



International treaty examination of the Agreement between the Kingdom of Spain and the Government of New Zealand for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income

Report of the Finance and Expenditure
Committee

The Finance and Expenditure Committee has conducted an international treaty examination of the Agreement between the Kingdom of Spain and the Government of New Zealand for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and has no matters to bring to the attention of the House.

The national interest analysis for the Agreement is appended to this report.

Shane Jones
Chairperson

Appendix—National interest analysis

International treaty examination of the Double Tax Agreement with Spain

Date of proposed binding treaty action

1 An Agreement between the Government of New Zealand and the Kingdom of Spain for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and the Protocol (together referred to as “the DTA” in this document) was signed in July 2005. Subsequent to signing and subject to the successful completion of the international treaty examination process, the DTA will be incorporated into domestic legislation through an Order in Council. The DTA will enter into force by way of an exchange of notes between New Zealand and Spain, in which each party will notify the other of the completion of their constitutional requirements for giving effect to the DTA in their respective domestic laws.

Reasons for New Zealand to become a party to the treaty

2 New Zealand currently has 29 double tax agreements (DTAs) in force. They are primarily aimed at reducing tax impediments to cross-border trade and investment, but also help tax administrations to detect and prevent tax evasion.

3 The negotiations with Spain were entered into in accordance with the Government’s Latin American strategy. The conclusion of a DTA with Spain is viewed as consistent with this strategy because Spain represents a key entry point to the region. Consultation with the Ministry of Foreign Affairs and Trade and the business community highlighted Spain as a high priority.

4 The DTA with Spain will facilitate increased trade and investment between our two countries by reducing the double taxation of cross-border transactions. Such double taxation arises because both countries will generally tax the same income. The DTA allocates taxing rights between the two countries. This will result in one or both countries having the right to tax the income. When both countries enjoy this right, the DTA provides that the country of residence will give a credit for tax paid in the country of source. The DTA gives residents of both countries who are considering entering into cross-border trade and investment greater certainty of tax treatment. The DTA also contains a mutual agreement procedure for resolving disputes or issues that might arise in relation to the DTA.

5 In relation to trade, the level of imports from and exports to Spain amounted to \$169.7 million and \$157 million respectively for the year ended June 2003. This makes Spain our twenty-fifth largest export market. The extent of trade with Spain is at a level where the conclusion of a DTA is likely to have beneficial results for both countries.

6 The DTA also assists tax administrations in the prevention of fiscal evasion by providing for the exchange of information on tax matters between two countries.

Advantages and disadvantages to New Zealand of the treaty entering into force

7 The DTA will be advantageous to New Zealand because it will remove tax impediments to cross-border transactions between New Zealand and Spain—in particular, the double taxation of income. The DTA will regulate how transactions should be taxed between the two countries so the income is effectively taxed only once. It will generally reduce withholding taxes on dividends, interest and royalties to 15 percent, 10 percent, and 10 percent respectively, and will exempt many short-term activities of individuals and businesses in the host country. When both countries are permitted to impose tax, it will ensure that the country of residence allows a credit for the tax paid in the country of source. The DTA will provide taxpayers with greater certainty of tax treatment, along with a mutual agreement procedure for resolving dispute issues that may arise in relation to the DTA. The DTA will also assist the tax administrations of both countries by facilitating the exchange of information relating to taxes.

8 A disadvantage of the DTA is that New Zealand may forgo some revenue because of the reduction in New Zealand tax and the allocation of taxing rights to Spain under the DTA. Although, as explained in the discussion under “Costs”, the reciprocal nature of the DTA means that these revenue costs will be offset by increases in revenue where taxing rights are allocated to New Zealand and where Spanish tax is correspondingly reduced under the DTA.

9 The requirement for New Zealand to provide information on tax matters to Spain under the DTA’s exchange of information provisions may be seen as a disadvantage. However, again, the ability to request information is reciprocal, and New Zealand’s experience with exchange of information in relation to its 29 other DTAs is predominantly positive (the benefit gained from being able to request information from the other country more than offsetting the administrative burden of having to provide information pursuant to their requests).

10 On balance, it is in New Zealand’s interest to conclude a DTA with Spain. It is expected to enhance cross-border trade and investment and will assist the New Zealand Government in the prevention of fiscal evasion. It will also advance New Zealand’s interest in the Latin American region, because of the strong economic and cultural ties between Spain and this region.

Obligations

11 The DTA does not impose requirements on taxpayers. The obligations it does impose are on the countries to the DTA and restricts their taxing rights under domestic law generally on a reciprocal basis. (A DTA can only reduce tax already imposed under domestic law; it cannot impose tax.)

12 Under domestic law, New Zealand taxes its residents based on their New Zealand and worldwide income. Non-residents are taxed only on their New Zealand-sourced income. Spain has a similar income tax system. This gives rise to the possibility that cross-border flows of income will be subject to double taxation. The DTA provides a way of allocating taxing rights as between New Zealand and Spain. Under this DTA, New Zealand

and Spain will be required to comply with the following rules when imposing tax on residents of either country.

