# International treaty examination of the Agreement between the Government of New Zealand and the Government of the Socialist Republic of Viet Nam for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income

Report of the Foreign Affairs, Defence and Trade Committee

**Contents**

# Agreement between the Government of New Zealand and the Government of the Socialist Republic of Viet Nam for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income

## Recommendation

The Foreign Affairs, Defence and Trade Committee has conducted an international treaty examination of the Agreement between the Government of New Zealand and the Government of the Socialist Republic of Viet Nam for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, and recommends that the House take note of its report.

### Reasons for the agreement

Viet Nam is New Zealand's 24th-largest trading partner. Both countries are parties to the ASEAN–Australia–New Zealand Free Trade Agreement, and are in the process of negotiating the Trans-Pacific Partnership Agreement; the lack of a double taxation agreement with Viet Nam is a key gap in our tax treaty network. Australia has had such an agreement with Viet Nam since 1992.

No agreement had previously been reached on this matter because Viet Nam sought a tax-sparing clause in the agreement, something New Zealand prefers not to include in its tax treaties to prevent opportunities for tax avoidance. Tax-sparing is a process whereby a tax credit from one party offsets a tax exemption granted by the other. It has now been agreed that New Zealand will provide Viet Nam with a tax sparing arrangement limited to ten years' duration, subject to anti-avoidance measures. We were told this was consistent with New Zealand's Double Taxation Agreement with Singapore.

There is expected to be little or no cost to the proposed agreement. The only cost to New Zealand would be in the form of loss of dividends, interest, and royalties, which are small as New Zealand's investment in Viet Nam is low, and there will be some off-setting in the form of tax exemption for New Zealand.

### Exchange of information

To help prevent tax avoidance and evasion, New Zealand generally seeks to exchange information about all types of taxes with other countries. Viet Nam has only ever exchanged income tax information with other countries, and this position is reflected in this agreement. This is not New Zealand's preference, but the agreement does have a "most favoured nation" clause, which obliges Viet Nam to enter into negotiations with New Zealand should it enter into an agreement with another nation that allows other tax information to be exchanged.

## Tax for students

A Vietnamese resident studying in New Zealand with a job related to the course of study, under article 20 of the agreement, in some circumstances, is not liable for income tax. The period worked must not exceed 183 days in a 12-month period. The clause is unusual. New Zealand has agreed to it because its inclusion is important to Viet Nam. We are assured by the Inland Revenue Department that this will not create a loophole allowing a student visa to be misused as a work visa.

## Conclusion

We support the proposed double taxation agreement. The national interest analysis for the agreement is appended to this report.

# Appendix A

### Committee procedure

The agreement was referred to the committee for examination on 9 September 2013. We met on 26 September and 24 October 2013 to hear evidence and consider it. We heard evidence from the Inland Revenue Department.

### Committee members

John Hayes (Chairperson)
Hon Phil Goff
Dr Kennedy Graham
Hon Tau Henare
Dr Paul Hutchison
David Shearer
Lindsay Tisch

# Appendix B

## National Interest Analysis –– Double Tax Agreement with Viet Nam

### 1. Executive summary

1.1 On 5 August 2013, New Zealand signed the Agreement between the Government of New Zealand and the Government of the Socialist Republic of Viet Nam for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, and Protocol (collectively, the Viet Nam DTA).

1.2 Double tax agreements (DTAs) are bilateral international treaties that are principally designed to encourage growth in economic ties between countries. They do this by reducing tax impediments to cross-border services, trade and investment. New Zealand has 37 DTAs in force, primarily with its major trading and investment partners. The authorisation to negotiate and give effect to DTAs comes from section BH 1 of the Income Tax Act 2007.

1.3 Consistent with the Government's DTA Strategy it is important for New Zealand to maintain a competitive DTA network with its main trade and investment partners in order to retain and grow internationally competitive companies. Viet Nam has been identified as one of the key gaps in the New Zealand tax treaty network. This gap has been further highlighted by the ASEAN-Australia-New Zealand Free Trade Agreement (AANZFTA), coming into force in 2010 (both New Zealand and Viet Nam are party to it), and the progress towards concluding the Trans-Pacific Partnership (TPP) Free Trade Agreement. Australia, by comparison, has had a DTA with Viet Nam since 1992. New Zealand has already concluded DTAs with five other key trading partners in the ASEAN region – namely Singapore, Thailand, Philippines, Indonesia and Malaysia.

