 Tax Administration Act 1994, s 143A.
78 Inquiry Report at [6.16].
80 Inquiry Report at [6.17].
81 Inquiry Report at [6.17].
82 Inquiry Report at [6.17].
83 Inquiry Report at [6.22].
THE REPORT'S PROPOSALS FOR ENHANCING DISCLOSURE AND THE GOVERNMENT'S RESPONSE

A The Identification of Enhanced Disclosure and Registration Requirements as the Solution

The Report's solution to the perceived problems with the NZFT are relatively simple: enhanced disclosure and record-keeping requirements, as well as a register that is searchable by the IR, Department of Internal Affairs ('DIA') and the Police's Financial Investigations Unit ('FIU'). This solution was widely promoted by academic commentators in the wake of the Panama Papers, with many tax experts suggesting that one way to deal with the perceived problem with NZFTs was increased disclosure. Professor Littlewood stated in a media interview that:84

The appropriate change would be to impose on all New Zealand resident trustees of foreign trusts the same obligations that currently apply in respect of where the settlor is Australian. In other words, adequate disclosure to the New Zealand IRD.

Deborah Russell similarly advocated disclosure as a solution:85

Up the disclosure requirements. Trustees should have to disclose the name of the trust, the names of the settlors, the value of the property held on trust, a description of the property held on trust, and the names of the beneficiaries. And this information should be made available to other tax regimes.

Anti-Money Laundering expert Ron Pol also argued that an appropriate response would be "a beneficial ownership and activities register accessible only by tax and enforcement authorities".86

It also emerged that this enhanced disclosure solution was supported by the majority of those submissions to the inquiry which were of the view that the current regime was inadequate.87 The major financial services provider KPMG was very supportive of further disclosures, stating that:88

84 Patrick O'Meara "Taxing foreign trust income could end industry – IRD" (7 April 2016) Radio New Zealand <www.radionz.co.nz>.
85 Deborah Russell "What's going on with foreign trusts?" (4 April 2016) Left Side Story <deborahfrussell.net>.
86 Ron Pol "Ron Pol says 'tax haven' misses the point: New Zealand's reputation offers a competitive advantage, and opportunity" (11 April 2016) Interest.co.nz <www.interest.co.nz>.
87 A number of submissions simply stated their support for Deborah Russell's submission: Jeremy Bowen, Denise Cavanaugh, and Dale Williams and John Clarke.
88 KPMG "New Zealand foreign trust review response" (23 May 2016) <www.treasury.govt.nz>. 
An arrangement should not rely on non-disclosure of its existence for its effectiveness. The effectiveness of an arrangement should rely on the application of the law to the facts and circumstances of the arrangement. We believe that:

- Disclosure to a Revenue Authority of the existence of arrangement is a natural consequence of that position.
- A user of an arrangement should not have a tax-effectiveness concern from disclosure but may have other concerns.

However there was resistance from some NZFT providers to the suggestion that a publically accessible register of trusts be created. There have been calls from ‘tax justice’ lobby groups for registers of beneficial ownership or significant control of trusts and companies to be made public, as has recently occurred in the UK with respect to companies (but not trusts) and in France in respect of trusts.\(^{89}\) It is clear that the balance between privacy of individuals’ financial arrangements and the desire to root out tax avoidance and evasion is shifting – but there is a legitimate question as to how far towards transparency is consistent with rights to privacy of one's financial affairs,\(^{90}\) and none of the submissions to the Inquiry advocated such a step.\(^{91}\) In addition there is the economic argument: the STEP submission made clear its view that a public register would effectively shut down the NZFT industry:\(^{92}\)

if there is an over-reaction to the push for greater disclosure in relation to foreign trusts (at its extreme, the (frankly) offensive suggestion that there should be publicly searchable registers identifying persons associated with these trusts and their investments), then there is nothing more certain than there will be a total loss of business. Clients will simply move to other jurisdictions which have a more coherent and balanced approach to personal privacy issues and a facility for exchange of tax information through proper and secure channels.

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\(^{89}\) For the UK significant control register, see Small Business, Enterprise and Employment Act 2016 (UK), discussed at Companies House "Keeping your people with significant control (PSC) register" (6 April 2016) <www.gov.uk>. See also Anthony Turner and Tim Follett "Tangled Up in Chains: Making Sense of the new UK Requirement to Keep Registers of 'People With Significant Control" (2016) 22 Trusts and Trustees 537. For the French trusts register, see Government of France "Creation of a French public register of trusts" (12 May 2016) <www.gouvernement.fr>.