- Income from immovable property will generally be taxed in the country where the property is situated. [Article 6 of the DTA refers.]
- Business profits of an enterprise will be taxable only in the country where the enterprise is resident unless profits are derived through a permanent establishment situated in the other country. In that case, the profits may be taxed in that country. A permanent establishment generally exists when there is a fixed base in the country in question where the business of an enterprise is carried on. [Article 7 of the DTA refers.]
- Profits of an enterprise of a country from the operation of ships or aircraft will be taxable only in that country. Such profits may also be taxable in the other country where the profit relates to operations confined solely to places in that other state. [Article 8 of the DTA refers.]
- Dividends paid by a company of one country to a resident of the other country may be taxed in that other country. The source country may also tax the dividend up to a maximum of 15 percent on the gross amount of the dividends. [Article 10 of the DTA refers.]
- Interest may generally be taxed in both countries. However, the country in which the interest arises may not impose tax in excess of 10 percent on interest. [Article 11 of the DTA refers.]
- Royalties may generally be taxed in both countries. However, the country in which the royalties arise may not impose tax in excess of 10 percent of the royalties. [Article 12 of the DTA refers.]
- Specific rules apply to the taxation of gains derived from the alienation of property. In the case of immovable property the gains are taxable where the property is situated. In the case of moveable property, the gain is generally taxable in the country where the alienator is resident. [Article 13 of the DTA refers.]
- Income from employment will be taxable only in the country where the employee is resident, unless the employment is performed in the other country. In this case, the country where the employment is performed may also tax the incomes, if the employee is present for 183 days and other conditions are met. [Article 14 of the DTA refers.]
- Directors' fees are taxable in the country where the company paying the fees is resident. [Article 15 of the DTA refers.]
- Artistes (entertainers) and sportspersons may be taxed in the country in which the activities of the artistes or sportspersons take place. [Article 16 of the DTA refers.]
- Pensions are taxable only in the country where the recipient is resident. [Article 17 of the DTA refers.]

- Salaries and wages for services to a Government of one country are generally exempt from tax in the other country. [Article 18 of the DTA refers.]
- Students are generally not taxed on payments received from outside the country when those payments are for the maintenance and education of the student. [Article 19 of the DTA refers.]
- New Zealand has to comply with the various administrative requirements of the DTA that make its operation possible. These include, in particular, the elimination of double taxation by giving credits for overseas tax paid in certain situations; not enacting tax laws that discriminate against residents of Spain (vis-à-vis residents of any other state); complying with the mutual agreement procedures set out in the DTA; and complying with the exchange of information procedures. [Articles 21, 22, 23 and 24 of the DTA refer.]

Economic, social, cultural and environmental effects

13 No social, cultural or environmental effects are anticipated. Any economic effects are expected to be favourable, as noted above.

Costs

14 New Zealand may forgo some revenue from the limitation of our taxing rights in relation to some income flows between New Zealand and Spain which we are currently able to tax under our domestic laws. This revenue cost could include, for instance, tax forgone in relation to short-term activities of Spanish residents in New Zealand, which the DTA will exempt. It could also include tax forgone on dividends, interest and royalties paid by New Zealand residents to residents of Spain, in respect of which the DTA will lower withholding taxes. However, Spain will also be similarly constrained from taxing certain income flows between Spain and New Zealand, and this reduced Spanish tax will often flow through to the New Zealand tax base through a reduction in credits for foreign tax paid. It is likely that these factors will offset each other to some extent over time. But, to the extent that the cost to the New Zealand revenue is not fully offset by the reduction in creditable Spanish tax, we would expect that the economic benefits of the DTA will outweigh these costs.

Future protocols

15 No future protocols are anticipated.

Implementation

16 Subject to the successful completion of the international treaty examination process, this DTA will be implemented by Order in Council in accordance with section BH 1(3) of the Income Tax Act 2004.

17 This agreement will be implemented by way of an overriding treaty regulation. Section BH 1 of the Income Tax Act 2004 enables DTAs to be given effect by Order in Council. It also provides that the DTA will override the Income Tax Act 2004 and any other enactment relating to income tax, unpaid tax and the exchange of information relating to a tax. This override is necessary to give effect to the terms of the DTA and will

effectively override the Income Tax Act 2004, the Tax Administration Act 1994 and the Goods and Services Tax Act 1985.

Consultation

18 The Treasury agrees with the terms of the DTA. Some consultation with the Ministry of Foreign Affairs and Trade and some with private sector firms was undertaken before the negotiations.

Withdrawal or denunciation

19 Article 27 provides that either contracting country may terminate the DTA by giving notice of termination, through diplomatic channels, after the expiration of five years from the date of its entry into force.