NEW ZEALAND BANKERS ASSOCIATION

Submission

to the

Inland Revenue Department

on the

Automatic Exchange of Information Common Reporting Standard

25 September 2014

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Submission by the New Zealand Bankers' Association to the Inland Revenue Department on the Automatic Exchange of Information Common Reporting Standard

About NZBA

1. NZBA works on behalf of the New Zealand banking industry in conjunction with its member banks. NZBA develops and promotes policy outcomes which contribute to a strong and stable banking system that benefits New Zealanders and the New Zealand economy.

2. The following fourteen registered banks in New Zealand are members of NZBA:
   - ANZ Bank New Zealand Limited
   - ASB Bank Limited
   - Bank of New Zealand
   - Bank of Tokyo-Mitsubishi, UFJ
   - Citibank, N.A.
   - The Co-operative Bank Limited
   - Heartland Bank Limited
   - The Hongkong and Shanghai Banking Corporation Limited
   - JPMorgan Chase Bank, N.A.
   - Kiwibank Limited
   - Rabobank New Zealand Limited
   - SBS Bank
   - TSB Bank Limited
   - Westpac New Zealand Limited.

Background

3. NZBA is grateful for the opportunity to submit in relation to the Automatic Exchange of Information (AEOI) initiative being advanced by the OECD and the G20.

4. NZBA commends IRD's ongoing commitment to meaningful consultation and engagement and appreciates the invitation to participate in this targeted consultation.

5. The following submission makes some brief comments on the AEOI Common Reporting Standard (CRS) in response to your email dated 29 August 2014.

6. If you would like to discuss any aspect of the submission further, please contact:

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Implementation Timing

7. NZBA's key concern is to ensure that the implementation date of the CRS is appropriate given the time and resources required for members to successfully implement a solution. In our view, following the standard tract to implementation is preferred as much more realistic than "fast tracking" implementation. Following the standard track will allow banks more time to prepare, develop internal systems and provide more leverage off equivalent experiences gained through the implementation of the FATCA regime.

8. It is critical that all the requirements are known well in advance of the implementation. The timing challenges, and the resulting uncertainty, that the industry was faced with for the FATCA implementation must be avoided. The legislative obligations are complex and require technical solutions so it is essential that sufficient time be provided to meet any new obligations.

9. Several of the NZBA member banks have parent banks based in Australia. We understand that at this stage it is anticipated that Australia will not join the early adopters group. From an administrative perspective, it would be advantageous for these banks to align the implementation with their Australian parent banks. However, in the event that Australia elects to join the group of early adopters, NZBA submits that the later adoption remains preferable as implementing after Australian parent banks will provide considerable assistance to the New Zealand subsidiaries, and would be significantly less problematic than trying to adopt before the parent banks.

10. Further, effective implementation of AEOI may not be possible within the early adopters' timeframe. This point is discussed further in relation to compliance costs below.

Compliance Costs

11. Our members have not had an opportunity to conduct a full analysis of the possible compliance costs in relation to the introduction of AEOI, but have provided some initial observations below. We would appreciate the opportunity to discuss these issues further once full analysis of these costs has been conducted.

12. Early feedback suggests that banks will look to use software integrated into their core banking system to comply with AEOI. Some banks are underway with significant projects to replace their core banking system and due to the size and timing of such projects, there is no way that these banks would be able to have an integrated AEOI solution in place should New Zealand join the early adopters group. Electing to implement AEOI early will require banks considering and implementing these system updates to develop interim, manual solutions at considerable additional cost.

13. In addition, many members intend to minimise compliance costs by leveraging on existing FATCA solutions, and early indications suggested that AEOI would be based

on the intergovernmental agreement (IGA) for FATCA. Therefore, NZBA considers the AEOI variations from FATCA outlined below will create the most significant compliance costs to banks.

Removal of Individual deminimus US$50,000 threshold

14. This change has possibly the most significant impact on compliance costs for banks. It will result in a substantial increase in the number of individual account holders needing to understand and self-certify their tax status in each of the participating tax authorities and a large increase in compliance costs for reporting NZFIs. An early estimate suggests that less than 10% of individual customers have more than US$50,000 in depository balances. On top of the increased tax authority catchment that at least the UK and Australia will have on NZFIs, this will have a significant impact on systems, staff and customers, along with associated costs. The large increased impact on the public, if not managed carefully, may have reputational impacts for the NZ government, Inland Revenue and reporting NZFIs.