\(^{90}\) See for example Filippo Noseda "Caught in the Crossfire Between Privacy and Transparency" (2016) 22 Trusts & Trustees 599.

\(^{91}\) However see the advocacy for public registers of trusts by the Tax Justice Network "Automatic Information Exchange is not the Answer" (28 May 2016) <www.taxjustice.net> and the Financial Transparency Coalition "Beneficial Ownership" <financialtransparency.org>.

\(^{92}\) STEP submission, above n 43, at 14.
This concern for financial privacy and the possible threat to the NZFT industry is a view that has been put forward by New Zealand providers for many years. It is mentioned in the file note 'Background to 2006 foreign trust information disclosure reform', which observes that a previous (2004) file note "states that submitters were concerned that requiring a New Zealand resident trustee to provide the name and contact details for the settlor would destroy the trust industry, due to privacy concerns" with the effect that "[t]rusts would simply relocate to jurisdictions with no reporting requirements".93 A summary of the submissions to IR on the 2004 proposals for greater disclosure and record-keeping requirements shows that all 17 submissions opposed this.94 Yet viewed from today's context, these trust provider arguments show how much the environment has shifted: now the Report’s proposals for increased disclosure and record-keeping are accepted (perhaps as inevitable, post-Panama Papers), and what is resisted is the further step of public access to trust information.

B No Solution in the Automatic Exchange of Tax Information and Anti-Money Laundering Regimes

The Report noted that some of the submissions had suggested that the new international regime for the automatic exchange of tax information may provide a solution for the problems of disclosure identified in the current NZFT regime.95 This is a new multilateral regime, created under the auspices of the OECD and to come into practical effect in 2017 and 2018, requires financial institutions to pass information about foreign account holders and controlling persons to the tax authorities of the jurisdiction in which the financial institution is doing business; the tax authorities will then automatically exchange this information with the identified foreign jurisdiction's tax authorities. As noted below, this represents a fundamental shift in international tax cooperation. However, the Report concluded that these automatic exchange obligations would not require New Zealand financial institutions or trust providers to collect and provide information about NZFTs to foreign jurisdictions.96

93 "Background to 2006 foreign trust information disclosure reform" <www.treasury.govt.nz>.
95 Inquiry Report at [6.27]. See the discussion below at Section IV:A.
96 Inquiry Report at [6.29]. Some submissions (from the New Zealand Law Society and TGT Legal) had argued that the AEOI requirements would include the trustees of foreign trusts as financial institutions and therefore make them subject to reporting requirements: <www.treasury.govt.nz>.
The Report's view is consistent with the IR's interpretation of the Common Reporting Standard ('CRS'), in light of its text and the associated OECD commentary.\textsuperscript{97} NZFTs are not likely to be required to pass on information to the IR under the CRS because the obligation to collect and exchange information falls primarily on the foreign Financial Institution ('FI') which holds the trust's asset, which the tax authority will then forward to foreign jurisdictions.\textsuperscript{98} Financial institutions located in jurisdictions participating in the automatic sharing regime must carry out due diligence on their account holders in order to identify whether they or any controlling person is a foreign tax resident (these are 'reportable persons' under the CRS).\textsuperscript{99}

The Report agreed with the IR view that NZFTs will usually not themselves be FIs, which means that they are not required to comply with the CRS obligations.\textsuperscript{100} This is because NZFTs usually do not fall within the definition of FIs, which includes institutions that primarily carry on the business of managing investments for customers, or of taking deposits as a custodian institution.\textsuperscript{101} Further, New Zealand-based FIs will usually not hold any assets for a NZFT, because this would likely generate New Zealand-sourced income subject to New Zealand taxation. If the NZFT did hold an account with a New Zealand FI, it is likely that the trust would fall under the 'passive non-financial entities' definition and the NZ FI would have to carry out due diligence and reporting.\textsuperscript{102} Unless the NZFT or another FI is required to report under the CRS, the only possible obligation for the NZFT's information to be reported is if it holds an asset at a FI in another jurisdiction that has implemented AEIO.\textsuperscript{103}

Further, the Report observed that the ongoing international efforts to constrain money laundering that are currently still being implemented in New Zealand were also not seen as a solution to the perceived problems of NZFTs.\textsuperscript{104}

\begin{itemize}
\item \textsuperscript{98} *Inquiry Report* at [6.31].
\item \textsuperscript{99} *Inquiry Report* at [6.31].
\item \textsuperscript{100} *Inquiry Report* at [6.33].
\item \textsuperscript{102} *Inquiry Report* at [6.34].
\item \textsuperscript{103} *Inquiry Report* at Appendix 5, at [12].
\item \textsuperscript{104} *Inquiry Report* at Part 7.
\end{itemize}
laundering ('AML') measures require FIs to detect illicit funds through customer due diligence ('know your customer') requirements; these include obligations to verify the identity of account holders and controlling persons, to determine the source of the funds involved, and to report any suspicious transactions.105 New Zealand is part of the Financial Action Task Force ('FATF') which has made Recommendations that constitute the main international standards on AML,106 with domestic implementation in New Zealand through the Anti-Money Laundering and Countering of Financing of Terrorism Act 2009.

