

PANAMA PAPERS MYTHS BUSTED



With the Shewan report joining other experts pointing to the long-ignored elephant in the room, RON POL looks at some inconvenient truths about the Panama Papers.

The release of the so-called Panama Papers has generated a flood of media coverage around the world.

Opposition parties here raised a clamour of complaint, little of which addressed the real issues; the Government's response was a co-ordinated wall of noise, equally bereft of meaning. Little wonder, then, that most people hit the snooze button weeks ago.

John Shewan's report, released near the end of June, is unlikely to cause more than a momentary stir, although by cutting through the noise, it might also help start a sensible debate about the Panama Papers.

The inquiry was given narrow terms of reference and heavy hints about the "detailed

financial and other records" already required by our rules. This, combined with assertive statements about the OECD's having given New Zealand its "highest possible rating", suggested it would require a brave expert even to acknowledge the elephant in the room.

Scything through the half-truths and misconceptions permeating the political and media debate, Shewan revealed the reality: the same thing that makes New Zealand foreign trusts and other opaque vehicles attractive to legitimate users – secrecy – attracts tax evaders, despots, drugs and arms traffickers and their attendant money launderers. Our regime, albeit inadvertently, manufactures almost perfectly designed getaway cars and throws in a free invisibility cloak for pretty much anyone who wants one.

Viewed dispassionately, that's clearly not good for New

Zealand's reputation. And Shewan said as much, ripping away the misconceptions that had been plastered on over several decades.

In any arena, political and media debate distorted by myths and half-truths matters, because policies built on half-truths are doomed to be ineffective. In this case, Labour wanted to abolish foreign trusts, which would close out legitimate users as well as criminals. The Government strenuously argued for maintaining the status quo (retaining legitimate and criminal use), though it eventually decided to install the time-honoured safety valve of an inquiry, at the same time sending the bob-each-way

political message that it had "always said we are open to making improvements".

Unencumbered by political affiliations and long familiar with corporate secrecy vehicles, I thought the solution was obvious from the outset:

adding factory-fitted immobilisers to those getaway vehicles to prevent criminal misuse, while allowing legitimate use to continue seemed a sensible and effective policy option. Yet the idea seemed to

get lost in the noise. Until now.

It has reappeared, labelled "Option 2", in the Shewan report, which has usefully added turbochargers. I could quibble with some elements within its 124 pages and might suggest some detailing, but



John Shewan



if the Government accepts Shewan's recommendations, it promises to be an effective means of addressing most of the unintended consequences of a legitimate policy decision not to tax New Zealand foreign trusts.

The Shewan report offers not only the opportunity for objective and dispassionate debate but also the prospect of effective policy. But first, we need to clear the fog of myths and half-truths. Here are 10 for starters.

1 Only 200 New Zealand entities were set up by Mossack Fonseca. New Zealand is barely a footnote. New Zealand has more than 100 firms that incorporate trusts and companies. Many law and accounting firms, here and overseas, also establish New Zealand foreign trusts and other structures. Focusing on the "fewer than 200" structures

set up by Mossack Fonseca is what is known as observational selection bias: it ignores thousands of such entities established by other firms. Yet the "we're too small" claims have escaped rigorous scrutiny and distracted the credulous into proclaiming that this issue is a "fizzer" and a "flop". Even left-wing commentators have sighed a disappointed "meh".

Half-truths divert attention from real issues. It doesn't matter who established the thousands of opaque New Zealand foreign trusts but who owns and controls them, and how many conceal criminal assets and activities.

Rating: Straw man, wrapped in a mirage.

2 No tax haven This country is no tax haven for Kiwis: we tax New Zealanders' income, collect comprehensive details about them and share it with

other countries. Nor are we a tax haven for Australians, whose Government didn't much like our foreign trusts, so we tweaked the design to block Aussie tax evaders.

We didn't extend the same courtesy to our other trading partners. Lawyers spotted the loophole, and some company-formation agents have been suggesting New Zealand as a tax-free offshore destination alongside Mauritius and the Seychelles. University of Auckland tax law specialist Michael Littlewood told the *Weekend Herald* that our foreign-trusts regime "plainly" fits his definition of a tax haven and a "shameful loophole" makes New Zealand "complicit in schemes to avoid tax". Shewan says by one OECD definition New Zealand is no tax haven, by another maybe, concluding that arguing about the label is inherently futile.

The fact is that, when

structured right, New Zealand foreign trusts offer the perfect vehicle for certain criminally minded people to evade taxes in whole or part, except Kiwis and Australians. So for 27 million people in two countries, New Zealand is no tax haven. For some proportion of the remaining 7.3 billion people in 212 or so other jurisdictions, it could be.

Rating: By one measure, as little as 0.4% true and up to 99.6% fib; by another, 100% irrelevant.

