18 February 2019

Ministry of Foreign Affairs and Trade
Via email: UKFTA@mfat.govt.nz

Dear Sir / Madam

UK-NZ FREE TRADE AGREEMENT

About the Corporate Taxpayers Group

The Corporate Taxpayers Group ("Group") is a group of over 40 of New Zealand's largest businesses. Most of these depend, to some degree, on international trade and/or investment for their prosperity. And collectively, their ability to compete in the world is strongly linked to New Zealand's prosperity and the wellbeing of its people.

The Group contributes to the development of tax policy, and to enhancements in tax administration, with a particular focus on issues of significance to large businesses that compete internationally. Further information about the Group is set out in the Appendix.

The Group welcomes the Ministry's call for submissions on preparing for a future Free Trade Agreement with the United Kingdom ("UK FTA"). Consistent with its mandate, the Group, in this submission, will address only tax-related issues of relevance to a UK FTA (and to trade policy more broadly). The Group expresses no view on other issues (including the specific questions listed on the Ministry's website) since we understand that affected members of the Group may make their own submissions on specific matters affecting them.

Why tax policy is relevant to trade policy

International trade and investment may result in a business being taxed in more than one country on the same income. This so-called "double tax" has long been recognised as a potentially significant barrier to international trade and investment.

Countries have sought to avoid this barrier by concluding double tax agreements ("DTAs") with trading partners. DTAs reduce barriers to international commerce in two ways:

- First, they reflect a framework for determining the circumstances in which a country will tax an enterprise that is resident in the other country. An example is the concept of permanent establishment ("PE"). Under most of New Zealand's DTAs, so long as an exporter's dealings do not result in a PE in the country where its customers are located, the exporter can generally trade with that country without being subject to income tax (and the resulting compliance obligations) in that country. This aspect of DTAs is critical not only to avoiding double tax, but also to affording exporters a high degree of certainty that selling goods to a country without having a PE in that country should not in itself result in the country of import taxing the exporter's income.

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We note the views in this document are a reflection of the views of the Corporate Taxpayers Group and do not necessarily reflect the views of individual members.

- Second, they contain mechanisms for relieving double tax in cases where income would otherwise be subject to tax in both countries.

First submission: the Ministry should note that recent and possible future changes in New Zealand's domestic tax laws may increase the extent to which tax is a barrier to international trade and investment and should actively monitor such developments

Until recently, it could be assumed that the risk of double tax, although not completely eliminated, had been substantially mitigated by a combination of New Zealand's DTA network (which extends to almost all our major trading partners) and domestic laws that tax international commerce generally in accordance with international norms.

Recent developments suggest that that assumption may no longer hold. New Zealand has embarked on reforms to its domestic law which in some cases override, or depart from, the rules and norms reflected in the DTAs New Zealand is party to. The motive for these reforms (to ensure that multinationals pay a "fair share" of tax) has no doubt attracted political support. But the consequences of reforms that override DTAs or depart from existing international practice may be far-reaching, and could lead to unintended and negative consequences for New Zealand exporters.

One example of such developments is the possibility of New Zealand implementing a digital services tax, similar to proposals being considered by some EU countries (including the UK) but strongly resisted (including on the grounds it would breach WTO rules) by the United States.[1] It is not clear if New Zealand has reached its own view on whether such a tax would breach New Zealand's obligations under DTAs and/or trade-related agreements.

What does seem clear is that a digital services tax would raise relatively little revenue for New Zealand, is at least at risk of breaching our international obligations, and has nothing going for it from a tax policy perspective except that it might seem "unfair" to some commentators not to follow similar measures that some other countries are pursuing.

Because the UK itself proposes to implement a digital services tax, it might be argued that there is no reason (at least in the context of preparations for a UK FTA) for New Zealand not to do so. Looked at in that narrow sense, that may be so.

But the broader significance of a digital services tax is that it is a first step in the direction of taxing income from exports in the destination country. Currently, the profits from exporting goods or services to another country are generally not taxed in the other country. For that to change would have significant implications for New Zealand, which need to be carefully considered before introducing this new tax on international commerce.

These tax policy developments are important to the Ministry's work, because if tax policies result in increased barriers to international trade, this will partially undo the gains to New Zealand from reductions in (non-tax) trade barriers under FTAs the Ministry negotiates.

It is no answer to this concern to say that some other countries are similarly amending their tax laws in ways that increase barriers to trade and investment. New Zealand has (appropriately) maintained its commitment to reducing trade barriers even in the face of more protectionist trade policies by some countries. It is critical at this time that that commitment not be undermined by our tax policy and tax treaty policy.

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[1] Letter from Orrin G. Hatch (Chairman of the U.S. Senate Committee on Finance) and Ron Wyden (Ranking Member of the U.S. Senate Committee on Finance) to the Honorable Donald Tusk (President of the European Council) and the Honorable Jean-Claude Juncker (President of the European Commission) regarding the European Commission proposal to introduce a digital services tax (18 October 2018) (see https://www.finance.senate.gov/imo/media/doc/2018-10-18%20OGH%20RW%20to%20Juncker%20Tusk.pdf).