1.4 Viet Nam is New Zealand's 24th largest trading partner (goods) and 13th largest within Asia. Education, tourism and consultation services are an increasingly important component of the economic relationship (Viet Nam was the ninth-largest source of international students in New Zealand in 2012). Opportunities are also now arising in areas such as clean technology and environmental management, agribusiness and the aviation sector. In addition, there are sizeable investments in the dairy, timber and education sectors in particular, with the prospect of future increases in outbound direct investment and foreign direct investment between New Zealand and Viet Nam.

1.5 DTAs are not just about eliminating double taxation. In the absence of a DTA, New Zealand generally relieves double taxation of its residents on a unilateral basis. However, DTAs provide a more principled and comprehensive basis for doing so, and enable the revenue cost to be shared. They also provide other advantages that can reduce the compliance cost and cash-flow implications of cross-border economic activity and enable business decisions to be made with greater certainty. For these reasons, DTAs generally tend to be favoured by business interests and other key stakeholder groups. The New Zealand Embassy in Ha Noi and Consulate/New Zealand Trade and Enterprise in Ho Chi Minh City receive regular enquiries from New Zealand businesspeople regarding the existence of a bilateral DTA.

1.6 The Viet Nam DTA is broadly consistent with New Zealand's other recent DTAs, and will be a good precedent for future DTA negotiations. However, as in all negotiations, some compromises were made by both countries. For New Zealand, the key compromise was the agreement to include a tax-sparing mechanism in the treaty. Tax sparing provisions were once a common feature of DTAs between developed and developing countries. The developed country would agree to provide a tax credit for tax deemed to be paid in the developing country, but not actually paid because of a tax exemption intended to attract foreign investment. While New Zealand stopped providing tax-sparing provisions some years ago, for tax policy reasons, recent changes to New Zealand's international tax rules (which result in foreign dividends received by companies no longer being taxed) mean that tax sparing is now a less significant concern for New Zealand. The mechanism will apply to dividends, interest, and royalties paid from a Viet Nam source to a New Zealand resident. This mechanism does not apply where the New Zealand resident is a financial institution, and contains an anti-avoidance provision to prevent abuse. The mechanism will terminate after a 10-year period.

## 2. Nature and timing of the proposed treaty action

2.1 The proposed treaty action is to bring the Viet Nam DTA into force through an exchange of diplomatic notes that confirm the completion of the respective constitutional and legal requirements for entry into force by each country, pursuant to Article 27 of the Viet Nam DTA.

2.2 Before the treaty action is taken, the Viet Nam DTA must successfully undergo Parliamentary treaty examination, in accordance with Parliament's Standing Order 394, and must successfully be given the force of law in New Zealand by an Order in Council made pursuant to section BH 1 of the Income Tax Act 2007.

## 3. Reasons for New Zealand becoming Party to the treaty

### General reasons why New Zealand enters into double tax agreements

3.1 New Zealand began entering into double tax agreements (DTAs) in 1947, and currently has a network of 37 DTAs in force, predominantly with its main trading and investment partners.

3.2 DTAs are bilateral international treaties that are principally designed to encourage growth in economic ties between countries. They do this by reducing tax impediments to cross-border services, trade and investment. The major impediment is double taxation. As explained below, DTAs allocate taxing rights and reduce withholding taxes. Entering into a DTA therefore results in a prima facie revenue cost to New Zealand. However, the expectation is that a DTA will create a more favourable economic environment that will foster an increase in cross-border income-earning activity.

3.3 At a practical level, DTAs are complex technical documents that provide an interface between two, often conflicting, tax systems. Despite their complexity, DTAs are generally favoured by all of the key stakeholder groups that are involved in cross-border economic activity:

Taxpayers – A primary concern for any taxpayer contemplating entering into commercial or employment activity in another jurisdiction is that they must comply with the tax and other legal obligations of two separate jurisdictions. This can be perplexing, and obtaining professional advice or tax rulings can be costly and time consuming. Unique issues also arise from cross-border activities, ranging from complex matters such as transfer pricing disputes, to more mundane considerations such as whether taxes paid in the other jurisdiction are creditable against home jurisdiction tax. DTAs help alleviate many of these problems. They establish a framework for the taxation of cross-border activity, prohibit discriminatory taxation, and establish a low-cost mechanism for taxpayers to raise concerns if they do not consider that the treaty is being correctly applied or interpreted.