Under these obligations, FIs must undertake due diligence on customers and their funds, and report suspicious transactions. According to the risk-based approach, trusts are seen as higher risk and are subject to enhanced due diligence requirements that require the identity or class of beneficiaries to be identified, the source of the funds (including verification if risk warrants this), and whether any customer or beneficial owner is a politically exposed person.107 The definition of 'beneficial owner' is the "individual who has effective control of a customer or person on whose behalf a transaction is conducted".108 As explained by the Department of Internal Affairs, which has released a fact sheet on the AML legislation, a person with beneficial ownership of a trust "may include the trustees and any other individual who has effective control over the trust, specific trust property, or with the power to amend the trust's deeds, or remove or appoint trustees".109 Due to its complexity, the Report argued that the guidance on this concept should be expanded,110 and it also observed that the 'source of funds' obligations were not adequate to prevent illicit funds finding their way into NZFTs.111 Unless the FI does identify something suspicious it does not need to pass the information it gathers on to a government agency.112 Furthermore, lawyers and accountants who do not fit the definition of

105 See Department of Internal Affairs "Services - Anti-Money Laundering and Countering Financing of Terrorism" <www.dia.govt.nz>.
107 Anti-Money Laundering and Countering Financing of Terrorism Act 2009, s 22(1)(a) discussed in Inquiry Report at [7.5].
108 Anti-Money Laundering and Countering Financing of Terrorism Act 2009, s 5.
109 Department of Internal Affairs "Beneficial Ownership Guideline" <www.dia.govt.nz>; and see also Inquiry Report at [7.7].
110 Inquiry Report at [7.10].
111 Inquiry Report at [7.15]-[7.16].
112 Inquiry Report at [7.4].
IMPLICATIONS OF THE PANAMA PAPERS FOR THE NZ FOREIGN TRUSTS REGIME

'trust and company service provider' are currently not subject to the AML obligations.\textsuperscript{113}

\textbf{V THE REPORT'S RECOMMENDATIONS AND THE GOVERNMENT'S RESPONSES}

The key changes that the Report recommends are found in Part 12. The Government quickly stated that it would adopt all of the Report's recommendations.\textsuperscript{114} They are to be implemented primarily through a Tax Bill; this has now been introduced as the Taxation (Business Tax, Exchange of Information, and Remedial Matters) Bill. The Inquiry's recommendations, and the Government's implementation of them (and the changes it made) can be summarised as follows.

\textbf{A Establish a Formal Register of Foreign Trusts and Information on Persons Involved with the Trust}

The Inquiry recommended that a formal register of foreign trusts – searchable by regulatory agencies – be established. This is implemented by cl 10 of the Bill, amending the Tax Administration Act 1994. The Government response indicated that the other governmental agencies who may search the NZFT would be limited to the DIA and the Police; IR would administer the register.\textsuperscript{115} The Government specified that the registration fee will be $270 and the annual filing fee $50, which reflects the calculated cost of administering the new regime. This may be modified by Order in Council if costs change.\textsuperscript{116}

In terms of information to be disclosed and registered, the Inquiry recommended that the register should contain the trust deed itself, along with the name, email, residential address, country of tax residence and Tax Information Number of all of the parties involved in the trust, including the settlor, beneficiaries and any other person with effective control over it.\textsuperscript{117} This package of information disclosure was

\begin{itemize}
  \item \textsuperscript{113} Inquiry Report at [7.5].
  \item \textsuperscript{114} English and Woodhouse "Government's Response", above n 4.
  \item \textsuperscript{115} Taxation (Business Tax, Exchange of Information, and Remedial Matters) Bill 2016 (149-1), cl 11, amending s 81 of the Tax Administration Act 1994 to allow the communication of foreign trust information from the IRD to members of the Police and officers, employees or agents of the Department of Internal Affairs.
  \item \textsuperscript{116} Taxation (Business Tax, Exchange of Information, and Remedial Matters) Bill 2016 (149—1), cl 10, creating s 59E.
  \item \textsuperscript{117} Inquiry Report at Part 12.
\end{itemize}
accepted by the Government, and the increased information disclosure is achieved through cl 10 of the Bill, replacing s 59B of the Tax Administration Act.\textsuperscript{118}

