

White Paper - N°6

NZ Foreign Trust and Look Through Company Regimes

New Zealand is a common law country that has a long standing and mature trust and foreign trust industry.

Trusts are extensively used for asset protection, tax planning and trading purposes. New Zealand Trust legislation, the Trustees Act 1956, is modelled on the United Kingdom Trust Legislation, the Trustees Act 1925, with some departures. It is possible to use a corporate trustee as the trustee of the Trust which offers greater flexibility and separates control further from the settlor.

The term Settlor is very broadly defined and includes anyone who provides services or goods to the Trust for less than a market value.

Taxation of New Zealand Foreign Trusts

New Zealand is generally perceived as a country with a robust tax system levying high taxes on its residents. However this analogy does not apply to taxation of New Zealand Foreign Trusts (NZFT's). New Zealand determines whether the income of the Trust is taxable by reference to the residence of the settlor. This means that a Trust with a foreign resident settlor is not subject to New Zealand tax, except on the income derived from a New Zealand source. This would be the case even if the Trustees were resident in New Zealand.

New Zealand tax legislation taxes income of a Trust either at the level of the Trust, as Trustee income, or at the level of the Beneficiary, as Beneficiary income. Income retained in the Trust is taxed as Trustee Income, whereas income distributed to a Beneficiary is taxed as Beneficiary Income. Accumulated earnings in the Trust which have been previously classified as Trustee income that are subsequently distributed to beneficiaries are referred to as Taxable Distributions.

Whilst this all may sound complex the taxation of NZFT's is fairly simple. Foreign sourced trustee income is not subject to New Zealand income tax. Beneficiary foreign sourced income that is distributed to New Zealand non-resident beneficiaries is not subject to New Zealand income or withholding tax. Taxable distributions made by NZFT's to New Zealand non-resident beneficiaries are not subject to New Zealand income or withholding tax. This taxation treatment applies to foreign sourced income only. It is recommended that NZFT's do not have New Zealand sourced assets settled on the Trust or derive New Zealand sourced income as that would be subject to New Zealand tax.

In summary a New Zealand non-resident beneficiary will not be liable to tax in New Zealand on any distribution from a NZFT unless it is from a New Zealand source. Similarly a New Zealand resident trustee will not be liable to New Zealand tax on income of a NZFT unless it is from a New Zealand source.

These popular vehicles are also often set up by persons wanting to migrate to NZ at some stage, as they, if used correctly can facilitate asset transfer to NZ without a NZ tax impost, thus mitigating migrant tax exposure.

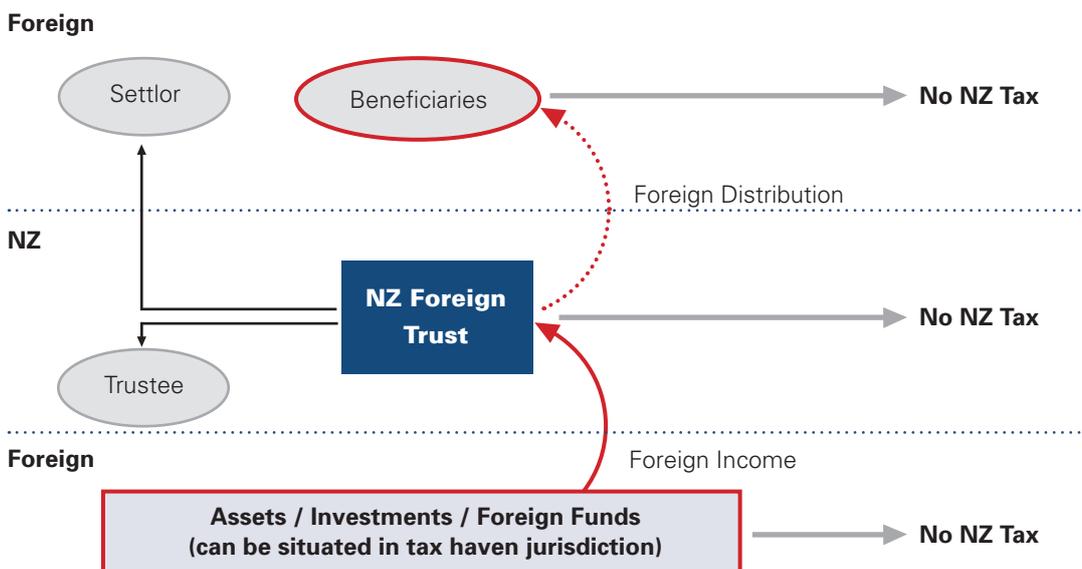
Tax Residence of a Trust

The residence of a Trust for tax purposes is determined by the residence of the Trustees, regardless of whether the income of the Trust is or is not liable to New Zealand tax due to the residence of the Settlor. This is the very reason why NZFT's are very popular vehicles for tax planning and asset protection. There is no central registry of Trusts in New Zealand therefore these vehicles offer a degree of privacy/ secrecy.

Application Of Double Tax Treaties

If a NZFT has trustees that are all resident in New Zealand, the possibility is raised of applying double tax treaties, regardless of whether the foreign sourced income earned by the NZFT is liable to tax in New Zealand. It should be noted that double tax treaties are not the same, thus the treatment of Trusts may vary from treaty to treaty. In general, NZFT is considered to be "Subject to tax" in New Zealand, consequently it would be eligible to benefit under the treaties yet not be liable to tax in NZ. As a result a NZFT can operate as an offshore trust without the negative stigma that is often associated with Offshore Entities. The advantage is that NZ is not considered a tax haven or a bad country, quite the opposite. A NZFT offers the advantages of an offshore entity with the convenient residency in a high tax country.