Investors – Investing across an international border always involves risk. Specific risks arise in respect of tax because of the inherent complexity of tax laws, which can lead to uncertainty as to the actual tax outcome. Tax laws can also change suddenly in some jurisdictions. DTAs assist investors by specifying the maximum rates of tax that can be applied to dividends, interest and royalties. These "headline" rates reduce compliance costs for investors by making it easier to determine the after-tax returns on potential investments. The tax rates are also "locked in" by the treaty, which means that investors can make business decisions with greater confidence. To encourage greater inward investment, New Zealand has unilaterally reduced withholding taxes on certain returns from inbound investment. However, lowering tax rates in a bilateral treaty setting ensures that the rates are also reduced on a reciprocal basis by the treaty partner. This provides benefits to domestic investors.

Governments – As double taxation distorts business decisions and generally hinders cross-border economic activity, most jurisdictions unilaterally relieve double taxation of their tax residents. For example, New Zealand tax legislation relieves double taxation by allowing tax residents who derive foreign-sourced income, to credit the foreign tax paid against their New Zealand tax liability. However, DTAs provide more comprehensive relief from double taxation than is possible unilaterally, and allow the cost of relieving double taxation to be shared. They do this by allocating taxing rights between the jurisdictions concerned, on the basis of internationally accepted principles. In addition, most countries tax their residents on income earned worldwide. International cooperation between tax authorities is therefore needed to enable tax authorities to verify that income earned in other countries is reported correctly by tax residents. DTAs facilitate this by authorising the exchange of tax-related information (such as tax records, business books and accounts, bank information and ownership information). The exchanged information assists tax authorities to detect and prevent tax evasion and tax avoidance.

3.4 The Organisation for Economic Co-operation and Development (OECD), has assumed a leading role in promoting the use of DTAs as a way of contributing to the expansion of world trade and developing the world economy. The OECD has produced a Model Tax Convention, and a comprehensive commentary, for member and non-member countries to use as a basis for concluding DTAs. As a member of the OECD, New Zealand is subject to an express recommendation issued by the OECD Council in 1997[1] for all member countries:

> *… to pursue their efforts to conclude bilateral tax conventions … with those member countries, and where appropriate with non-member countries, with which they have not yet entered into such conventions …*

[1] The recommendation follows similar OECD Council recommendations that have been in place since before New Zealand joined the OECD.

### Specific reasons for the double tax agreement with Viet Nam

3.5 New Zealand primarily enters into DTAs with countries with which it has a significant existing or potential economic relationship. Consistent with the Government's DTA Strategy it is important for New Zealand to maintain a competitive DTA network with its main trade and investment partners in order to retain and grow internationally competitive companies. DTAs can also be entered into to exploit a particular opportunity, or to address particular taxation problems.

3.6 The lack of a DTA with Viet Nam has been one of the key gaps in New Zealand's tax treaty network, particularly given the growing economic relevance of the Asian region to New Zealand. New Zealand already has DTAs with the other five major ASEAN nations. A DTA with Viet Nam will be an important part of the "connectivity" architecture that New Zealand seeks to put in place in its home region. This is recognised in the NZ Inc ASEAN Strategy, which was publicly launched by the Prime Minister on 5 August 2013.

3.7 Investment between New Zealand and Viet Nam, in either direction, is still not high. However, the two-way goods trade rose 20 per cent between 2010 and 2012 to NZ$777 million, with services trade in 2012 adding a further NZ$69 million[2]. This makes Viet Nam New Zealand's 24th largest trading partner (goods), and 13th largest within Asia. Education, tourism and consultation services are already an increasingly important component of the economic relationship (Viet Nam was New Zealand's 10th largest source of international students in 2011), but additional opportunities are now arising in areas such as clean technology, environmental management, agribusiness and aviation. The entry into force of the ASEAN-Australia-New Zealand Free Trade Agreement (AANZFTA), to which both New Zealand and Viet Nam are party, has given rise to fresh opportunities to increase bilateral trade, particularly in services. The two countries will further cement their relationship in the Trans-Pacific Partnership (TPP) free trade agreement, which is currently in the last stages of negotiation. The TPP is expected to deliver a much more liberalised framework for cross- border services and investment that will underpin the expansion of our trade and economic relationship.

3.8 The lack of a DTA has been further highlighted by the fact that Australia has had a DTA with Viet Nam since 1992. This has meant that New Zealanders engaged in income-earning activities in Viet Nam have in some cases been operating at a competitive disadvantage vis-à-vis Australian residents.

3.9 New Zealand has previously held back from entering into DTA negotiations with Viet Nam because of that country's strict requirement for tax-sparing concessions from their DTA partners. New Zealand, by contrast, has had a strong preference for not including tax-sparing concessions in DTAs.

