

# Shifting sands: the unavailing of international exchange of information and disclosure rules on tax matters

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This article investigates the purview of Article 26 (Exchange) a which empowers revenue authorities in two different jurisdictions to obtain taxpayer related information from each other. The operation of Article 26 is considered in light of the issues surrounding the non disclosure of information in judicial reviews as well as New Zealand's recent international commitment to implement the new global standard on Automatic Exchange of Information (AEOI). The (NZ); and the leading exchange of

information cases in New Zealand. The article further examines New Zealand's recent international commitment to implement the G20 and OECD's Automatic Exchange of Information (AEOI) in accordance with the Common Reporting Standard (CRS) due diligence, as significant shift in how jurisdictions share tax information and step away from the traditional 'exchange on request' model. The article demonstrates that, as evidenced by case law, an alternative approach to the strict rule of non disclosure of information to the taxpayer in judicial reviews would protect the confidentiality obligations of tax authorities and maintain taxpayer confidence. It is argued that the principles enunciated by the House of Lords in *Belmont* (2006) in relation to the scope for discovery under the *Belmont* (UK) and in UK judicial review proceedings would form an appropriate basis for such an approach. The analysis in this article serves as a guide for policy makers to take the necessary steps to ensure that tax information secrecy is not sacrificed in the desire to achieve greater transparency.

: article 26; OECD Model Tax Convention; double taxation; secrecy; Automatic Exchange of Information; i

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evasion but it also serves as a double edged sword, allowing the DTA jurisdiction tax authorities to exert significant power over New Zealand taxpayers while suppressing their ability to question the grounds for exercising that power:

Cases on the exchange of information have indicated difficulties in applying the provisions of the DTA with consideration to the New Zealand Income Tax Act 1996 (ITA) and the Income Tax Act 2007 (ITA). In particular, taxpayers have argued that the revenue authorities' secrecy obligation under s 81 of the ITA has not been fully excluded for the purpose of carrying out the provisions of Article 26. However, it is questionable as to the DTA take precedence over domestic law<sup>10</sup>. Additionally, an appropriate balance must be maintained between the privacy rights of the taxpayer and protection of public revenue<sup>11</sup>. It is not a valid argument to say that when it comes to tax collection, all privacy rights are outweighed as a matter of public interest<sup>12</sup>. This suggests that further work is still required to achieve a genuinely workable Article 26 of the MTC.

Whilst bilateral treaties such as those based on Article 26 of the OECD MTC permit barr

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The study evaluated the cost and benefits of AEOI to New Zealand in terms of sovereignty, rights of taxpayers, administrative expense for Inland Revenue and financial institutions, and the impact of offshore tax evasion under AEOI. The study concluded that the implementation of AEOI would be less beneficial to New Zealand than suggested in advocating tax evasion. The study reported that the cost of AEOI to New Zealand in terms of the factors listed above would outweigh the benefits of the AEOI. The study noted that the OECD's implementation of AEOI has a direct impact on New Zealand legislation and the OECD is effectively redefining the monopoly of the state over tax policy.

Arts Score's study<sup>22</sup> examined whether AEOI invades the privacy rights of the individual proportionately in Estonia. Contrastingly, Score's study reported that AEOI serves as an efficient tool, and that information processes under automatic exchange do not interfere with the fundamental rights of the individual. It also argued that financial account information provided by the individual under AEOI is the standard information an individual is required to provide.

Sadiq and Sawyer's study indicated that many of the developing Asia Pacific countries will be likely face challenges in grappling with understanding the implications of the common reporting standard for AEOI for their tax administrations and require modifications in their domestic laws to enable effective AEOI.<sup>23</sup> Dirlis and Bordfield's study<sup>24</sup> examined the growth of international collaborative initiatives to improve transparency and exchange of information. Their study also concluded that the Australian tax authorities' active involvement with the Joint International Tax Shelter Information Centre (JITSIC), (FATCA) treaty with the US and participation in the OECD Multilateral Convention will be complex and resource intensive to manage.<sup>25</sup>

The literature has not yet examined exchange of information in the context of rules relating to disclosure of information by tax authorities to taxpayers with consideration of the implementation of AEOI. This study addresses this gap and considers application of Article 26 of the OECD MIC and the issues surrounding the non-disclosure of information in judicial reviews. It suggests alternatives to the strict rule of non-disclosure of such information in judicial reviews. The next section first considers New Zealand tax authorities' information gathering powers both outside and within the DIA.