3 The OECD gave New Zealand's tax system a tick In 2013, the OECD rated New Zealand's overall tax system highly. We comprehensively tax Kiwis and our GST system is world-leading.

But the OECD report also pointedly exposed gaps in our foreign trusts and companies regime, such as allowing nominees and not maintaining

beneficial owner details. Another OECD report found “serious deficiencies” and criticised the ease with which shell companies can be and were being “established in New Zealand ... as fronts for international laundering of drug money, fraud and terrorism”.

OECD sister organisation the Financial Action Task Force requires member states – including New Zealand – to obtain information on “the beneficial ownership and control of legal persons”, particularly for countries that allow opaque shareholders and nominee directors to mask the real owners. New Zealand plainly doesn’t meet those standards.

The inconvenient truth is that our lack of transparency in foreign trusts and company registration is consistently rated poorly by the OECD and other international monitors. As Littlewood said, it seems to be the only area where we’re “right out of step with OECD norms”. **Rating:** Half-truth, stretched past breaking point with foreign trusts and company registration.

4 The rules were “tightened” by requiring New Zealand-resident directors

New Zealand companies must now have a local resident director. The implication that this prevents or even substantially restricts misuse is, however, a non sequitur. One does not lead to the other.

The most celebrated example involves a Kiwi company that chartered a plane carrying 35 tonnes of munitions from North Korea bound for Iran in breach of international sanctions. It had a resident director even before the rule change. A young fast-food worker was convicted and discharged but had no idea about the transaction or who was behind it.

Having a resident director was completely ineffective. The organised-crime or terrorist group that used a New Zealand company to shield its arms trafficking business has never been found.

New Zealand allows people who own and control companies and foreign trusts to hide behind nominee directors and trustees and corporate shareholders. Most legitimate users choose not to. But anyone with criminal intentions would be plain crazy not to wrap New Zealand’s special invisibility cloak over their activities.

Rating: Half-truth. Do the new rules make a difference? Yeah, nah.

5 We share information about New Zealand foreign trusts

If another country stumbles across the name of a New Zealand foreign trust, itself no easy feat, it can ask for more details. If we have an information-sharing agreement, we’ll oblige. We might tell them the name of the trustee, typically a lawyer acting as nominee. But we don’t collect any material details, such as who really owns, controls and benefits from it. And so what we pass on when asked is nothing much.

Rating: Half-truth, nudging misleading.

6 A crack IRD squad found no tax evasion by Kiwis

The IRD’s team of experts charged with ensuring no New Zealanders were dodging their tax obligations found about 200 Kiwi entities linked to Mossack Fonseca, and Prime Minister John Key told Parliament that the “IRD has cross-referenced them all ... to ensure they pay their fair share of tax”. Undoubtedly true.

Yet the IRD could have sent in a pack of beagles or flock of budgies to the same effect.

New Zealand has chosen not to tax foreign trusts and Kiwis can’t use them. So there was never going to be evidence of New Zealand tax evasion or of Kiwis using New Zealand foreign trusts.

Anyone induced to think otherwise, by people stretching reality beyond credulity like blogger Whale Oil crowing that no Kiwis were named, wasn’t paying attention.

Rating: Half-truth, in the sense that if politics was a business, anyone caught peddling this line might be prosecuted for deceptive conduct.

7 It doesn’t affect New Zealand’s tax base

Finance Minister Bill English told Parliament that foreign trusts don’t affect our tax base, but this is because we’ve chosen not to tax them. That’s a legitimate policy decision, which Shewan supports, but if these structures allow their owners to avoid paying tax elsewhere, it’s disingenuous to suggest turning a blind eye to any damage done to other countries’ tax bases won’t affect New Zealand’s interests.

Rating: Mostly true, but ...

8 It’s not our job to protect other countries’ tax bases

Contrary to the rationale of information-sharing, handing out invisibility cloaks for a few pieces of silver to anyone who might be able to use New Zealand to undermine the tax bases of other countries inevitably damages our reputation.

It’s perhaps not quite so damaging in a relative sense, because some other countries offer much the same services. But we can hardly expect fulsome support from those who are sheltering Kiwis ripping off our tax base if we offer a shelter designed to hide their tax evaders. The same applies when we

proclaim New Zealand’s corruption-free reputation while selling corporate vehicles that facilitate pretty much any illegal activity for which secrecy is useful. We can’t have it both ways without being two-faced.

Rating: Yes, but. And a one-fingered salute to our trading partners, Australia excepted.

9 Vast amounts of dodgy money are rushing into New Zealand

Labour leader Andrew Little told Parliament that we were allowing foreigners to stash their money in New Zealand to avoid taxes in their homeland. However, the money associated with foreign trusts and other secrecy vehicles, whether legitimate assets or criminal proceeds, is hardly ever “in” New Zealand.