However, in the Bill the concepts of 'protector' and 'natural person with effective control' identified by the Inquiry Report's recommendation have been translated into "person with a power under the trust deed to control the dismissal or appointment of a trustee, to amend the trust deed, or to add or remove a beneficiary" and "person with a power under the trust deed to control a trustee in the administration of the trust".\textsuperscript{119} Given that financial service providers will be inquiring into the owners of their accounts according to these terms to comply with AML and tax information exchange measures, it is not clear that trust providers should not be required to apply this concept for NZFT registration purposes. The effective control test must be applied by financial service providers in the context of AML measures under the Anti-Money Laundering and Countering Financing of Terrorism Act 2009,\textsuperscript{120} as the Inquiry Report details.\textsuperscript{121} It is also a crucial part of the CRS, which is the centrepiece of the new tax information exchange regime discussed above: 'controlling persons' that must be reported include any natural persons "exercising ultimate effective control over the trust (including through a chain of control or ownership)".\textsuperscript{122}

While the concepts found in the Bill are more legally precise and therefore simpler to apply, they may be narrower than the concept of "effective control" found in the wider regulatory frameworks. It might be said that someone who has the right to revoke the trust or to distribute trust property, or someone who does not even have any of these powers but who in reality is in control of the trust, should be identified and their information provided and registered. They may have been caught by the effective control provision, depending on how that concept is interpreted. In addition, the concept of effective control "through a chain of control or ownership" found in the Inquiry's recommendations is not found in the disclosure requirements of the Bill. This concept requires that the natural persons who have control over

\textsuperscript{118} Taxation (Business Tax, Exchange of Information, and Remedial Matters) Bill 2016 (149—1), cl 10, replacing s 59B

\textsuperscript{119} Taxation (Business Tax, Exchange of Information, and Remedial Matters) Bill 2016 (149—1), cl 10.

\textsuperscript{120} Anti-Money Laundering and Countering Financing of Terrorism Act 2009, ss 11, 16, 18, and 26, referring to 'beneficial owner' – which is defined in s 5 as "has effective control of a customer or person on whose behalf a transaction is conducted". See the Department of Internal Affairs "Beneficial Ownership Guideline", above n 109.

\textsuperscript{121} Inquiry Report at [7.6]-[7.10] and [7.29] and Appendix 6.

assets through complex layers of companies and trusts be identified. The reason for this change is not explained in the introductory material to the Bill.

From another perspective, it might be said that the concepts in the NZFT registration regime might include persons who are not identified as falling within the AML and tax exchange regime's definition of effective control. This is again because of the particular powers identified not being equivalent to that concept.

Further analysis beyond the scope of this article is necessary to fully understand the differences in the Report and the Bill's requirements for those persons for whom information must be reported. It not clear that this change significantly weakens the information disclosure requirements – particularly when the NZFT disclosure rules are placed alongside the AML and tax exchange requirements – but the choice not to implement the Report recommendations' wording should have been explained and justified.

B Annual Return to be Filed and Alterations to Trust Information Disclosed

In addition to the initial registration of the NZFT, the Report recommended that the filing of an annual return should be required, including any changes to the information provided on registration, financial statements, and the amount and identification details relating to any distributions of trust property to beneficiaries. The Government accepted this, and added that any new settlements of property on the trust must be reported along with the identifying particulars of the settlor. This might have been implicit in the requirement to provide in the annual return information on any changes to the information about the trust provided at the time it was initially registered, but it is useful to make clear that this new information must be provided.