15. An example of accounts that will be caught under this change are the large number of very low balance accounts (eg $0.01 or $4.00) that are not closed accounts but are generally inactive. This change brings these accounts into scope, and obtaining self-certifications from these customers will likely prove difficult.

Changing definition of Financial Institution (FI) and other entity classifications

16. While these definitions are may not affect the scope of banks and their related entities as Reporting FIs under AEOI, we foresee a material impact on banks' back-office reasonable determination processes and existing customers' self-certifications under FATCA. One possible option to save on implementation costs and bank entity customers' time and patience would be if FATCA self-certifications of Financial Institution, or IGA Annex II exclusions could be retained under AEOI definitions.

17. This suggested approach would save on compliance costs for Reporting FIs, but also assist New Zealand entity Account Holders in managing what could become an array of different classifications under different tax authorities. NZBA accepts that where entities are resident (or controlled by residents) in different tax jurisdictions, this will be necessary, but we submit that the FATCA IGA Annex II exemptions and FATCA FI definitions should wherever possible persist under AEOI.

Changing the reasonable determination procedures

18. Further to paragraphs 16 and 17 above, the AEOI removal of Reporting FIs being able to 'reasonably determine' new entities that are NZFIs/Partner jurisdictions FIs or Active NFFEs will most likely result in a substantial compliance cost and may impact upon customers, as many banks' systems and manual procedures will have to be altered to account for the additional scope of customers who would normally be reasonably determined under the FATCA requirements. It also creates operational complexity as there would need to be different processes for AEOI and for FATCA.

Enforcement Provisions

19. In relation to the design of an appropriate enforcement regime for the implementation of AEOI, we make the specific comments below.

Framework for thinking about enforcement of global AEOI in New Zealand

Relationship with FATCA

20. Although the model Competent Authority Agreements (CAA) and CRS for AEOI adopt a similar approach to the model IGA for FATCA, it should not be automatically assumed that the FATCA enforcement regime would be appropriate for AEOI.

21. The context and key drivers for New Zealand's adoption of AEOI are different from those for FATCA. New Zealand's participation in AEOI should be seen in the context of an international coordinated approach to countering tax evasion/avoidance and the benefits that New Zealand expects from it (i.e. information to facilitate the administration and collection of New Zealand taxes). In contrast, the New Zealand solution to FATCA was driven by the need to respond to pressure from the rules of one country, to prevent New Zealand financial institutions from incurring a prohibitive cost or being shut out of the US capital markets and with no (or little) expectation of reciprocal benefit to the New Zealand tax system.

22. There are differences between the coverage and the application of the due diligence and reporting rules in AEOI and FATCA. AEOI is much broader than FATCA. It involves multiple countries and envisages information exchange on a much bigger scale than FATCA. Its implementation will be by way of a series of separate bilateral or multilateral CAAs, which could result in differences in the way that AEOI applies as regards particular jurisdictions. There are also some significant technical differences between the IGA for FATCA and the CRS for AEOI.

23. These differences support the case for considering AEOI enforcement afresh without being constrained by the enforcement regime adopted for FATCA. FATCA enforcement relies on the existing offence provisions in sections 143 and 143A of the Tax Administration Act 1994 (TAA) and linking them with the new operative provisions in Part 11B. While some of those provisions may be appropriate for AEOI (for example, the avoidance provision in section 185L may be sufficient to meet CRS requirements), New Zealand should take advantage of the opportunity to design an enforcement regime that is fit for purpose.

Conforming with international standards

24. We accept that New Zealand's enforcement regime must conform with international standards to signal to the international community its commitment to AEOI. There is, however, no advantage to be gained from going above and beyond the international standard. In this regard, New Zealand should strive to be a follower, not a leader.

