Chapter 1

New Zealand: Treaty Interpretation on an Exchange of Information[1]

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1.1. Introduction

This case concerns the exchange of information made under the Korea-New Zealand double tax treaty.[2] The Korean National Tax Service (NTS) asked the New Zealand revenue authorities (Inland Revenue) to obtain information in respect of New Zealand-based subsidiaries of a Korean multinational. The agent for the New Zealand subsidiaries (an accounting firm called Chatfield & Co) resisted providing this information and commenced proceedings for the judicial review of the actions of the New Zealand Commissioner.

There are two key questions addressed in the decision:

(1) First, what is the position for a tax authority (New Zealand) when a taxpayer demands access to a request for information from a foreign tax authority (Korea)? Should the tax authority release the request for information from the foreign authority to the affected taxpayer?

(2) Secondly, how should recent developments in the OECD Model on confidentiality requirements be interpreted? In particular, can the OECD Commentary be used to clarify the application of the confidentiality rules?

With respect to the first question above, an interesting balancing act was undertaken by the High Court between the interests of public disclosure (and fairness to taxpayers) on the one hand and the interests in the withholding of information (secrecy and international confidentiality obligations) on the other.

Disclosure of the NTS information request was the critical factor in this case. The taxpayer, through their agent, wanted to understand the nature

1. NZ: High Court (HC), 1 Sept. 2015, *Chatfield & Co Ltd v. Commissioner of Inland Revenue*, NZHC 2099.
2. Double Taxation Relief (Republic of Korea) Order 1983.

of the Korean request. They felt they needed access to the documents exchanged, including the original request, in order to understand the validity of the New Zealand Commissioner's request for information.

But the New Zealand Inland Revenue's reluctance to provide the NTS information request was also justified. A government provides information to another government with the understanding that the information exchanged is treated as secret. This could be summarized in the deposition of the New Zealand competent authority (Mr Nash) when he said:[3]

> New Zealand considers any failure to keep confidentiality would severely curtail future exchanges of information with the Republic of Korea as well as other treaty partners.

So the New Zealand Commissioner argued for a blanket and undifferentiated claim of confidentiality. In doing so she relied upon a 25-year-old New Zealand Court of Appeal decision.[4] This submission was not accepted, however; the legal landscape in relation to taxpayer secrecy has changed since that decision. There is no automatic right to reject such a request on the grounds of confidentiality.

The court decided that the Commissioner could not simply refuse the provision of the NTS information to the taxpayer's agent. The information can be disclosed to governmental or judicial authorities to decide whether the information should be passed to the taxpayer, their agent or witnesses.

The New Zealand Commissioner was ordered by the court to go back to the NTS to make specific enquiries of Korea as to whether the disclosure of the specific documents could be made. If secrecy was going to be sought by the NTS, then that application would be reviewed by the judge. She would then balance the international confidentiality obligations owed to the NTS with the public interest in disclosure. If the public interest in disclosure exceeded the international confidentiality obligations (weighing up the reasons given by the NTS for withholding the information), then she would order such disclosure to the taxpayer's agent.

With respect to the second point above concerning confidentiality and the use of the OECD Commentary, the decision examines closely the meaning of the exchange of information article in the Korean-New Zealand DTA

3. *Chatfield* (2015) at [12].
4. NZ: Court of Appeal (CA), 2 Oct. 1992, *Commissioner of Inland Revenue v. E R Squibb & Sons (New Zealand) Ltd*, 6 PRNZ 601 (CA).

(the relevant agreement being signed in 1983). In interpreting the DTA, the OECD Commentary plays a pivotal role.

The use of the OECD Commentary by the New Zealand court is legally justified by express reference to the Vienna Convention on the Law of Treaties (VCLT) and, in particular, article 32. Article 32 is referenced because of the ambiguity in interpreting the plain text. Another interesting aspect to the decision is that it applies Commentary that was written quite a long time after (2005 and 2012) the signing of the relevant Korean DTA (1983). Accordingly, the decision considers whether the changes made over time to the OECD Commentaries in respect of article 26 are to be considered as an amendment intended to simply clarify the meaning. Because it clarifies rather than changes the meaning, this suggests that an *a contrario* interpretation is wrong in this particular circumstance.