Martin's study aptly pointed out that the State's<sup>39</sup>

.. right to enact laws that impose a tax liability on persons who are outside New Zealand is distinct from its right to enforce those laws against those same persons outside New Zealand

According to Martin, the New Zealand IIA does not extend to foreign jurisdictions but rather restricts its application to 'persons and transactions, which have a reasonably close legal and factual connection to New Zealand'.<sup>40</sup> However, the Commissioner is entitled to know the income earning activities performed in New Zealand and decide accordingly whether they are taxable or not. The revenue authorities' enforcement jurisdiction can only be exercised over persons that are residents of New Zealand, and incomes sourced from New Zealand. The criteria of falling within the definition of a resident are set out in ss YD 1 to YD 4 IIA.<sup>41</sup>

The Australian decision in *Commissioner of Taxation v. Australian Federal Police*<sup>42</sup> illustrates the principle that revenue authorities cannot use their powers of inspection or interview to obtain information for the tax office of a foreign state.<sup>43</sup> The Court concluded that the Australian revenue authorities acted in exercising subdivision 35B 10<sup>44</sup> to obtain evidence for the purpose of providing assistance to New Zealand to enforce its revenue law.<sup>45</sup> The Court specifically commented that revenue authorities cannot use their powers of inspection or interview to obtain information for the tax office of a foreign state.<sup>46</sup>

New Zealand courts applied this restriction in *Commissioner of Taxation v. Australian Federal Police*<sup>47</sup> and *Commissioner of Taxation v. Australian Federal Police*<sup>48</sup>

In *Commissioner of Taxation v. Australian Federal Police*,<sup>49</sup> the Permanent Court of International Justice gave an important dictum on the parameters of a State's enforcement jurisdiction. The Court concluded that a State cannot exercise its jurisdiction outside its territory unless an international treaty or customary law permits it to do so. It further held<sup>50</sup>

Now the first and foremost restriction imposed by international law upon a State is that, failing the existence of a permissive rule to the contrary — it may not exercise its power in any form in the territory of another State. In this sense jurisdiction is certainly territorial; it cannot be exercised by a state outside its territory except by virtue of a permissive rule derived from international custom or from the convention.

<sup>39</sup> Dehan Martin 'Enforcing Trusts'



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matters relevant for carrying out the provisions of the Convention. The OECD Committee on Fiscal Affairs in 1975 revised and approved the text of Article 26 and the



















assistance to the appellant's case on proportionality, over and above the summary already furnished, to justify its disclosure in the interests of fair disposal of the case.<sup>126</sup>

It is suggested that the principle in *Wentworth* could be adopted into the New Zealand judicial review system and that the courts are currently not bound by *Wentworth* which enforced the second part of Article 26(2), in interpreting it to hold that the Article prevents disclosure of relevant documents.

On the second part, Baagwanth J suggested an alternative to the strict non-disclosure rule. In the *Wentworth* case, Baagwanth J promoted the possibility of providing the applicant leave to appoint a special counsel to act as *amicus curiae* where the information sought is secret under the DIA.<sup>127</sup> The necessary boundaries of the counsel's obligation would include non-disclosure of confidential information to the applicants and submissions to the court to be made on an *in camera* basis. An option for a special counsel would restore confidence to the taxpayer by providing representation, and preserve the secrecy obligations of the tax authorities imposed by domestic law and the DIA. However, difficulties would emerge in the appointment of the special counsel, which would require mutual agreement between the taxpayer and the Crown (tax authorities).

As discussed in the introduction, in order to tackle offshore secrecy and tax evasion, the Multilateral Convention<sup>128</sup> provides a new global standard for the automatic exchange of financial account information (AEOI) pursuant to the Common Reporting Standard (CRS)<sup>129</sup> and all possible forms of administrative co-operation between Contracting States. The next section covers studies from different jurisdictions that examine the issues related to implementation of AEOI and taxpayers' secrecy. Since New Zealand has signed the Multilateral Convention<sup>130</sup> it is relevant to consider the impact of implementation of AEOI on the secrecy provision under s 81 of the TAA.