In addition to the initial disclosure and annual return requirements, there is also an obligation for a resident trustee to "provide to the Commissioner the details of an alteration to a particular" of the foreign trust information that has been disclosed. This must be provided within 30 days of the trustee becoming aware of the alteration. As with the initial disclosure, there will be a grace period from the

123 See Department of Internal Affairs "Beneficial Ownership Guideline", above n 109, at [14]-[24].
125 Taxation (Business Tax, Exchange of Information, and Remedial Matters) Bill 2016 (149—1), cl 10, replacing s 59B(5).
126 Clause 10, replacing s 59C(2).
registration and disclosure requirement for trustees who are new migrant individuals and are not providers of trust services.127

C Stricter Sanction of Losing Tax Exemption in Cases of Non-Disclosure

The Report recommended that the tax consequences for non-compliance with registration and disclosure requirements should be reviewed with an eye to strengthening them. At present, a NZFT that has a qualifying resident foreign trustee128 will never be liable for tax due to non-compliance.129 Even if this safe-harbour from the sanction does not apply, there must be a conviction of the trustee for knowingly failing to keep or supply information before the tax exemption is lost.130 While the Inquiry's formal recommendation was only for a review of these issues, it stated its view:131

that the exemption foreign trusts enjoy from New Zealand tax on foreign source income should apply only where the registration and associated disclosure obligations at that time have been complied with.

The Government responded not with a review, but by agreeing with the Report's view that the tax exemption only apply where a trust has complied with registration and disclosure requirements. It stated that the appropriateness of this safe-harbour for qualifying resident foreign trustees had already been reviewed, and that the Government agreed that it should be removed.132 The change is realized in cl 5 of the Bill.133 This is obviously a more proactive move than the Report's recommendation. The Government slightly modified the substance of the Report's proposal, by not applying the taxation sanction to situations where "the non-registration or lack of disclosure was unintentional and remedied immediately".

127 Clause 10, replacing s 59C(3).
128 This concept is defined in the Tax Administration Act 1994, s 3(1).
129 Income Tax Act 2007, s HC 26(3).
130 Income Tax Act 2007, s HC 26(3). See also Inquiry Report at [6.18]
131 Inquiry Report at [6.18].
**D Expedited Inclusion of Lawyers, Accountants and Real Estate Agents in AML Regime, and Other Changes to AML Requirements**

In the Report's recommendation, the exclusion of lawyers and accountants from the AML reporting requirements should be removed sooner than the current plans for this to occur in late 2017.\(^{134}\) This was not accepted by the Government, which argued that the application of the AML regime to lawyers and accountants will be progressed as soon as practicable, but that this will remain within the Government's planned development of phase II of the AML reforms. This is due to "issues surrounding legal privilege and regime supervision that can only be dealt with through primary legislation and not regulation". However, the planned timeframe has been expedited, with legislation expected to be passed in the first half of 2017. It is nevertheless still not clear that the application of AML to lawyers and accountants will come into practical effect before the "end of 2017 or later" timeframe that the Report thought was inadequate.

The Report's further recommendations in respect of AML were that assets placed in a NZFT should automatically be subject to verification requirements for their source,\(^{135}\) and further guidelines should be put in place to explain the customer due diligence requirements for verifying beneficial ownership.\(^{136}\) Further, suspicious transaction obligations should be changed to ensure that they apply to transactions even where they do not relate to accounts held at a New Zealand bank.\(^{137}\) The Government agreed and stated that these recommendations would also be dealt with as part of the Phase II AML reforms.

**E Other Key Recommendations**

The Report also recommended that a review should be undertaken of the sharing of trust information between the regulatory agencies with supervisory responsibilities over trust disclosures, in order to "determine the financial and efficiency gains and other implications (including secrecy considerations) of sharing strategic intelligence and other information between agencies".\(^{138}\) In response the Government indicated that that in the review of how NZFT information is shared between regulatory agencies, it may be appropriate to review the role of other agencies (in addition to the IR, the DIA, and the Police FIU). The timing of the

\[^{134}\text{Inquiry Report at [12.15].}\]
\[^{135}\text{Inquiry Report at [12.16].}\]
\[^{136}\text{Inquiry Report at [12.17].}\]
\[^{137}\text{Inquiry Report at [12.18].}\]
\[^{138}\text{Inquiry Report at [12.20].}\]
review is stated as "after the initial changes to the disclosure rules have bedded in and possibly coincide with phase 2 of the AML regime reform of tax secrecy rules".

F Conclusions

With the Government accepting the recommendations of the Inquiry Report, it is clear that there will be significant changes to the transparency of the ownership and control of NZFTs. Despite the narrowing of the identification of beneficial ownership noted above, the Government's implementation of the Inquiry's proposals will likely be satisfactory for those who believed that the Inquiry had found good solutions to the problems in the NZFT regime. At the time of writing, the legislation implementing the changes has begun the passage through the New Zealand Parliament and may yet change; it is only once it has been further debated and passed into law that it will be finally possible to assess its likely effects. But at this stage, the proposed changes should go far in cleaning up the illegitimate use of the NZFT identified by the media and the Inquiry.