Drugs cartels awash with billions of dollars of criminal cash might make the occasional drive-by sneak purchase of 50 Auckland houses, but our foreign-trusts regime doesn’t operate as a criminal bank to stash their ill-gotten loot. For those who want to use New Zealand to hide illegal activities, our foreign-trusts regime is more like a criminal getaway car.

If the Sinaloa Cartel, an international drug trafficking, money laundering,



and organised crime syndicate, owns a chunk of New York real estate, any New Zealand foreign trust used could be part of a secrecy web spanning Belize, Panama and the British Virgin Islands, with an invisibility cloak over each and maybe a Nevada limited liability company holding some of the assets. If they use Kiwi foreign trusts, the vast profits of drugs traffickers are never “in” New Zealand; we’re just the concierge handing out keys to one of the getaway cars.

Rating: Wrong. New Zealand foreign trusts are getaway cars, not bank accounts.

10 Our anti-money laundering rules are designed to prevent crime

Associate Justice Minister Simon Bridges proclaimed that New Zealand’s anti-money laundering regime is “aimed at preventing crime”. Certainly that’s the intention, even if the aim is imperfect. New Zealand law doesn’t meet international standards in some areas, and aspects of our laws, and those standards, are arguably sub-optimal.

It’s easy enough to show how our laws and the global standards themselves might be improved to boost

crime prevention, but I wouldn’t quibble with the minister’s broad sentiment

– with one exception. Pretty much everywhere else, our anti-money laundering rules do try to prevent crime, sometimes quite successfully. Foreign trusts are the infamous outlier. Their design not only fails to prevent crime, but enables and facilitates serious crime on a global scale.

Rating: True for the most part, but in this area false.

As the Shewan report illustrates, a dispassionate perspective stripping away the cloying fog of half-truths reveals a certain clarity. Our foreign-trusts industry indiscriminately offers an invisibility cloak for just about anyone wanting to use New Zealand to hide their activities, whether legitimate or criminal.

For any policy initiative to be effective, it must squarely address the ultimate policy objective, and the Shewan report does this admirably, offering a blueprint to retain and enhance New Zealand’s reputation. With serious crime prevention the goal, we could apply the same clarity to the political and media debate surrounding the Panama Papers if, like Shewan, we first ditch the nonsense and face the issues themselves. ■

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Criminal trusts harm us all

Legitimate use of the Kiwi version of an invisibility cloak doesn’t harm New Zealanders. When Emma Watson used another type of secrecy vehicle to mask a London house purchase from stalkers, she wasn’t avoiding taxes or doing anything unlawful. Likewise, when Disney bought Florida swamp land using secretly owned companies before building Disney World, it paid the market price without being gouged by sellers who knew the buyer’s real identity.

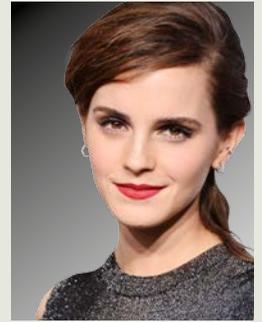
Harmful issues arise only because New Zealand’s foreign-trusts regime doesn’t discriminate between legitimate and criminal use.

When the rich and powerful use New Zealand to evade taxes, the effects of global wealth and income inequality inevitably widen. Ordinary people can only invest after-tax income, but anyone who uses secrecy vehicles to evade taxes can invest all their income. There is a legal distinction between (unlawful) tax evasion and (lawful) tax avoidance, but their economic effect is much the same. The wealth gap between taxpayers and those who evade or avoid tax widens, and with compounding eventually does so exponentially, to society’s detriment.

A nested series of secrecy vehicles between, say, New Zealand, Panama, the British Virgin Islands and Delaware can also help create virtually impenetrable barriers protecting drugs and arms traffickers and other criminal groups hiding the proceeds of serious crime. So if some of the Chinese or Mexican gangs considered responsible for sending vast shipments of ephedrine to our shores avail themselves of New Zealand’s invisibility cloak, we are helping to fund and perpetuate the vast societal and economic harm wrought by the methamphetamine trade we think we are trying to prevent.

There’s scant evidence that New Zealand’s foreign-trusts regime is effectively helping fund the same crime groups causing social and economic harm in our own communities. For all we know, like Mossack Fonseca, the drug gangs supplying New Zealand may prefer the British Virgin Islands’ variety of secrecy vehicle. But there may be no evidence precisely because New Zealand foreign trusts are perfectly designed as secrecy vehicles and because we haven’t mustered the intestinal fortitude to lift the bonnet to check.

It is the very design of these trusts, which fails to discriminate between legitimate and criminal use, that creates clear and present harm for all New Zealanders. Adopting the Shewan recommendations would go some way towards fixing the design fault and reducing that harm.



Lawful user: Emma Watson.



From left, John Key, Bill English, Andrew Little and Simon Bridges.