International treaty examination of the Agreement between the Government of New Zealand and the Government of the Commonwealth of The Bahamas on the Exchange of Information with Respect to Taxes

Report of the Finance and Expenditure Committee

Contents

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Recommendation

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

The Finance and Expenditure Committee has conducted an international treaty examination of the Agreement between the Government of New Zealand and the Government of the Commonwealth of The Bahamas on the Exchange of Information with Respect to Taxes and has no matters to bring to the attention of the House.

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

Appendix A

Committee procedure

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

Committee members

Craig Foss (Chairperson)
Amy Adams
David Bennett
John Boscawen
Brendon Burns
Hon David Cunliffe
Aaron Gilmore
Raymond Huo
Rahui Katene
Peseta Sam Lotu-Iiga
Stuart Nash
Dr Russel Norman

Appendix B

Agreement between the Government of New Zealand and the Government of the Commonwealth of The Bahamas on the Exchange of Information with Respect to Taxes

National Interest Analysis

Executive Summary

1 On 18 November 2009 New Zealand signed The Agreement Between The Government Of New Zealand And The Government Of The Commonwealth Of The Bahamas On The Exchange Of Information Relating To Taxes ("the TIEA").

2 The TIEA establishes a mechanism by which tax officials from New Zealand and the Bahamas ("the Parties") can request information from each other (such as business books and accounts, bank information, and information on the ownership of legal entities) for the purpose of detecting and preventing tax avoidance and evasion. Access to this previously unobtainable information will enhance Inland Revenue's ability to detect and prevent tax avoidance and tax evasion. Any reduction in tax avoidance or tax evasion will be beneficial to New Zealand in financial, fiscal and economic terms. New Zealand already has a network of 35 double tax agreements ("DTAs") in place with key trading and investment partners which provide for exchange of information arrangements similar to those which are established under the TIEA. TIEAs are designed to be used to establish exchange of information arrangements with jurisdictions where DTAs may not be appropriate, such as with low-tax jurisdictions. The Bahamas is a low-tax jurisdiction, and is also an important international finance centre. New Zealand, to date, has signed a number of other TIEAs – with the Netherlands Antilles, in 2007, and with Bermuda, the British Virgin Islands, the Cayman Islands, the Cook Islands, Gibraltar, Guernsey, the Isle of Man and Jersey this year.

3 The TIEA is based on a model produced in 2002 by the Organisation for Economic Cooperation and Development ("the OECD"). The TIEA provides a comprehensive set of rules that support the exchange of information. These rules ensure that requested information will be obtained and provided in a timely and effective manner. However, the rules also ensure that information may not be requested or used indiscriminately. Information requests may only be made in prescribed circumstances, and information received pursuant to a request may only be disclosed to authorised persons and used by those persons for authorised purposes (principally, the administration and enforcement of the domestic tax laws of the respective Party.) The text of the TIEA is attached as Annex A.

Date and nature of proposed binding treaty action

4 It is proposed that the TIEA be brought into force for New Zealand following completion of the Parliamentary treaty examination process in accordance with Standing Orders 388 to 391.

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

6 Upon the promulgation of the Orders in Council, the TIEA can then be brought into force, in accordance with Article 14 of the TIEA through an exchange of diplomatic notes that confirms the completion of the respective constitutional and legal requirements for entry into force of the TIEA by each Party.

Reasons for New Zealand becoming taking the treaty action

7 New Zealand domestic law specifically prohibits Inland Revenue from divulging information it holds to foreign jurisdictions, except when authorised by a tax treaty.[2] Other countries generally follow the same principle. Therefore, to assist in the detection and prevention of tax avoidance and tax evasion, most developed countries are building networks of treaties that allow for the exchange of information on tax matters.

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

9 New Zealand signed its first TIEA, with the Netherlands Antilles, on 1 March 2007. A second TIEA, with Bermuda, was signed on 16 April 2009. TIEAs have since been signed with the British Virgin Islands, the Cayman Islands, the Cook Islands, Gibraltar, Guernsey, the Isle of Man and Jersey. Each new TIEA concluded further expands New Zealand's network of exchange of information arrangements and reduces the tax evasion and avoidance options available to New Zealand residents.

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

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

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

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

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

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

Consideration of other options

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

Advantages and disadvantages to New Zealand of the treaty action

14 The TIEA will enable New Zealand tax officials to request tax records, business books and accounts, bank information, and ownership information from the Bahamas. Access to this previously unobtainable information will enhance Inland Revenue's ability to detect and prevent tax avoidance and tax evasion. (The TIEA permits New Zealand to request information in relation to "taxes of every kind and description". Its likely principal application, however, will be in respect of income taxes.) Any reduction in tax avoidance or tax evasion will be beneficial to New Zealand in financial, fiscal and economic terms. The TIEA is based on the 2002 OECD model TIEA. The OECD has produced a comprehensive commentary to the 2002 model which ensures that there is consistent interpretation and application of the TIEA provisions between both Contracting Parties.