VI THE PROPOSALS IN THE WIDER INTERNATIONAL CONTEXT

A International Tax Information Sharing Developments

It is worth briefly noting that this inquiry into the New Zealand offshore financial regime and the proposals for increased disclosure of information about foreign trusts falls within a wider recent shift to much greater transparency in offshore trusts, companies, and bank accounts. In the last 15 years, major international legal developments have been developed to address corruption, money laundering and tax avoidance and evasion, with the G20 leaders stating in 2009 that "the era of banking secrecy is over".139 These developments have been intensifying, and to some degree been a response to the ICIJ's previous investigations of leaked information about the offshore financial industry, which have clearly upped the political ante. It might be said that 21st century international tax policy and law is now beginning to catch up with the development of offshore financial structures over the 20th century, in order to counteract their adverse effects.

These transparency developments are evident in New Zealand's ongoing domestic implementation of international AML standards developed by the Financial Action Task Force, which seek to control the flow of illicit wealth by

identifying those who own or control financial assets, and assessing the legitimacy of the sources of that wealth.\textsuperscript{140}

But perhaps the more radical development is the current implementation of international obligations on tax authorities to automatically share tax information concerning foreign accounts and entities – the Automatic Exchange of (tax) Information (‘AEOI’). It is radical because for many years international legal obligations on the exchange of tax information were usually limited to an 'on request' model – this is the exchange obligation found in most bilateral tax agreements.\textsuperscript{141} Under these obligations, tax information and records about accounts or entities with a link to foreign nationals is required to be exchanged, but only if the foreign jurisdiction makes a specific request about a taxpayer, and so long as the information requested is relevant to an ongoing investigation.\textsuperscript{142} These measures are often criticised as ineffective for, as the Report observes, foreign jurisdictions usually do not know that the offshore structure such as a NZFT exists.\textsuperscript{143}

This is the problem that the new AEOI regime seeks to deal with. Many jurisdictions have now signed up to international obligations under the Convention on Mutual Administrative Assistance on Tax Matters, to automatically collect and exchange tax information with each other – relating to financial accounts that are owned or controlled by each other’s tax residents. To facilitate AEOI, the OECD has provided a Common Reporting Standard (CRS) specifying requirements for the scope of accounts and information to be reported, for due diligence in the identification of foreign accounts, and a uniform format for exchange.\textsuperscript{144} Because vast amounts of data that will be transmitted, the automatic sharing framework also includes obligations on confidentiality and electronic security requirements in the


\textsuperscript{142} See for example see the Double Taxation agreement between New Zealand and the United Kingdom: Convention between the Government of New Zealand and the Government of the United Kingdom of Great Britain and Northern Ireland for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and capital gains. For discussion of how these rules usually work, see Tom Lowe QC "Cross-Border Tax Investigations and the OECD’s Tax Information Exchange Regime" (2015) 21 Trusts and Trustees 1012; Antoine Confidentiality in Offshore Financial Law, above n 141, at 362-383 and Antoine Offshore Financial Law, above n 51, at ch 18 generally.

\textsuperscript{143} Inquiry Report at [6.17].

receiving country.\textsuperscript{145} AEOI does promise to identify accounts that foreign taxpayers have not declared to their home jurisdiction - and which the foreign tax authority may not know about – and it is this that promises to uncover or deter evasion.

These AEOI practices will be put into effect during 2017 and 2018. A fact sheet released by IR outlines the plan for implementing the regime in New Zealand.\textsuperscript{146} The legislation implementing the CRS is the same Bill that makes the aforementioned changes to the foreign trust regime,\textsuperscript{147} and IR will exchange information with other reportable jurisdictions by 30 September 2018 at the latest.

What we have seen in the last 15 years is, to quote the title of an article examining it, the "The amazing development of exchange of information in tax matters".\textsuperscript{148} This level of international cooperation on tax can be characterised as radical if compared with an older model whereby states declined to enforce the tax obligations levied by another state.\textsuperscript{149} Professor Antoine argued as recently as March 2014, commenting on the proliferation of Tax Information Exchange Agreements (TIEAs) between 'tax havens' and OECD countries, that:\textsuperscript{150}

[t]he movement toward increased cooperation in tax matter is, of course, a significant paradigm shift for offshore states. Nonetheless, the recent thrusts toward more transparency, and the advanced policy commitments given by offshore countries promising to facilitate information requests on tax matters, should be placed into context. They should not be interpreted as carte blanche licences for automatic disclosure. Rather, confidentiality remains an important, though increasingly unobtainable ethic in offshore jurisdictions. Moreover, important principles limiting disclosure, such as the rules on fishing, legal privilege, foreseeable relevance, favourable interpretations of beneficial ownership, and the like, remain entrenched in law and treaty interpretation.