3.10 Tax-sparing provisions were once a common feature of DTAs between developed and developing countries. The developed country would agree to provide a tax credit for tax deemed to be paid in the developing country, but not actually paid because of a tax exemption intended to attract foreign investment. Many countries, including New Zealand, stopped including tax-sparing provisions in their DTAs some years ago, for tax policy reasons (including concerns about their use in tax avoidance schemes).

[2] New Zealand's main exports to Viet Nam are dairy products, timber and timber products. Vietnamese imports have been mainly in phosphates, furniture, petroleum, nuts, footwear, telecom handsets, coffee and crustaceans.

3.11 Recent changes to New Zealand's international tax rules (which result in foreign dividends received by companies no longer being taxed) mean that tax sparing is now less of an issue for New Zealand. Tax-sparing provisions have been included in some recent DTAs, most recently in the Papua New Guinea DTA signed in October last year. Given these developments, New Zealand is no longer constrained from concluding a DTA with Viet Nam. The Viet Nam DTA includes the tax-sparing provisions requested by Viet Nam, but also includes a number of anti-abuse rules proposed by New Zealand. Moreover, the tax-sparing provisions will automatically terminate after a 10-year period.

## 4. Advantages and disadvantages to New Zealand of the treaty entering into force and not entering into force for New Zealand

4.1 As a bilateral instrument, the Viet Nam DTA necessarily involves trading-off advantages and disadvantages. However, on balance, entering into the Viet Nam DTA is expected to be in New Zealand's overall interests.

### Advantages of the treaty entering into force

4.2 A key advantage of the Viet Nam DTA is that New Zealanders engaging in cross-border income-earning activities can operate on an even footing with competitors from countries such as Australia, that already have the protection of a DTA. It also closes a perceived gap in New Zealand's network of DTAs with its main trading and investment partners.

4.3 The general advantages of the Viet Nam DTA can be summarised as follows:

- The DTA will reduce tax impediments to cross-border activities and transactions (such as services, trade and investment). For example, in some circumstances the DTA will only permit one country to tax a particular transaction, thereby reducing compliance costs and providing cash-flow advantages to the parties to the transaction.
- The reduction in tax impediments is likely to foster increased bilateral economic activity that will benefit New Zealand in terms of employment and business opportunities, and offshore earnings.
- The allocation of taxing rights under the DTA will enable New Zealand to share the cost of relieving double taxation with Viet Nam, on an equitable basis.
- For tax authorities, the exchange-of-information mechanism will assist in detecting and preventing tax evasion and tax avoidance. The mechanism will also be a general deterrent against evasion and avoidance activity, and will further reduce the opportunities available to residents to escape legitimate New Zealand tax.
- For New Zealand business interests, the DTA will reduce the cost of importing capital, and make it easier to repatriate profits from Viet Nam.
- For investors in both jurisdictions, the DTA will reduce compliance costs and provide the certainty of low headline withholding tax rates, locked in by the treaty.
- For investors, businesses and taxpayers from both jurisdictions, the DTA will provide safeguards such as a mutual agreement procedure, which will facilitate the resolution of tax disputes (including disputes in complex areas such as transfer pricing), or the non-discrimination[3] provision, which prohibits states from treating

[3] Note that non-residents are not considered to be in the same circumstances as residents.

nationals of the other state less favourably than their own would be treated in the same circumstances.

4.4 In 2011, the Global Forum on Transparency and Exchange of Information for Tax Purposes concluded a review of New Zealand's legal and administrative frameworks for tax information exchange, and recommended that New Zealand should continue to develop its exchange-of-information network. The Viet Nam DTA will help New Zealand to meet this recommendation.

### Disadvantages of the treaty entering into force

4.5 As noted above, DTAs offer bilateral solutions to problems that cannot be solved unilaterally. However, a potential downside to DTAs is that those solutions are then locked in place by the treaty and can be difficult and costly to change. This can create difficulties if treaty provisions need to be changed urgently. Practical experience indicates that in genuine cases, treaty partners are usually amenable to making necessary changes. However, in extreme cases, if the treaty partner were to refuse to cooperate, the treaty may need to be terminated.

4.6 A second general disadvantage of DTAs is that they typically give rise to an upfront revenue cost. DTAs decrease the withholding tax rates on investment income and allocate taxing rights between the two jurisdictions. This means that New Zealand will lose the ability to tax some income streams to the extent that it could previously. This applies on a reciprocal basis, and the reciprocal reduction of Vietnamese tax will often provide an offset to the New Zealand reduction of tax (through, for example, not having to provide a foreign tax credit). In addition, any increase in cross-border activity as a result of the DTA entering into force will result in a further offset to the New Zealand reduction of tax. However, to the extent that the New Zealand reduction of tax is not completely offset, the DTA will have a net revenue cost. (Note that DTAs will generally give rise to favourable economic benefits – such as an increase in trade and investment – and these can be expected to outweigh the revenue impact.)