In response to the G20's April 2009 call for action 'to make it easier for developing countries to secure the benefits of the new co-operative tax system environment, including a multilateral approach for the exchange of information',<sup>131</sup> the OECD and Council of Europe amended the Multilateral Convention and developed a Protocol<sup>132</sup>

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[2006] UKHL 53 [41].

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(2007) 23 NZIC 21, 616 (HC).

<sup>128</sup> The DIA gives effect to the Multilateral Convention to Implement Tax Treaty Measures to Prevent Base Erosion and Profit Shifting (MLI).

<sup>129</sup> As noted at n.16 above, the information collected and supplied is in a standard format.

(CRS) is a part of AEOI and ensures that the

<sup>130</sup> The MLI was signed by 68 jurisdictions (including New Zealand) on 7 June 2017 and has since been signed by a further 19 jurisdictions. The MLI entered into force for New Zealand on 1 October 2018 see OECD, 'Signatories and Parties to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting Status as of 23 January 2019,

effective from June 2011. The Protocol ensures that the Multilateral Convention is consistent with agreed international standards on exchange of information for tax purposes developed by the OECD Global Forum on Transparency and Exchange of Information for Tax Purposes<sup>133</sup> and opened the membership of the Multilateral Convention to non members of the OECD.<sup>134</sup> The Multilateral Convention is now a

signature to the Multilateral Convention, which entered into force for New Zealand on 1 March 2014 with effect from 1 July 2017. New Zealand has implemented AEOI and intends to complete its first information exchange under the regime by 30 September 2018<sup>140</sup>

The new AEOI international standard will result in significant amounts of tax information being shared regularly and automatically around the world and has been described as a significant step towards achieving global tax transparency by obliging those who are best able to identify the real persons hiding behind identities (mechanisms) widely used for tax evasion<sup>141</sup>. The AEOI standards are based on the United States' FATCA standard<sup>142</sup> and are designed to benefit all participating jurisdictions<sup>143</sup>.

It is a fundamental shift because it moves from a passive compliance to an active gathering and reporting. AEOI standards requires all financial institutions pursuant to due diligence standards to identify from their financial accounts those accounts that are held or controlled by non-residents. From these non-residents accounts financial institutions are required to collect CRS-compliant<sup>144</sup> identity, tax residency and financial information of the tax residents in reportable jurisdictions<sup>145</sup> and provide the information to the relevant revenue authorities<sup>146</sup>.

New Zealand has adopted a wider approach than a narrower due diligence procedure and the legislation requires financial institutions to report in eXtensible Markup Language (XML) format.

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decision of the court set the precedent for nondisclosure,<sup>158</sup> but the courts have moved away from the judgment, and an appropriate system for disclosure has not been introduced. The recent decision of the High Court in *Deputy Commissioner of Taxation v. Bunnell*<sup>159</sup> quashing section 17 notices is recognition that the pendulum has swung too far in favour of the tax authorities.

The counter argument against disclosure is that confidentiality is an essential feature of all tax authorities. Although the equivalent domestic laws are not as stringent as the DTA, they also do not allow for the dilution of confidentiality obligations.<sup>160</sup>

In substitution of the rigid rule set by the *Deputy Commissioner of Taxation v. Bunnell* case, Lord Caswell's principle in *Deputy Commissioner of Taxation v. Bunnell* is an appealing option.<sup>161</sup> The principle requires an assessment of documents by a judge to decide whether the disclosure would provide sufficient assistance to the appellant's case over the summary of information already provided. In addition, the 2017 OECD Commentary to the OECD MTC allows for the disclosure of information to the taxpayer when the judicial authorities allow it.<sup>162</sup>

It is arguable that when information is highly confidential or if there are no mechanisms to protect sensitive details, Baagwanth's approach in the *Deputy Commissioner of Taxation v. Bunnell* case<sup>163</sup>

