

The Treasury

Foreign Trust Inquiry Information Release

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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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[4]	to maintain the effective conduct of public affairs through the free and frank expression of opinions	9(2)(g)(i)
[5]	that the making available of the information requested would be contrary to the provisions of a specified enactment [the Tax Administration Act 1994]	18(c)(i)

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POLICY ADVICE DIVISION

PAD report: Foreign trusts: proposed amendments to recommendations

Date:	13 April 2005	Priority:	High
Security Level:	In Confidence	Report No:	PAD2005/094

Action sought

	Action Sought	Deadline
Minister of Revenue	Agree to recommendations	13 April 2005
Associate Minister of Revenue (Hon David Cunliffe)	For your information	None

Contact for telephone discussion (if required)

Name	Position	Telephone
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13 April 2005

Minister of Revenue

cc: Associate Minister of Revenue (Hon David Cunliffe)

Foreign trusts: proposed amendments to recommendations

Executive summary

In a report dated 7 February 2005 (PAD2005/022, T2005/160 refers) we recommended that certain information disclosure and record keeping requirements be introduced for qualifying New Zealand resident trustees of foreign trusts.

As part of the legislative drafting process, we have identified a gap in how the law would be applied. To address this concern we recommend that:

- the requirement to disclose certain information to Inland Revenue and maintain financial records for New Zealand tax purposes be imposed on New Zealand resident trustees, and not restricted to qualifying New Zealand resident trustees; and
- the Commissioner of Inland Revenue has the ability to make an income tax assessment for any income year for which a foreign trust had no qualifying New Zealand resident trustee and financial records requested by Inland Revenue could not be provided.

The Treasury has been consulted in the preparation of this report and agrees with the proposed recommendations. The Ministry of Justice has advised that the proposed changes are unlikely to give rise to issues of discrimination under the New Zealand Bill of Rights Act 1990.

Recommended action

We recommend that you:

- (a) **Agree** that information disclosure and record keeping requirements be imposed on New Zealand resident trustees, and not restricted to qualifying New Zealand resident trustees.

Agreed/Not agreed

- (b) **Agree** that the Commissioner of Inland Revenue should have the ability to make an income tax assessment for any income year for which a foreign trust had no qualifying New Zealand resident trustee and financial records requested by Inland Revenue could not be provided.

Agreed/Not agreed

Michael Nutsford
Portfolio Manager
Policy Advice Division

Hon Dr Michael Cullen
Minister of Revenue

The problem

1. In a report dated 7 February 2005 (PAD2005/022, T2005/160 refers) we recommended that certain information disclosure and record keeping requirements be introduced for qualifying New Zealand resident trustees of foreign trusts. As part of the legislative drafting process, we have identified a gap in how the law would be applied.
2. Qualifying New Zealand resident trustees are New Zealand resident trustees who satisfy an additional requirement to be a member of an organisation that has been approved by Inland Revenue (such as ICANZ or the New Zealand Law Society). This membership requirement is intended to provide assurance to Inland Revenue that a trustee has the necessary expertise and the incentive to maintain records of the required standard, and will comply with the law.
3. Under the current proposal, qualifying New Zealand resident trustees would be required to disclose information to Inland Revenue and maintain financial records for New Zealand tax purposes. New Zealand resident trustees who are non-qualifying would initially be subject to a new criminal penalty for non-compliance. If a non-qualifying trustee failed to become qualifying (or have a co-trustee appointed who satisfied this requirement) within thirty days of receiving notice from Inland Revenue of its intention to prosecute, the worldwide income of foreign trusts that the non-qualifying trustee provided trustee services to would be subject to tax in New Zealand. This tax treatment would be applied prospectively.
4. As it stands, non-qualifying New Zealand resident trustees could not be penalised for failure to keep financial records for past income years. Foreign trusts that have a non-qualifying New Zealand resident trustee would only be subject to tax in New Zealand on a prospective basis. Also, a non-qualifying New Zealand resident trustee would not be subject to a criminal penalty for failure to keep or provide records, as the record keeping obligation would only be imposed on *qualifying* New Zealand resident trustees.

Proposed solution

5. To address these concerns, we consider that the requirements to disclose certain information and maintain financial records should be imposed on all New Zealand resident trustees of foreign trusts, and not restricted to qualifying New Zealand resident trustees. This will ensure that all non-compliant New Zealand resident trustees will be subject to existing criminal penalties for failure to provide information and keep or provide financial records.
6. In addition, we consider that the tax treatment of foreign trusts that have a non-qualifying New Zealand resident trustee should vary, depending upon whether the non-qualifying trustee can or cannot provide the required financial records to Inland Revenue, if requested. The tax treatment would be applied as follows:
 - Inland Revenue requests information and a non-qualifying New Zealand resident trustee *can* provide the required financial records: the foreign trusts that the non-qualifying trustee provides trustee services to will be subject to tax in New Zealand on a

prospective basis. However, if the trustee becomes a qualifying New Zealand resident trustee (or has a co-trustee appointed who satisfies this requirement) within thirty days of receiving notice by Inland Revenue of its intention to prosecute for non-compliance, the foreign trusts will not be liable for tax in New Zealand (under the current proposal).

- Inland Revenue requests information and a non-qualifying New Zealand resident trustee *cannot* provide the required financial records: the Commissioner of Inland Revenue will have the ability to make income tax assessments for any income year for which financial records were requested, but were not kept or provided. If the trustee does not become a qualifying New Zealand resident trustee (or have a co-trustee appointed who satisfies this requirement), this tax treatment will also be imposed prospectively. If the non-qualifying trustee subsequently provides the information requested by Inland Revenue, the tax liability will be removed.

7. Foreign trusts will only be liable to tax on their world-wide income, under these proposals, for the period post 1 April 2006 – the commencement date of the proposed changes.

8. If the worldwide income of a foreign trust becomes liable to tax in New Zealand, the New Zealand resident trustee will be required to file an income tax return on that basis. The tax return may provide Inland Revenue with information that it can provide to New Zealand's DTA partners, if requested.

9. We consider that the proposed changes will strengthen the incentive for New Zealand resident trustees to become qualifying New Zealand resident trustees, and maintain and provide financial records of the required standard.

Consultation

10. The Treasury has been consulted in the preparation of this report and agrees with the proposed recommendations.

11. We provided the Ministry of Justice with a copy of the amended proposal for their consideration. The Ministry of Justice has advised that the proposed changes are unlikely to give rise to issues of discrimination under the New Zealand Bill of Rights Act 1990.

