



**Inland Revenue**  
Te Tari Taake

POLICY AND STRATEGY

RECEIVED

21 JUL 2017



**THE TREASURY**  
Kaitohutohu Kaupapa Rawa

MINISTERIAL SERVICES UNIT

**Tax policy report: Cabinet paper - tax measures to prevent base erosion and profit shifting**

Date:	6 July 2017	Priority:	Medium
Security level:	In Confidence	Report no:	T2017/1847 IR2017/410

**Action sought**

	Action sought	Deadline
Minister of Finance	<p><b>Agree</b> to the recommendations.</p> <p><b>Authorise</b> the attached Cabinet paper for lodgement with the Cabinet Office.</p>	10am, Thursday 20 July 2017
Minister of Revenue	<p><b>Agree</b> to the recommendations.</p> <p><b>Authorise</b> the attached Cabinet paper for lodgement with the Cabinet Office</p>	10am, Thursday 20 July 2017

**Contact for telephone discussion (if required)**

Name	Position	Telephone
Steve Mack	Principal Advisor, The Treasury	Withheld under section 9(2)(a) of the Official Information Act 1982
Carmel Peters	Policy Manager, Inland Revenue	
Paul Kilford	Policy Manager, Inland Revenue	

6 July 2017

Minister of Finance  
Minister of Revenue

## **Tax policy report: Cabinet paper - tax measures to prevent base erosion and profit shifting**

---

1. This report recommends that you authorise the attached Cabinet paper for lodgement with the Cabinet Office by 10am Thursday 20 July 2017 for the Economic Growth and Infrastructure Committee to consider at its meeting on 26 July 2017. This report also recommends you agree to a change to our previously recommended hybrids measures in respect of foreign trusts.

2. The attached Cabinet paper provides an overview of three other Cabinet papers which seek approval for a package of measures to address base erosion and profit shifting (BEPS) in New Zealand. The Cabinet paper also summarises the background to the other papers, highlights the most important aspects of the proposals, and discusses matters common to all three papers (including application dates, publicity, and financial implications). The other papers are:

- BEPS – interest limitation submissions and policy decisions;
- BEPS – transfer pricing and permanent establishment avoidance submissions and policy decisions; and
- BEPS – recommendations on addressing hybrid mismatch arrangements.

3. At the request of your office we have prepared the attached Cabinet paper in advance of the other three. We are currently working on the other papers and will provide those to you next week.

4. We reported to you on the package of BEPS measures to which all four Cabinet Papers relate on 22 June 2017 (T2017/1576, IR2017/325; T2017/1577, IR 2017/330; T2017/1578, IR2017/329; T2017/1604, IR2017/353).

5. If you agree with the drafting of the attached Cabinet paper, we recommend you authorise it for lodgement with the Cabinet Office (together with the other 3 Cabinet papers) by 10am Thursday 20 July 2017 for consideration at the Economic Growth and Infrastructure Committee meeting of 26 July 2017.

## Foreign Trusts

6. In regards to foreign trusts, the Cabinet paper is consistent with our recent hybrids policy report (T2017/1604 / IR2017/353), but it also reflects some further policy development as well as filling in a gap in the recommendations contained in the policy report. As set out in that report, in principle we believe that New Zealand foreign trusts can result in double non-taxation due to a hybrid mismatch, where:

- New Zealand does not tax the New Zealand trustee because the beneficiary or settlor is non-resident; and
- the beneficiary's or settlor's residence country does not tax that person because the trustee is non-resident.

7. We now recommend amending that proposal slightly, to clarify that the New Zealand trustee should not be taxable on income so long as someone is required to include that income in their taxable income. So, for example, New Zealand should not tax an amount allocated to a beneficiary if the settlor is required to include that amount in its tax return in its own jurisdiction in that year. Similarly, we should not impose tax on unallocated income retained by the trustee if a beneficiary is required to include the amount in their tax calculation for that year. This clarification is important to avoid our proposed rules imposing two layers of tax on the trust income.

8. Accordingly, we recommend taxing a New Zealand trustee on foreign-sourced beneficiary income allocated to a non-resident beneficiary as if the trustee were a New Zealand resident individual taxpayer to the extent that:

- the beneficiary is in the same control group as the trustee (many family trusts would meet this requirement);
- the beneficiary would be taxed on the trust income if it held the trust assets directly; and
- the income is not subject to tax as the income of any person other than the trustee (such as the beneficiary or settlor).

9. We also recommend taxing the New Zealand trustee of a foreign trust on foreign-sourced trustee income to the extent that:

- the settlor is in the same control group as the trustee (again this would often be the case);
- the settlor would be taxed on the trustee income if it held the trust assets directly; and
- the income is not subject to tax as the income of any person other than the trustee.

10. In error, our policy report did not include any recommendations on trustee income (see recommendation (k)). We therefore take this opportunity to clarify that trustee income is within the scope of the proposed rules, subject to the modifications discussed above.

11. We recommend a de minimis, so that neither of these rules applies if the total foreign sourced income of the trustee does not exceed the greater of \$10,000 and 20% of the total income of the trust.

12. Importantly, we do not consider any of the changes proposed here are inconsistent with the discussion between officials and Ministers at our meeting on 29 June. We are still only proposing to tax income of foreign trusts to the extent they are “reverse hybrids” and we are not proposing to impose tax on all income of trustees of foreign trusts.

## Recommended action

---

We recommend that you:

(a) **Agree** that New Zealand should tax a New Zealand resident trustee on foreign-sourced beneficiary income allocated to a non-resident beneficiary as if the trustee were a New Zealand resident individual taxpayer to the extent that:

- the beneficiary is in the same control group as the trustee; and
- the beneficiary would be taxed on income from the assets giving rise to the beneficiary income if it held the assets directly; and
- the income is not subject to tax as the income of any person other than the trustee (such as the beneficiary or settlor)

Agreed/Not agreed

Agreed/Not agreed

(b) **Agree** that New Zealand should tax a New Zealand trustee of a foreign trust on foreign-sourced trustee income to the extent that:

- the settlor is in the same control group as the trustee;
- the settlor would be taxed on the trustee income if it held the trust assets directly; and
- the income is not subject to tax as the income of any person other than the trustee.

Agreed/Not agreed

Agreed/Not agreed

- (c) **Agree** that a de minimis apply, so that neither of the rules in recommendation (a) and (b) applies if the total foreign sourced income of the trustee does not exceed the greater of \$10,000 and 20% of the total income of the trust.

Agreed/Not agreed

Agreed/Not agreed

- (d) **Authorise** the attached Cabinet paper for lodgement with the Cabinet Office by 10am Thursday 20 July 2017 for the Economic Growth and Infrastructure Committee to consider at its meeting on 26 July 2017.

Signed and referred

Signed and referred

Withheld under section 9(2)(a) of the Official Information Act 1982

**Steve Mack**  
Principal Advisor  
Tax Strategy  
The Treasury



**Carmel Peters**  
Policy Manager  
Policy and Strategy  
Inland Revenue

**Hon Steven Joyce**  
Minister of Finance



**Hon Judith Collins**  
Minister of Revenue