VISUAL REPRESENTATION OF A NZFT



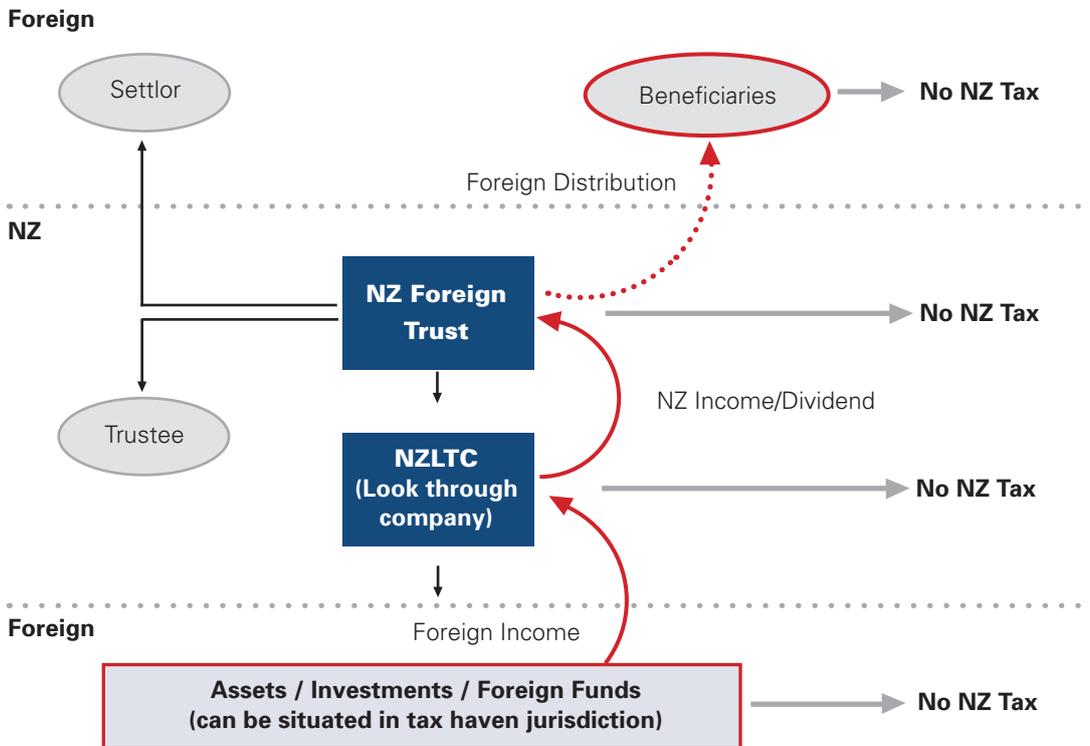
New Zealand Look Through Companies

A New Zealand Look Through Company (NZLTC) is a company incorporated in New Zealand. Upon incorporation it is entered into the register of companies. It is a separate legal entity providing limited liability to its owners. Its capital is divided into shares. A NZLTC is a transparent vehicle for New Zealand tax purposes akin to the US LLC. This is another useful vehicle that is finding traction with foreign owners. As opposed to Limited Partnership an owner can be the shareholder and the director of a NZLTC. There are a few criteria that have to be met with NZLTC's; such as that there can be only class of shares with the same rights, shareholders can be natural persons, another NZLTC, a Trust, or can be a NZFT. NZLTC's must be resident in New Zealand and cannot be non-resident by virtue of application of a double tax treaty. Directors of NZLTC must be natural persons and cannot be corporate directors.

Taxation of the NZLTC

NZLTCs are treated as transparent for tax purposes and follow partnership taxation. Where the shareholders of NZLTC are individuals, tax resident outside New Zealand or New Zealand resident Trustees of a NZFT, then the shareholders will not be liable to New Zealand income tax on their foreign sourced income or any withholding tax at the time the dividend is distributed to its shareholders. NZLTCs work well in combination with the NZFT's. At times it may be beneficial for the owners to have a company interposed between the underlying investments in the source country and the NZFT. A good reason for this could be a requirement of the settlor in a NZFT to further distance himself from the underlying assets of the NZFT. NZLTC's, just like NZFT's, provide a flow through tax treatment with addition of limited liability.

VISUAL REPRESENTATION OF A TYPICAL NZLTC STRUCTURE



Conclusion

New Zealand's Foreign Trust regime is a robust industry and is becoming more and more popular with foreign settlors. NZFT's offer a flow of income through the New Zealand vehicle that is not liable to New Zealand income or withholding tax on foreign sourced income. The residency of NZFT, which is determined by reference to the Trustees, provides a residency in a high tax country and possibility of the application of double tax treaties. New Zealand Look Through Companies are a good alternative to US LLC's which can complement the NZFT structures quite well. Both of these entities therefore become good alternatives, whether alone or in combination, to vehicles established in classical tax haven countries.

On a final note, New Zealand is not classified as an offshore jurisdiction that is blacklisted for tax purposes. It has a sound legal and regulatory system, thus becoming a viable alternative to offshore jurisdictions.

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Our clients tell us that they value our commercial experience and our ability to cut through to the heart of the matter. They appreciate our strategic insight and they value our ability to come up with creative solutions to difficult problems. They are reassured by our grasp of the technical detail – based on years of experience, together with the latest research. They rely on us to maintain oversight of their strategy implementation and to let them know when they've drifted off course. And they enjoy our fresh, straight-forward approach.

We pride ourselves on giving you specialist commercial and taxation advice in everyday language. We keep it simple. We don't beat around the bush.

We understand the technical issues, and we use plain English to make sure you understand them too, so you can make sensible, well-founded decisions about your business, your family, and your future.

We are Chartered Accountants and members of NZICA, so you can be assured that our advice is dependable.

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