The Treasury

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[1]	to prevent prejudice to the security or defence of New Zealand or the international relations of the government	6(a)
[2]	to protect the privacy of natural persons, including deceased people	9(2)(a)
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TRANSPARENCY INTERNATIONAL New Zealand

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20 May 2016

Patron, Sir Don McKinnon

Transparency International New Zealand Submission to the Government Inquiry into Foreign Trust Disclosure Rules

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Dear John

Thank you for the opportunity to respond to the Government Inquiry into Foreign Trust Disclosure Rules (the "Inquiry"). This Inquiry is important. New Zealand's reputation as an international good citizen and the resulting financial benefits are at stake.

Transparency International New Zealand (TINZ) finds that:

- existing foreign trust disclosure rules are not sufficient
- disclosure rules for corporate entities are also not sufficient
- gaps exist in the Anti-Money Laundering and Countering Financing of Terrorism (AML/CFT) laws
- reactive international data sharing arrangements are ineffective

Loose governance in these four key areas enables exploitation of our national systems. All of these areas need to be addressed in order to ensure that New Zealand is not a conduit for, or a location supporting, money laundering, tax fraud, reputation cleansing, and hiding of assets from authorities or others with entitlements or rights (such as shareholders or spouses).

There is no question that New Zealand's international reputation generates immense returns to the economy including a major contribution to billions of dollars in export, tourisms and on-line business earnings. By assuming an aggressive leadership role in international efforts to eliminate misuse of trusts and corporate entities, New Zealand will enhance both its reputation and the return to the economy. Positive initiatives including the existing AML/CFT regime, the Common Reporting Standard initiative, an International Anti-Corruption Law Enforcement Coordination Centre, and New Zealand's support for the UN Convention against Corruption will only be weakened if known gaps, now internationally publicized as system failings in our rules, are not corrected, and seen to be corrected.

Our specific answers to the Inquiry questions are below

Question 1: Whether you consider the existing foreign trust disclosure rules are adequate to ensure that New Zealand's reputation as a country that cooperates with other jurisdictions to deter abusive tax practices?

TINZ does not consider that New Zealand's existing foreign trust disclosure rules are adequate.

1. There is no general requirement to register a foreign trust in New Zealand.
2. When involved in taxable New Zealand events, information collected by the IRD on foreign trusts does not extend to the persons who exercise effective control (beneficial owner) over the trust or

the trust's assets.

3. There is no proactive process - except with Australia - for reporting involvement of foreign nationals to their respective governments.
4. The absence of the information about the beneficial owners makes cooperation ineffective in tax evasion and criminal matters.

Even corporate disclosure rules share the above inadequacies. The looseness of New Zealand's disclosure rules undermine international efforts to combat organised crime, including financial and asset flows to tax evasion, fund terrorism, money laundering, corruption and impunity. This inadequacy undermines New Zealand's reputation as a country that cooperates with other jurisdictions in these critical areas of governance and instead likely promotes effortless usability of our systems as open for exploitation.

Question 2: Concerns have been raised that foreign trusts may be used as vehicles to hide investments that might not have a legitimate source. Do you consider that the existing anti-money laundering/countering foreign terrorism legislation is able and sufficient to address such concerns?

TINZ does not consider that existing AML/CTF legislation is sufficient and able to address concerns related to the hiding of investments that might not have a legitimate source. A significant gap remains as lawyers, accountants, and real estate agents who provide similar services, fall outside the AML/CFT regime. While there is a commitment to including lawyers and accountants in the AML/CFT regime (Phase 2), no timetable has been provided for this.

If New Zealand implemented Phase 2 as soon as possible, it would be positioned to meet international standards set by the FATF and to address Principle 5 of the G20 High Level Principles. The importance of these laws is highlighted by findings of the 2010 National Risk Assessment on Money Laundering which rated gatekeepers and professional services, including lawyers and accountants, as high risk of being misused for money laundering.