15 The Bahamas is unlikely to raise many requests for information from New Zealand. If requests for information are received from the Bahamas, New Zealand will incur

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

administrative costs in obtaining and providing the requested information. However, streamlined and effective mechanisms for dealing with exchange of information requests have already been established in relation to New Zealand's existing DTAs and TIEAs. The administrative costs of responding to requests from the Bahamas will therefore only be marginal. Experience gained from administering the exchange of information arrangements already in place under New Zealand's existing tax treaties indicates that the benefits arising from the enhanced ability to reduce tax avoidance and evasion outweigh any of the costs that arise.

16 New Zealand may be required to bear some costs in relation to requests for information that it makes to the Bahamas. A supporting less-than-treaty status instrument will be agreed between the two Contracting Parties before the TIEA enters into force. The supporting less-than-treaty status instrument will set out a shared understanding of the Parties with respect to costs, as is required by Article 10 of the TIEA. The intention of the less-than-treaty status instrument is to ensure that the requested jurisdiction does not become burdened with excessive cost when complying with a request. Thus, ordinary costs of complying with a request will be borne by the requested party, but extra-ordinary costs (such as the cost of hiring 3rd party translators) will be borne by the requesting party. This means that New Zealand could be required to bear some costs when making requests to the Bahamas, and vice versa.

17 The TIEA contains one article, Article 9, not found in the OECD model TIEA. Article 9 imposes an obligation on the Parties not to impose "prejudicial or restrictive measures based on harmful tax practices" against each other. This obligation relates to the OECD Harmful Tax Practices initiative, in which the prospect of OECD member countries taking defensive measures to restrain the harmful tax practices of other countries has previously been raised.[5] The key identifier of harmful tax practices is whether a jurisdiction engages in effective exchange of information on tax matters. Given that the TIEA provides for full exchange of information on tax matters with the Bahamas, it would be inappropriate for New Zealand to impose any such measures on the Bahamas while the TIEA is in force. The provision was included in recognition of this, but was expressed as a reciprocal obligation on both Parties.

18 On balance, it is in New Zealand's interests to conclude the TIEA with the Bahamas.

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

19 The TIEA places a reciprocal obligation on each Party to provide, upon request, information that is relevant to the administration and enforcement of specified taxes (Article 1). In the case of the Bahamas, the specified taxes are "taxes of every kind and description". However, as noted above, the Bahamas currently has a very limited tax system, and so is unlikely to make many requests for information from New Zealand.

5 The 1998 OECD report "Harmful Tax Competition: An Emerging Global Issue" and 2000 OECD report "Towards Global Tax Co-operation: Progress in Identifying and Eliminating Harmful Tax Practices" refer. The G20 Leaders Summit of 2 April 2009 re-raised the prospect of counter-measures against non-complying jurisdictions. The Leaders Statement from that Summit contained the statement that "we stand read y to deploy sanctions to protect our public finances and financial systems".

20 The Parties are required to maintain strict confidentiality in relation to any information received pursuant to a request (Article 8). Such information may only be disclosed to authorised persons and may only be used for specified purposes (principally the administration and enforcement of the domestic tax laws of the respective Party).

21 Both Parties are constrained from imposing "prejudicial or restrictive measures based on harmful tax practices" (Article 9). New Zealand does not currently impose any such measures and, given that the TIEA provides for full exchange of information on tax matters with the Bahamas, would not contemplate introducing such measures with respect to the Bahamas while the TIEA is in force.

22 Reservations are not provided for under the TIEA.

23 Article 13 of the TIEA provides that any difficulties or doubts arising as to the interpretation or application of the TIEA are to be resolved, if possible, by mutual agreement between the competent authorities (for New Zealand, the Commissioner of Inland Revenue or his or her authorised representative; for the Bahamas, the Permanent Secretary in the Ministry of Finance or the Permanent Secretary's authorised representative). The Parties may also decide upon other forms of dispute resolution.

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

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

25 Subject to the completion of the Parliamentary treaty examination process, the TIEA will be implemented into New Zealand domestic law by Orders in Council in accordance with section BH 1 of the Income Tax Act 2007.

26 After the Orders in Council have entered into force, and after the supporting less-than-treaty status instrument has been finalised, New Zealand will notify the Bahamas by diplomatic note that all of its domestic constitutional and legal procedures for entry into force of the TIEA are complete. The Bahamas will likewise notify New Zealand by diplomatic note when it has completed its domestic constitutional and legal procedures for entry into force of the TIEA. The TIEA will enter into force on the date of the last notification.

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

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

The costs to New Zealand of compliance with the treaty

28 New Zealand will likely be required to reimburse the Bahamas for extraordinary costs (such as the cost of hiring translators or interpreters) that may arise from a New Zealand request made under the TIEA. It is intended that the MOU will set out the parameters of which New Zealand will be required to reimburse the Bahamas for request of information it makes. It is intended that this will ensure that New Zealand will only progress information requests giving rise to significant reimbursement costs if the need to obtain the information justifies the expenditure.

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

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

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

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

Subsequent protocols or amendments to the treaty and their likely effects

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

Withdrawal or denunciation provision in the treaty

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

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

Adequacy statement

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