\textsuperscript{145} OECD The CRS Implementation Handbook <www.oecd.org>, at [70]-[76]; IRD "Implementing the global standard on automatic exchange of information: an officials' issue paper" (February 2016) <taxpolicy.ird.govt.nz>, at [1.18]-[1.20].

\textsuperscript{146} Inland Revenue "Automatic Exchange of Financial Account Information for financial institutions" (July 2016) <taxpolicy.ird.govt.nz>.

\textsuperscript{147} Taxation (Business Tax, Exchange of Information, and Remedial Matters) Bill 2016 (149—1), cls 12-26.

\textsuperscript{148} Henry Christensen III and Jean-Marc Tirard "The amazing development of exchange of information in tax matters: from double tax treaties to FATCA and the CRS" (2016) 22 Trusts and Trustees 898.

\textsuperscript{149} Antoine Offshore Financial Law, above n 51, at ch 17.

\textsuperscript{150} Antoine Confidentiality in Offshore Financial Law, above n 141, at 382.
The automatic exchange of tax information under the CRS represents a fundamental break with this old model. AEOI is a kind of fishing expedition, whereby the home jurisdiction's tax authorities are provided with names and tax information numbers of its tax residents who have a connection to accounts or legal entities in other jurisdictions without there being any investigation related to the tax resident. On this basis, the home tax authorities may open an investigation and thereby can use the old model obligations to request the records and documents relevant to the investigation.\textsuperscript{151}

B A Lacuna of Information Sharing in the Inquiry's Proposals?

In light of this wider international background of a shift to AEOI, it may seem unclear why the Report's proposals for NZFTs do not see IR automatically providing the information it will receive to the jurisdictions of tax residence of the trust's settlor, beneficiaries, trustee, or other persons holding key powers over trust decisions. This may seem a lacuna in the proposals. Indeed, remember that the IR has analysed the CRS system as likely not requiring it to automatically pass on the information gathered pursuant to the proposed disclosure requirements to foreign jurisdictions. This is because most NZFTs will not fall within the definition of financial institutions for the reasons noted above.

So at the point that the trust is established and registered, the foreign country will still not know of its existence. The Report's proposed changes do nothing to alter this. No more information will be passed to the tax authorities in the jurisdiction in which the parties associated with the trust are tax residents.

There have been some criticisms of the Report's proposals on this basis. Journalists Gareth Vaughan, Denise McNabb and Richard Smith, who provided a significant amount of the New Zealand media commentary on the Panama Papers, updated an article on NZFTs to take into account the Report's proposals. They questioned whether the perceived problem with NZFTs – that foreign tax residents may be able to use them for tax evasion or avoidance purposes – given that the proposals do not result in the foreign jurisdiction whose tax residents have an association with the NZFT knowing this fact.\textsuperscript{152} They point to developments in the European Union relating to the possible identification and blacklisting of tax

\textsuperscript{151} Lowe, above n 142, at 1017.

development which identify the lack of automatic provision of information about trusts and the lack of a public register as problematic features of offshore financial law.\textsuperscript{154} From this perspective, not providing for some kind of automatic reporting of the existence of the NZFT to the home jurisdiction of the settlor – as already exists for Australian settlors – seems to be a failure to take a simple and rational step to more effectively prevent the use of the regime for tax evasion or avoidance purposes.

However, there are reasonable responses that may be made to such criticisms. As the Report makes clear, the enhanced disclosure requirements it recommends for NZFTs sit within a wider framework of measures to tackle money laundering and harmful tax practices. Although the IR will not automatically share the information that it receives through the proposed changes with other jurisdictions' tax authorities, there are mechanisms for this to occur.

One option would be for the IR to disclose suspicious trust structures to home jurisdictions spontaneously – without request from the home jurisdiction. As mentioned above, this is (by volume) the main way currently that information about NZFTs is being provided to foreign tax authorities. According to many of New Zealand's double taxation agreements, New Zealand must provide such information where it is foreseeably relevant for the enforcement of the other state's tax law.\textsuperscript{155} It seems likely that the fuller information provided to the IR will reveal more of the kinds of trust structures that IR is already reporting spontaneously to foreign tax authorities.