Comments on the potential scope of the AEOI enforcement regime

Proactive, but risk-based, enforcement

25. AEOI appears to require greater and more proactive involvement by domestic tax authorities in enforcement than FATCA. Under Section IX of the CRS, New Zealand will be required to have rules and administrative procedures in place to ensure effective implementation of AEOI, including:

- rules to prevent adoption of practices intended to circumvent the CRS;
- rules requiring reporting financial institutions to keep records of steps undertaken and evidence relied on for performance of due diligence procedures in the CRS and to obtain such records;
- administrative procedures to verify financial institutions' compliance with reporting and due diligence procedures in the CRS, and follow up on undocumented accounts;
- administrative procedures to ensure non-reporting financial institutions and excluded accounts continue to have low risk of being used to evade tax; and
- effective enforcement provisions to address non-compliance.

26. As a practical matter, we consider that the periodic verifications of compliance required by AEOI should be undertaken as part of Inland Revenue's current risk-based approach to audits. Given a risk-based approach, we do not think that there should be a separate annual inquiry or review of every financial institution. An annual inquiry/review approach would have to be balanced against the high compliance and administrative costs that it would entail for financial institutions and the Inland Revenue.

Penalties commensurate with AEOI objectives

27. When considering what penalties should be imposed for non-compliance with AEOI, it is important to bear in mind that the immediate objective of AEOI is to gather information, not to collect taxes (albeit that the information collected pursuant to AEOI will be used in the administration and collection of taxes). We expect that each jurisdiction that participates in AEOI will already have its own enforcement regime for the collection and payment of taxes. Accordingly, the penalties regime for AEOI should be viewed differently from the existing penalties regime that underpins the rest of the tax statutes. We consider that a separate line of lesser offences and penalties for AEOI may be more appropriate.

28. In the context of FATCA, the criminal offences provisions in sections 143 and 143A of the TAA were considered to be broad enough to cover most aspects of non-compliance. Officials recommended (contrary to submissions) that those provisions be extended further to cover other aspects of non-compliance (i.e. failure to register) on the basis that it would be incoherent to have criminal penalties for some aspects of non-compliance and civil penalties for others.

29. As discussed above, AEOI offers the New Zealand Government the opportunity to consider afresh its approach to enforcement. We consider that civil penalties in the form of fines would be more appropriate for AEOI and recommend that officials be

asked to give it serious consideration. The OECD commentary on Section IX of the CRS contemplates imposition of fines or other penalties and does not require criminal sanctions. The imposition of fines would also be consistent with the UK approach to FATCA penalties.

30. Furthermore, we consider that enforcement actions should not be taken without prior engagement. Non-complying persons should be notified of the alleged non-compliance and given a reasonable timeframe to remedy it before they suffer the full force of the enforcement regime.

Inclusion of reasonableness/materiality standard

31. Compliance with AEOI is arguably more onerous for New Zealand financial institutions than compliance with FATCA because of the multiple jurisdictions involved and the possibility of variations in the CAAs. The sheer volume of information to be collected and reported also increases the risk of errors.

32. Accordingly, we consider that there is an even stronger case for inclusion of a reasonableness/materiality standard in the context of AEOI than for FATCA. Given the complexity and scope of AEOI, a strict liability regime may be too idealistic and unrealistic. In this regard, we note that, even in the context of FATCA, the UK approach allowed an exemption from enforcement where there was a reasonable excuse for non-compliance.

Extending enforcement regime beyond financial institutions

33. Officials should consider shifting some of the obligations (and hence penalties for non-compliance) onto account holders rather than financial institutions. For example, imposing an obligation on account holders to validly self-certify would bring self-certification within the enforcement regime and shift the general burden of responsibility for accuracy of such information to the account holder and away from the financial institution. This approach is suggested by the commentary to the CRS and seems to us to be fairer than the FATCA enforcement regime which focuses solely on financial institutions. As a consequence, officials should give some thought to each stage of the AEOI compliance process and consider who should bear the obligation for complying with it.

Co-ordination with Inland Revenue's Business Transformation project

34. As a final comment, we note that if possible the design of the AEOI enforcement regime should be considered in tandem with any changes to the TAA proposed as part of Inland Revenue's business transformation project, in order to minimise the costs of systems and process changes for financial institutions.