4.7 A third general disadvantage of entering into DTAs is the cost of administering the exchange-of-information provisions. If a DTA partner makes requests for information, New Zealand will incur costs in complying with those requests. However, New Zealand already has exchange-of-information arrangements with 47 other jurisdictions (including 37 DTAs and 10 Tax Information Exchange Agreements), as well as the systems for administering them. The costs of providing information under the Viet Nam DTA will therefore be marginal.

4.8 As noted above, in the negotiations New Zealand agreed to Viet Nam's proposal to include tax-sparing provisions. This could be seen as a disadvantage, given that New Zealand's established preference has been not to include tax-sparing provisions in its DTAs. However, also as noted, recent changes to New Zealand's international tax rules mean that tax sparing is now a relatively minor issue for New Zealand, and tax-sparing provisions appear in some of New Zealand's recent DTAs. In addition, the tax-sparing provisions include a number of anti-abuse rules, and will automatically terminate after a ten-year period.

4.9 Despite the fact that DTAs generally only apply to taxes on income (and, in the case of countries with capital taxes, to taxes on capital), the exchange-of-information provisions typically have a wider scope, applying to all taxes. However, Viet Nam has never previously agreed to extend its exchange-of-information provisions beyond taxes on income. The Viet Nam DTA reflects this Vietnamese preference for a narrower exchange-of-information scope. This could be seen as a disadvantage. However, the wider exchange-of-information scope is a relatively recent international development, and most of New Zealand's DTAs have a narrower scope. In addition, New Zealand asked for the insertion into the DTA of a most-favoured-nation obligation that will require Viet Nam to renegotiate the scope of the exchange-of-information provisions if they ever agree to a wider scope in any other DTA.

### Advantages of the treaty not entering into force

4.10 Not having a DTA with Viet Nam is an option. In that case, the disadvantages identified above will not arise.

### Disadvantages of the treaty not entering into force

4.11 If the Viet Nam DTA does not enter into force, New Zealand business interests will continue to operate at a competitive disadvantage, compared with Australian firms that are covered by a DTA. It is likely that the Government would be strongly lobbied by those New Zealand business interests.

## 5. Legal obligations which would be imposed on New Zealand by the treaty action, the position in respect of reservations to the treaty, and an outline of any dispute settlement mechanisms

### Summary of key legal obligations

5.1 DTAs do not impose requirements on taxpayers. Moreover, the Viet Nam DTA will not (and cannot) require the imposition of a tax that is not already imposed under domestic law. The DTA obligations will apply solely to the New Zealand and Viet Nam Governments.

5.2 When income is derived from one jurisdiction (the source jurisdiction), by a tax resident of the other jurisdiction (the residence jurisdiction), both countries typically tax on that income. DTAs primarily relieve such double taxation by allocating taxing rights. The key allocation of taxing rights in the Viet Nam DTA is as follows:

- Business profits of an enterprise will be taxable only in the jurisdiction in which the enterprise is resident, unless profits are derived through a permanent establishment in the source jurisdiction. In that case, the profits may be taxed in both jurisdictions. (Article 7 refers.) The term "permanent establishment" is generally defined in the Viet Nam DTA as meaning a fixed place of business through which the business of an enterprise is wholly or partly carried on. However, this general rule is supplemented by a number of clarifications and deeming rules which follow New Zealand's preferred formula, and which will ensure that New Zealand can continue to impose tax on significant business activities such as natural resource exploration or exploitation. (Article 5 refers.)
- Investment income (dividends, interest and royalties) may generally be taxed in both jurisdictions. However, the amount of withholding tax that can be imposed by the source jurisdiction is limited to 5% where the dividend is paid to a company that owns at least 50% of the voting power in the company issuing the dividend, or 15% for any other dividend (Article 10 refers), and 10% for interest and royalties (Articles 11 and 12 refer). The limitation does not apply if the dividends, interest

or royalties are derived in connection with a permanent establishment in the source jurisdiction.