Question 3: If no to either of the above questions, is this because the law is not adequate or because the enforcement is not sufficiently rigorous?

The law is inadequate. More rigorous enforcement in these circumstances is both costly and frustrating as evidential audits are complex because of lack of transparency and ownership accountability. Legal remedies will need to include proper funding to establish and enforce.

Question 4: What changes to the foreign trust disclosure rules or their enforcement do you recommend?

Establish a comprehensive register for the collection and maintenance of accurate beneficial ownership information on all types of legal constructions including foreign trusts. It would require the registration and of all trusts foreign and domestic, maintain accurate and up-to-date information, have the capability to be interrogated as needed in domestic and international criminal investigations and integrate with the international Common Reporting Standard initiative The New Zealand Anti-money Laundering/Countering Financing of Terrorism (AML/CFT) Act (2009) should be extended to cover all professionals, including lawyers, accountants and real estate agents that are engaged in setting up or managing assets of New Zealand corporate vehicles and trusts.

Question 5: What other actions might be taken?

Take account of work already done by the Task Force on Money Laundering (FATF) and others to develop a beneficial ownership register of companies with sufficient resources and information sharing arrangements.

Please contact us for more information

TINZ welcomes the opportunity to discuss this submission with you in person. Please do not hesitate to contact us if you have any questions or would like to meet.

A. Introduction

There are a range of fundamental issues relating to transparency and financial integrity in regards to the structure of trusts in New Zealand. Many of these issues are not new as there have been international standards to ensure the transparency of offshore corporate vehicles for years.

For example, see the Financial Advisory Task Force (FATF) recommendations from 2013 (see www.faft-gafi.org). The purpose of these recommendations is to prevent and detect money laundering, tax evasion and corruption. While New Zealand has taken some actions to address the misuse of trusts (and other legal constructions) for criminal purposes, further tightening is required. For example, there is a pressing need for a public central register of company beneficial ownership information.

Amongst other things, this would bring New Zealand alongside the Netherlands, the United Kingdom, and France, who have all made concrete efforts to create greater public transparency related to all corporate vehicles registered in their countries.

The direction taken by your Inquiry will have a material impact on the future of New Zealand's standing in the world. As such, it also has the potential to impact on our collective prosperity and that of future generations, by undermining New Zealand's reputation for integrity based on evidence-based research done for the New Zealand Story due to the now public and global perception that New Zealand is a soft touch with poor management of corporate structures with offshore ownership.

This submission responds both to the specific issues raised in the Inquiry and recommends solutions beyond the Inquiry's limited scope as communicated to you previously.

The reason is that transparency around beneficial ownership relates both to offshore trusts and any companies or trust registered in New Zealand.

For the purposes of this submission, Transparency International (New Zealand) is referred to as TINZ.

B. Background

The Panama Papers have identified that there are hundreds of thousands of offshore corporate vehicles domiciled in countries other than the principal residences of the beneficial owners. Yet, in many countries, depending on the type of offshore vehicle that is registered, the only formal, usually limited, records are held at a lawyer's or accountant's office in the relevant offshore financial centre.

It is important to recognise that offshore vehicles, perhaps even the majority of those registered in New Zealand, may be used for legitimate purposes. The risk to New Zealand is that its reputation attracts some to use foreign trusts to provide asset protection and security expecting to hide behind the New Zealand's good standing. This reputation is evidenced in its annual (good) Corruption Perceptions Index (CPI) score and ranking, and, through other related surveys, such as its Good Country ranking as number 5.

The New Zealand Story (see www.nzstory.gov.nz/what-is-nz-story), a government initiative launched in 2013, has found that international focus groups regard New Zealand's strongest attractions for doing business are its integrity, kaitiaki and resourcefulness.

Offshore vehicles can be misused for criminal purposes including tax evasion, money laundering and corruption. For example, the World Bank Puppet Masters report found that over 80% of grand corruption cases involved the use of offshore vehicles. Much evidence for this finding has been found by Transparency International. Recent news has identified senior politicians in South America, among others, who are indicted for corruption, using such a vehicle in New Zealand.