Second submission (of particular relevance to the UK FTA as well as the (more advanced) work on the EU FTA): New Zealand's DTA with the UK, as well as our DTAs with other major European countries (in particular Germany and France) are outdated relative to the upgraded DTAs that other countries (especially Australia) have.

Australia is a potential competitor for our trade with the UK and EU, and is/will be negotiating FTAs with the EU and UK with similar timing to our own negotiations. So for New Zealand's DTAs with UK, Germany and France to be inferior to (ie, provide less relief from double tax than) Australia's, risks being an extra barrier for New Zealand businesses, thereby partially undoing whatever benefits the Ministry's trade negotiators are able to secure under New Zealand's FTAs with the UK and EU.

It should therefore be a priority for New Zealand to conclude revisions to those DTAs which further reduce the risk of double taxation, in line with the upgraded DTAs that Australia has concluded with those same countries. While we understand that New Zealand is currently negotiating a protocol to the DTA with the UK, consideration of the UK FTA should bring new impetus to concluding those negotiations.

For your information, the members of the Corporate Taxpayers Group are:

1. AIA Sovereign
2. Air New Zealand Limited
3. Airways Corporation of New Zealand
4. AMP Life Limited
5. ANZ Bank New Zealand Limited
6. ASB Bank Limited
7. Auckland International Airport Limited
8. Bank of New Zealand
9. Chorus Limited
10. Contact Energy Limited
11. Downer New Zealand Limited
12. First Gas Limited
13. Fisher & Paykel Appliances Limited
14. Fisher & Paykel Healthcare Limited
15. Fletcher Building Limited
16. Fonterra Cooperative Group Limited
17. Genesis Energy Limited
18. IAG New Zealand Limited
19. Infratil Limited
20. Kiwibank Limited
21. Lion Pty Limited
22. Meridian Energy Limited
23. Methanex New Zealand Limited
24. New Zealand Racing Board
25. New Zealand Steel Limited
26. New Zealand Superannuation Fund
27. NZME Limited
28. Pacific Aluminium (New Zealand) Limited
29. Powerco Limited
30. Shell New Zealand (2011) Limited
31. SKYCITY Entertainment Group Limited
32. Sky Network Television Limited
33. Spark New Zealand Limited
34. Summerset Group Holdings Limited
35. Suncorp New Zealand
36. T & G Global Limited
37. The Todd Corporation Limited
38. Vodafone New Zealand Limited
39. Watercare Services Limited
40. Westpac New Zealand Limited
41. WSP Opus
42. Xero Limited
43. Z Energy Limited
44. ZESPRI International Limited

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Yours sincerely

John Payne

John Payne
For the Corporate Taxpayers Group

CC: Carmel Peters, Cath Atkins, David Carrigan & Emma Grigg, Inland Revenue
James Beard, The Treasury

APPENDIX

ABOUT THE CORPORATE TAXPAYERS GROUP - INFORMED, PRINCIPLED, PRACTICAL

The Corporate Taxpayers Group is an organisation of major New Zealand companies whose objective is to pursue the principled interests of its members in the tax policy sphere. The Group has a number of principles by which it judges tax policy issues and believes that a good tax system for New Zealand should be built around these principles. These principles are set out below:

- *High certainty and low business risk:* For the corporate sector, tax is not just a cost of doing business but is also a very significant risk. Funds are raised, staff hired, and investments made on the basis of expected returns to corporate shareholders / owners. If tax rules increase business risk by creating uncertain or unexpected tax outcomes then the rate of return on investment has to be higher to compensate for this. Higher required rates of return mean less investment and fewer jobs, to the detriment of the economy. To lower business risks caused by the tax system, tax rules need to be as certain as possible and they need to be administered and interpreted by the Inland Revenue consistently and speedily. Having a high level of certainty over the medium to long term is of high importance to the Group.

- *Low compliance costs*: Compliance costs imposed by the tax system are an economic cost. Those resources would be better employed creating jobs and raising the wealth of New Zealand.

- *Positive contribution*: The tax system plays a significant role in society and has the ability to contribute to the overall welfare and wellbeing of New Zealand and New Zealanders. Any changes to the tax system should focus on building and utilising the collective human, social, natural and financial capital of New Zealand, and should also make a positive contribution to New Zealand.

- *International competitiveness, especially with Australia*: Taxes are a significant cost of doing business. The higher those costs are in New Zealand relative to other countries, the higher the relative costs of doing business in New Zealand. That flows through to less investment, fewer jobs and lower wealth. New Zealand's tax system plays a critical role in our competitive position with our major trading partners and competitors. In addition to attracting foreign investment, a competitive tax system is one that ensures that New Zealand is attractive as a base for outbound investment. While New Zealand businesses compete with the rest of the world for investment funding, markets and skilled workers, Australia is our nearest and most significant competitor. For that reason the Group considers that the New Zealand tax system should set as a minimum benchmark, a system that provides a business environment at least as good as that which exists in competing countries, especially Australia.