- Income from independent personal services will be taxable only in the jurisdiction in which the individual performing the services is resident, unless (i) the individual has a fixed base in the source jurisdiction, or (ii) the individual is present in the source jurisdiction for the purpose of performing the services, for more than 183 days in any 12-month period. In such case, the services income may be taxed in both jurisdictions. (Article 14 refers.)
- Income from employment will be taxable only in the jurisdiction in which the employee is resident unless the employee is present in the source jurisdiction for more than 183 days in a 12-month period, or the employer is a resident of the source jurisdiction (or is non-resident but the employee's remuneration is borne by a permanent establishment in the source jurisdiction). In that case, the employment income may be taxed in both jurisdictions. (Article 15 refers.)
- Pensions will be taxable only in the jurisdiction in which the recipient is resident. (Article 18 refers.)

5.3 A number of exceptions to the above rules also apply. These include:

- Income from real property, including income from alienation of real property (referred to as "immovable property" in the Viet Nam DTA), will always be taxable in the jurisdiction where the property is situated, regardless of whether the residence country also has a taxing right. (Articles 6 and 13 refer.)
- Profits of an enterprise from the operation or alienation of ships or aircraft in international traffic will be taxable only in the jurisdiction in which the enterprise is resident. However, profits from domestic carriage by ship or aircraft will be taxable in both jurisdictions. (Articles 8 and 13 refer.)
- Directors' fees will always be taxable in the jurisdiction in which the company paying the fees is resident, regardless of whether the country in which the director is resident also has a taxing right. (Article 16 refers.)
- Income from the activities of entertainers and sportspersons will always be taxable in the source jurisdiction, regardless of whether the residence country also has a taxing right. (Article 17 refers.). If the visit is wholly or mainly supported by the public funds of either state, then it is taxable only in the residence country.
- Salaries and wages for services to a Government of one jurisdiction will generally be exempt from tax in the other jurisdiction. (Article 19 refers.)

5.4 Where the allocation of taxing rights permits both jurisdictions to tax an item of income, the Viet Nam DTA will require New Zealand to relieve double taxation of its residents by allowing a credit for the tax paid in Viet Nam. (Article 22 refers.) This is consistent with the unilateral relief mechanism that already applies under New Zealand domestic law. The obligation also applies reciprocally, so Viet Nam must allow its residents a credit for New Zealand tax paid.

5.5 As noted above, the Viet Nam DTA includes tax-sparing provisions. These provisions, located at Article 22(3) to (5), require New Zealand to allow its residents to claim a foreign tax credit in certain circumstances, even though no tax has been paid in Viet Nam. The tax-sparing credits apply solely in the case of Vietnamese tax incentives that promote foreign investment for development purposes. They are designed to ensure that the tax incentives are not clawed back by New Zealand taxing its residents in full (which would remove the incentive for New Zealanders to invest in the Vietnamese development areas). As noted above, anti-abuse rules have been built in to the tax-sparing provisions, to ensure that they are used appropriately. The tax-sparing provisions will also automatically terminate after a 10-year period.

5.6 The non-discrimination provision requires that New Zealand does not subject Viet Nam nationals to a greater tax burden than New Zealand nationals would be subject to in the same circumstances, in particular with regard to residence. (Article 23 refers.) This requirement applies to both taxation and connected requirements. Similar rules apply for permanent establishments, deductions and New Zealand companies that are wholly or partly owned or controlled by Viet Nam residents. This provision does not create an exception to the related-party dealing rules around interest or royalty payments, or associated party dealings.

5.7 In addition to the above obligations, New Zealand will be required to comply with various administrative requirements imposed by the Viet Nam DTA. These are as follows:

- Mutual agreement procedure. New Zealand must comply with the procedures for settling disputes set out in the mutual agreement procedure article of the Viet Nam DTA. (Article 24 refers.) This is discussed below, in the section Dispute resolution.
- Exchange of information. As discussed, the Viet Nam DTA includes an Article that provides for the exchange of tax-related information between tax authorities, for the purpose of detecting and preventing tax evasion and tax avoidance. New Zealand will be required to respond to requests for information from Viet Nam. If Inland Revenue receives a valid request, and if it does not already hold the requested information, it must use its information-gathering powers to obtain the information. Inland Revenue can similarly request information from Viet Nam. (Article 25 refers.)