There are important considerations of privacy, compliance costs and coverage when developing good policy. In this case, however, the Financial Action Taskforce (FATF) has been working for over 25 years to address this considerations and based on the resolution of them, has developed policy for making the beneficial ownership of offshore vehicles transparent, in an efficient and effective way to prevent their illegal misuse. New Zealand has undertaken its own policy work in this area as background to its participation in the G20 initiative which in November 2014 where the country leaders attending committed to the implementation of the High Level Principles of Beneficial Ownership[1]. These principles call on countries to tackle the risks raised by the opacity of legal persons and legal arrangements.

New Zealand is due to be evaluated by the FATF in 2019. This Inquiry, then, is an important opportunity to recommend steps so that there is an effective AML/CFT regime prior to this evaluation. As well as reducing the risk of illicit and criminally sourced funds infecting our financial systems and society, this has the potential to restore New Zealand's position as a leader on the international stage in regards to preventing corruption and to enhance its reputation for an integrity system based on doing the right thing.

Other countries are looking to New Zealand to take an active role in discussing and implementing workable remedies and to set an example. This is evidenced whenever TINZ attends international conferences such as the recent Tackling Corruption Conference held for NGOs the day before UK Prime Minister, David Cameron's Anti-corruption Summit on 12 May 2016.

C. Scope of the Inquiry

As mentioned above, Transparency International New Zealand (TINZ) understands that substantial government policy work has already been completed around the corporate register and the registration of foreign trusts that the Inquiry could build on. As well as being part of the preparation for the G20, where New Zealand was invited by host country Australia to attend as a guest, there has also been policy work undertaken for the development of the omnibus Organised Crime and Anti-corruption Legislation passed in November 2014 which led to the introduction of 15 new Acts and the New Zealand Government ratifying the United Nations Convention Against Corruption (UNCAC).

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[1] http://www.g20australia.org/official_resources/g20_high_level_principles_beneficial_ownership_transparency

A comprehensive register which collects and maintains accurate beneficial ownership information on all types of legal constructions, adequately resourced and funded to be effective would have the following attributes:

- adequate enforcement of the requirements by the Companies Office so that the beneficial ownership information maintained is accurate, up-to-date and with clear access criteria and processes
- a database of beneficial owners that has sufficient capability to be interrogated and accessed for clearly defined purposes, cross-referenced with other government information such as that held by the IRD, and
- information-sharing principles and arrangements in place for authorities to access the information when needed in criminal investigations.

The benefits of such a register can be learned from the development of beneficial ownership registers that has been advanced globally. For example, several European Union countries are developing beneficial ownership registers following the EU directives on this topic. The United Kingdom has implemented legislation in April this year. South Africa already has a register.

The risk of New Zealand's prevarication impacts on its global alignment, probably on its role of the UN Security Council and perversely has the potential to create greater demand for setting up offshore entities here. There is potential for arbitrage to occur between jurisdictions for the registration of offshore entities that are used for inappropriate and illegal purposes, essentially looking for the easiest options, that is, jurisdictions where legislation is the loosest.

D. Questions posed by the Inquiry

Question 1: Whether you consider the existing foreign trust disclosure rules are adequate to ensure that New Zealand's reputation as a country that cooperates with other jurisdictions to deter abusive tax practices?

TINZ does not consider that New Zealand's existing foreign trust disclosure rules are adequate for any purpose stated in the question. There is an opportunity to address this by committing to international conventions as indicated by the Rt Hon Judith Collins at the 12 May 2016 London Anti-Corruption Summit.

While some basic information is collected by the IRD on foreign trusts, this does not extend to the persons who exercise effective control over the trust or the trust's assets. There simply is no ability to cooperate with other countries in the absence of the information to make cooperation effective. Even if the IRD were able to request this information from the foreign trust, this reactive mechanism lacks timeliness and does not support investigations or effective international cooperation.