The other way that the information concerning the NZFT may be made available to foreign tax authorities is through the international AEIO regime; the offshore financial institution that holds the assets of the foreign trust is likely to be located in a country that has undertaken AE obligations. If so, the account and personal information relating to all the parties involved in the trust must be acquired and reported to their home jurisdiction. Then, on the basis of gaining information that its tax residents have some involvement with the NZ foreign trust, if there is an on request obligation in place, the home jurisdiction may make a request for NZ to acquire and provide more detailed information about the NZ trust to help with the

\textsuperscript{153} European Parliament News "MEPs call for tax haven blacklist, patent box rules, CCCTB and more" (6 July 2016) <www.europarl.europa.eu>.

\textsuperscript{154} Vaughan et al "New Zealand Foreign Trusts", above n 152.

\textsuperscript{155} For example, Convention between the Government of New Zealand and the Government of the United Kingdom of Great Britain and Northern Ireland for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and capital gains, Article 25.
home jurisdiction's investigations. The disclosure requirements recommended by the Report will be a good foundation for the provision of this information.

As is inevitable, there may be loopholes to exploit. The new information requirements depend on the information gathered and verified by the trustee, and there may be ways for the unscrupulous to hide their interests in the NZFT behind undeclared nominees. There is also the possibility that jurisdictional arbitrage may occur, with the assets of the NZFT being deliberately placed in jurisdictions that are not participating in the AEIO regime, or which have not agreed to provide information to the jurisdiction where the parties to the trust are resident. Or it may be that, as the submission of TGT Legal pointed out, that the parties to a trust are not resident in a jurisdiction that is participating in the AEOI regime. In such cases, the information about the existence of a NZFT that the home jurisdiction's tax residents have some relationship to will not be disclosed to those authorities. In such cases the NZFT will retain its status as an entity which provides a degree of secrecy from an individual's home tax authorities. However, with the continuing shift to transparency, it seems foolhardy to set up trusts for the reason of tax evasion or avoidance – at least if this requires a relatively long-term structure – because of the risk that holdouts against the AEOI regime will cave to international pressures or that the home jurisdiction may agree to further information-sharing with New Zealand, at which point the spontaneous sharing of the information held by IR seems likely.

**VII CONCLUSION**

While not extending as far as jurisdictions that have opted for complete transparency for trusts, the Inquiry Report's recommendations for reforming NZFTs strike a far more appropriate balance between financial privacy and transparency than the current rules do. The Government has committed to implementing these recommendations, with the legislative changes impending. These changes will go far in getting New Zealand the clean foreign trusts industry that it portrays to the world, and to dispel the charges of 'tax haven New Zealand'. However, we should not rest on our laurels, as there will always be ways of exploiting legal forms for illegal or illegitimate purposes.

Without the Panama Papers, the Inquiry would not have happened, and the status quo would have likely continued. There should be a more proactive effort to identify aspects of the law that should be reformed, without having to wait for major scandals to occur. This may apply to other areas of New Zealand law too - for example, there has been local coverage of New Zealand-registered financial service providers that

156 TGT Submission, above n 45, at [3.6].
are being used for illegitimate purposes,¹⁵⁷ with Gareth Vaughan's Panama Papers stories focussing on this issue as much as they did on trusts.¹⁵⁸ Of course, the landscape has now changed, and the Government will be more sensitive to these kinds of perceived problems in New Zealand law and regulation. There are promising movements on the financial service provider issue as well,¹⁵⁹ despite it not commanding anywhere the airtime that the NZFT regime did. More significantly, it seems that the wider international concern about money laundering and tax avoidance and evasion will see developments that force action at the domestic level in New Zealand. Money laundering, harmful tax practices and fraud may always be with us, but scandals caused by major leaks of information may be bringing us into a new era of regulatory strategies to clamp down on such activities.

¹⁵⁷ Gareth Vaughan “Why the Financial Service Providers Register brings NZ’s reputation into disrepute and how the Government should change it” (25 July 2015) Interest.co.nz <www.interest.co.nz>; Gareth Vaughan "Standard Capital PB, PB Standard Capital, a NZ financial service provider, an ‘undisputed US$1 mln debt’ and the man who wants it back” (11 July 2016) Interest.co.nz <www.interest.co.nz>.

¹⁵⁸ Gareth Vaughan "The global footprint of shonky NZ companies, trusts, financial service providers and building societies” (22 June 2016) Interest.co.nz <www.interest.co.nz>.

¹⁵⁹ Gareth Vaughan "Commerce Minister Paul Goldsmith says Financial Service Providers Register to stay, but those on it must have a ‘strong connection’ to New Zealand” (13 July 2016) Interest.co.nz <www.interest.co.nz>.