### Dispute resolution

5.8 The Viet Nam DTA establishes a "mutual agreement procedure" for resolving disputes. Under this procedure, a taxpayer who considers that they have been taxed incorrectly under the treaty, including in transfer pricing cases, can approach their local tax authority under Article 24 to invoke a mutual agreement procedure. If the tax authority considers the case to be justified, and is unable to resolve the case through its own actions, it must approach the tax authority of the other jurisdiction to seek a bilateral resolution. This bipartisan approach is particularly appropriate in the tax treaty context because a single issue will generally affect a person's tax position in both jurisdictions. The mutual agreement procedure is not a true disputes resolution mechanism, as the two sides are only obliged to "endeavour" to reach resolution. However, the taxpayer remains free to pursue a case through the courts (including if they do not agree with the decision reached under the mutual agreement procedure).

5.9 The mutual agreement procedure also authorises the tax authorities of the two jurisdictions to collectively resolve any difficulties or doubts about the correct interpretation or application of the Viet Nam DTA.

### Reservations

5.10 The Viet Nam DTA does not allow parties to make a reservation upon ratification.[4]

## 6. Measures which the Government could or should adopt to implement the treaty action, including specific reference to implementing legislation

6.1 Subject to the successful completion of the Parliamentary treaty examination process, the Viet Nam DTA will be incorporated into domestic legislation by Order in Council pursuant to section BH 1 of the Income Tax Act 2007. Section BH 1 authorises the giving of overriding effect to DTAs by Order in Council. However, the override relates only to tax matters, and applies only in respect of the Inland Revenue Acts, the Official Information Act 1982 and the Privacy Act 1993.

6.2 The override of the Inland Revenue Acts is necessary to give effect to the core provisions of the Viet Nam DTA, which may provide relief from tax that would otherwise be imposed under domestic law. The override of the Official Information Act is necessary to ensure that confidential communications with the other jurisdiction do not have to be disclosed. The override of the Privacy Act is necessary to ensure that information regarding natural persons can be exchanged according to the terms of the treaty.

6.3 Article 27 of the Viet Nam DTA provides for the agreement to be brought into force through an exchange of diplomatic notes between the Contracting States. The Viet Nam DTA will enter into force on the date of the last of these notes. New Zealand will be able to notify Viet Nam that all procedures required by domestic law have been completed once the Order in Council has entered into force, which will be 28 days after its publication in the New Zealand Gazette.

6.4 Thereafter, the provisions of the Viet Nam DTA will have effect from various dates, according to the terms of the DTA. In New Zealand, the provisions relating to withholding taxes will generally take effect on 1 January following the year of the date of entry into force. The provisions relating to other taxes will have effect for income years beginning on or after 1 April in the calendar year following the year in which the DTA enters into force.

6.5 As an alternative to the above Order in Council mechanism, the Viet Nam DTA could be given legislative effect by means of the enactment of a dedicated statute. However, this option would unnecessarily increase the amount of primary tax legislation, and is therefore not preferred.

## 7. Economic, social, cultural and environmental costs and effects of the treaty action

7.1 No social, cultural or environmental effects are anticipated.

7.2 As already noted, the overall economic effects of the Viet Nam DTA are expected to be favourable to New Zealand. This is because the DTA can be expected to encourage growth in economic activity, and to assist Inland Revenue to detect and prevent tax evasion and tax avoidance.

## 8. The costs to New Zealand of compliance with the treaty

8.1 New Zealand will forgo some revenue from the limitation of its taxing rights, as outlined above. This will mean that New Zealand will not be able to tax some income that

[4] Reservations typically only feature in multilateral treaties. When permitted, they effectively enable a party to specify which treaty obligations they are committing to. However, reservations typically do not feature in bilateral treaties.

is currently taxed under domestic law, and that the rate of tax that can be imposed on certain other income will be reduced.

8.2 This revenue cost will include tax forgone in relation to short-term activities of Vietnamese residents in New Zealand, which the DTA will exempt from New Zealand tax. It may also reflect reduced tax on royalties derived from New Zealand by residents of Viet Nam, in respect of which the DTA will restrict withholding tax rates to 10% (the domestic law rate being 15%). There may also be some revenue cost from reduced withholding tax rates on dividends and interest derived from New Zealand by residents of Viet Nam, although that tax is already largely relieved under domestic law.

8.3 Because investment flows from Viet Nam to New Zealand are currently low, investment returns paid from New Zealand to Viet Nam in the form of dividends, interest and royalties are correspondingly low. The prima facie revenue cost to New Zealand is therefore expected to be negligible.

8.4 Viet Nam will be similarly constrained in terms of the tax it can impose on income derived by residents of New Zealand. This reduced foreign tax will tend to flow through to the New Zealand tax base through a reduction in credits for foreign tax paid. In addition, the exchange of information provisions of the DTA will enhance our ability to detect and prevent tax avoidance and tax evasion.