This adds greatly to the cost of searching for evidence for investigation.

An internationally comparatively advantageous taxation regime for foreign trusts (and other offshore vehicles) increases the risk that New Zealand is misused for illicit purposes. Criminals may seek to use foreign trusts (and other offshore vehicles) to hide high volume of assets.

In addition, without sufficient information held onshore in New Zealand, it can make it difficult for authorities to detect suspicious activity or have comfort over the funds because information on the assets and the taxpayer is held in different countries. It is, therefore, impossible for New Zealand tax authorities to support their counterparts in countries from where the funds came from, undermining these source country authority's ability to pursue crime in their own jurisdictions.

An independent assessment of New Zealand's trust regime by the OECD Global Forum has independently confirmed that there is no general requirement to register a trust in New Zealand[2]. New Zealand should consider establishing a centralised register which maintains beneficial ownership information on all legal entities registered in New Zealand, any intermediate legal entities registered offshore, and final beneficial owners. This register should be accessed by law enforcement and regulatory supervisors. The register will be an effective tool to enable law enforcement to look through offshore vehicles in investigations where they may be used to disguise the beneficial owners. A register would also allow New Zealand to provide timely and extensive international cooperation in investigations of tax evasion and corruption cases.

The beneficial ownership registers should contain sufficient information about the trusts and companies to allow authorities to identify and understand the natural persons who exercise effective control over the corporate vehicles.

The definitions should ensure consistency with international standards set by the FATF and OECD.

For example:

- for companies, this should include all natural persons with greater than 25% shareholding, and
- for trusts, this should include information on the trustees, settlors, protectors (if any) and the beneficiaries of a fixed trust.

We further recommend that the Register be so configured to flag suspicious activity and registrations automatically to New Zealand enforcement agencies and regulators, rather than to allow it to be only interrogated only when an investigation is deemed necessary.

New Zealand has committed the implementation of the automatic exchange information (AEOI) requirements in 2017 and this will enhance the transparency of the foreign trusts. However, this should be extended to ensure that real time information is available on trusts for use by authorities.

Question 2: Concerns have been raised that foreign trusts may be used as vehicles to hide investments that might not have a legitimate source. Do you consider that the existing anti-money laundering/countering foreign terrorism legislation is able and sufficient to address such concerns?

TINZ does not consider that existing AML/CTF legislation is sufficient and able to address concerns related to the hiding of investments that might not have a legitimate source.

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[2] See the Global Forum on Transparency and Exchange of Information for Tax Purposes Peer Reviews: New Zealand 2013 (Phases 1 and 2) at page 41. Last accessed 18 May 2016 at http://www.oecd-ilibrary.org/taxation/global-forum-on-transparency-and-exchange-of-information-for-tax-purposes-peer-reviews-new-zealand-2013_9789264205864-en

In November 2015, New Zealand passed legislation further regulating trust and company service providers for anti-money laundering and countering the financing of terrorism (AML/CFT) purposes. Under this new legislation, businesses providing services for the establishment of trusts and companies are required to undertake a risk assessment and establish an AML/CFT programme.

This includes the identification of customers, monitoring activity and reporting any suspicious transactions. In high risk situations, businesses must identify and take reasonable steps to verify the source of wealth or funds of the client. These laws act as a deterrent for the misuse of trusts and companies and ensure that information is available to law enforcement in investigations.

With this new legislation, a significant gap remains as lawyers and accountants, who provide similar services, fall outside the AML/CFT regime. While there is a commitment to including lawyers and accountants in the AML/CFT regime, no timetable has been provided for the implementation of Phase 2.

If New Zealand implemented Phase 2 as soon as possible, it would be positioned to meet international standards set by the FATF and to address Principle 5 of the G20 High Level Principles. The importance of these laws is highlighted by findings of the 2010 National Risk Assessment on Money Laundering[3] which rated gatekeepers and professional services, including lawyers and accountants, as high risk of being misused for money laundering.

Given the diverse nature of Phase 2 entities, including and professional service providers, there is scope for policy that provides sufficient guidance and active supervision to ensure effective implementation.

Best practice risk management at professional services firms includes risk assessments and due diligence on potential clients as a matter of conflict management, so this should not in fact be onerous.

Question 3: If no to either of the above questions, is this because the law is not adequate or because the enforcement is not sufficiently rigorous?

TINZ does not consider the laws to be adequate. As a result, enforcers can only follow transactions to New Zealand and then the trail goes dead. More rigorous enforcement in these circumstances is both costly and frustrating as evidential audits are complex because of the lack of transparency and ownership accountability.

Other research by TINZ for its 2013 New Zealand National Integrity Systems (www.transparency.org.nz/NIS) assessment found that an area where New Zealand can keep costs down, relative to other jurisdictions, is anti-corruption enforcement.

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[3] http://www.justice.govt.nz/policy/criminal-justice/aml-cft/publications-and-consultation/documents/national-risk-assessment-2010

This is because of the existence of corruption prevention policies and conventions. In the past, it has been possible for many daily transactions between citizens and businesses to work effectively through convention.

This is an attribute of New Zealand that has considerable value – it would be much more costly to become a country with high levels of international money laundering and organised crime with its considerable higher enforcement costs.

As outlined in previous sections, gaps remain in the AML/CFT laws. New Zealand has not implemented international standards to which it has committed to mitigate the risk of offshore vehicles being misused for criminal purposes. In the absence of the disclosure of beneficial interests, the registration of such entities and their advisors, there is limited scope for any enforcement agency or regulator to identify the identity of beneficial owners, in order to be able to determine whether their funds were generated illegally or not.

We have also submitted our comments on resourcing for effectively addressing and preventing corruption in several sections of this Submission. Having said this, evidence collected by the 2013 NIS found that corruption prevention would be assisted with greater resourcing for education about corruption, particularly to anti-corruption units at the SFO, Police and FMA (as well as part of civics study generally).

Even when strengthened, having laws in place is not sufficient to ensure that compliance with those laws can be effectively monitored to achieve the outcome intended. Due to the technical nature of investigations and the increasingly digital nature of financial transactions, human resourcing, training and professional development is also a matter of priority.

Question 4: What changes to the foreign trust disclosure rules or their enforcement do you recommend?

As highlighted in question 1, we consider that additional disclosure rules are required through the establishment of a register of legal entities which holds beneficial ownership information. TINZ four main recommendations cover the changes in entity structures.

Question 5: What other actions might be taken?

TINZ has discussed a range of actions to taken in its answers to the four previous questions.

The establishment a legal entity registry, appropriately resourced, to maintain an up-to-date register of beneficial ownership information, is a means of ensuring the transparency of corporate vehicles to prevent their misuse for criminal purpose.

In addition, criminals often seek to use multiple layers of ownership to disguise beneficial ownership and this may include the use of foreign trusts in the ownership change of New Zealand registered companies.

To address the risks associated with the misuse of companies, new laws commenced in 2015 requiring one New Zealand resident director are a step in the right direction.

The early introduction of a beneficial ownership register, administered by a registry with adequate resources and powers will ensure an effective and efficient mitigation of the criminal risks from large international transactions seeking a place to put assets or launder money.

E. Presenting to the Inquiry

The area of trusts, identification, definition and registration of beneficial owners, the structuring of registers and the setting up robust processes for accessing and using the data, while maintain privacy and low compliance costs, are all issues requiring discussion and thought. TINZ has been collecting information and building knowledge on this topic for some years now. One of our members has worked for both the OECD and FAFT, directly addressing the questions of the Inquiry in New Zealand and abroad.

TINZ would welcome the opportunity to discuss this submission with you in person. Please do not hesitate to contact us if you have any questions or would like to meet.

Yours sincerely,

Suzanne Snively, ONZM

Chair, Transparency International New Zealand Inc.