8.5 Finally, the DTA will generally give rise to favourable economic benefits (such as increased trade and investment). To the extent that the cost to the New Zealand revenue is not fully offset by the factors mentioned above, we would expect that the economic benefits of the DTA will outweigh the costs.

8.6 The tax sparing provisions of the DTA are not expected to give rise to specific costs. This is because of recent changes to New Zealand's international tax rules that generally result in foreign dividends received by New Zealand companies no longer being taxed. As discussed, the tax sparing provisions will terminate after a ten-year period.

8.7 The exchange of information provisions of the Viet Nam DTA will result in some administrative costs for Inland Revenue, arising from the need to respond to requests for information from Viet Nam. Based on previous experience, the numbers of requests are not expected to be significant. If requests are received, Inland Revenue already has efficient systems in place for administering the exchange of information provisions of New Zealand's other 37 DTAs and 10 Tax Information Exchange Agreements in force, and the additional costs will be marginal.

8.8 Compliance costs for New Zealand businesses are expected to be reduced under the Viet Nam DTA. This is because New Zealand businesses will have clear guidance about when they will be liable for tax on activities in Viet Nam, in line with internationally recognised norms.

### 9. Completed or proposed consultation with the community and parties interested in the treaty action

9.1 The Treasury, and the Ministry of Foreign Affairs and Trade, were consulted about the terms of the Viet Nam DTA and the content of this extended National Interest Analysis, and agree with its analysis and conclusions.

### 10. Subsequent Protocols and/or amendments to the treaty and their likely effects

10.1 The Viet Nam DTA does not expressly set out the process for amendments to the agreement, but amendments are typically made by negotiating an amending Protocol. New Zealand will consider any future amendments on a case-by-case basis. Future amendments will be subject to New Zealand's normal domestic approvals and procedures for DTAs.

10.2 Only one future amendment to the DTA is currently contemplated. Article V of the Protocol to the Viet Nam DTA is a most-favoured-nation obligation that applies to Viet Nam. It provides that if, in any future DTA, Viet Nam agrees to extend the scope of the exchange-of-information article to taxes not otherwise covered by the DTA, it will enter into negotiations with New Zealand with a view to providing a similar extension of scope to New Zealand.

### 11. Withdrawal or denunciation provision in the treaty

11.1 Under Article 28 of the Viet Nam DTA, five years from the date of entry into force, either party may terminate the agreement by giving notice of termination through diplomatic channels. This is the same approach taken in New Zealand's other DTAs.

### 12. Agency Disclosure Statement

Inland Revenue has prepared this extended NIA. Inland Revenue has analysed the issue of implementing the new DTA between Viet Nam and New Zealand, and the legislative and regulatory proposals arising from that implementation. As part of that process, Inland Revenue considered the option of not entering into the treaty. Inland Revenue is of the view that there are no significant constraints, caveats or uncertainties concerning the regulatory analysis.

12.2 The allocation of taxing rights under the Viet Nam DTA is consistent with the New Zealand negotiating model, which in turn is based on the OECD's Model Tax Convention. Although the revenue cost to New Zealand as a result of the allocation of taxing rights under the DTA cannot be accurately measured, Inland Revenue estimates that the revenue cost to New Zealand as a result of the allocation of taxing rights will be negligible.

12.3 The tax sparing mechanism agreed with Viet Nam represents a potential risk. The mechanism therefore has a potential cost to New Zealand. The tax sparing mechanism could be seen as potentially creating a precedent that may lead to other developing countries seeking a similar provision. However, that precedent already exists. (Six[5] of New Zealand's existing DTAs contain tax sparing provisions.) Moreover, the mechanism has been narrowly crafted, contains an anti-abuse rule, and will terminate after a ten-year period.

12.4 An Order in Council will be required to give the new DTA effect in New Zealand law. The Order in Council will override the Inland Revenue Acts, the Official Information Act 1982 and the Privacy Act 1993; this is authorised by section BH 1 of the Income Tax Act 2007 and is necessary to give effect to the terms of the new DTA.

12.5 The Ministry of Foreign Affairs and Trade, and the Treasury, have been consulted about the terms of the Viet Nam DTA and the content of this extended NIA, and no concerns were raised.

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[5] A DTA has also been signed with Papua New Guinea, which includes tax sparing provisions. Once that agreement enters into force the number will increase to seven.

12.6 Inland Revenue's view is that the policy options considered will not impose additional costs on business interests; nor impair private property rights, market competition, or the incentives for business to innovate and invest; nor override fundamental common law principles.

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