One concerning aspect of the decision is that it imports into the words of the Korea-New Zealand DTA six words from the current OECD Model that were introduced in 2005 (and which were not part of the 1983 Agreement). When these changes were made to the OECD Model, the Committee of Fiscal Affairs intended that they represent a substantive change from the previous Model. The fact that the Committee of Fiscal Affairs intended a substantive change to the Model article was not noted by the court.

Notwithstanding this oversight, the more critical aspects of the OECD Commentary relied upon by the judge were those that clarified that the disclosure of the competent authority's letter was acceptable in court proceedings "unless the requesting State otherwise specifies". It seems strongly arguable that the changes to the Commentary that ultimately led to the decision on confidentiality were in the nature of clarification and that they were therefore "to be viewed not as recording an agreement about a new meaning but as reflecting a common view as to what the meaning is and always had been".[5]

1.2. Facts of the case

This case, which was held in the Auckland High Court in late 2015, concerns the legitimacy of a request made by the New Zealand Commissioner of Inland Revenue for tax documents held by Chatfield & Co Ltd (a firm of

5. *Chatfield* (2015) at [62].

chartered accountants based in Auckland who are the taxpayer's agent).[6] The requested information belonged to a New Zealand-resident company KNC Construction Ltd (and a number of associated companies). The New Zealand operations of KNC Construction are owned by a Korean multinational and operate as a "leading property development and construction company in Auckland".[7] Some of its key projects include the new 67-level Elliott tower (which will be the tallest building in New Zealand) and a 23-level Commercial office tower on Shortland Street.

The New Zealand companies were under investigation by the tax authorities in the Republic of Korea. As a result of this investigation, the NTS requested the New Zealand Commissioner of Inland Revenue to obtain from the New Zealand operations of KNC and provide this information under the New Zealand-Korea Double Tax Relief Order (DTA). Article 25 of the Korean DTA generally follows the terms of article 26 of the 1977 OECD Model Convention.

The New Zealand Commissioner issued notices under New Zealand domestic legislation[8] requiring Chatfield to provide information relating to its client KNC in order for it to be passed on to the NTS.

Chatfield sought a judicial review of the decision made by the Commissioner to issue these notices to furnish information, effectively stalling the request. As part of the judicial review of the Commissioner's notice requiring the supply of information, Chatfield requested copies of documents exchanged between the NTS and the Commissioner.[9] Chatfield asserted that in order to understand whether the decision to request the information was validly made they needed to see the reasons given by the NTS leading to the New Zealand Commissioner's decision to request the documentation and the procedures followed by the New Zealand Commissioner.

Chatfield therefore wished to test whether the request from Korea was, first, necessary for carrying out the provisions of the DTA.[10] Secondly, Chatfield also wanted to establish whether the information was obtainable

6. *Chatfield* (2015).
7. According to its website found at http://kncl.co.nz/about-us/ abstracted on 21 March 2016.
8. NZ: Taxation Administration Act 1994, sec. 17.
9. One of the grounds of the judicial review being that the Commissioner had failed to take into account relevant considerations relating to the DTA and the requirements of article 25.
10. This is required by article 25(1) of the DTA. It will be recalled that the DTA was based on the 1977 OECD Model. This was therefore prior to the introduction of

under Korean law or in the normal course of the administration of Korea.[11] For example, the material sought by the tax administration in Korea dated back to 2002 and there was no information available as to the position in Korea as regards a statute bar.[12]

The Commissioner simply refused to supply the documents exchanged between NTS and the New Zealand IRD. She asserted they were not relevant and in any event related to "matters of State", which meant she could not provide them unless the judge directed her to do so.[13] In New Zealand, the law provides[14] that a "Judge may direct that a communication or information that relates to matters of State" must not be disclosed if in the opinion of the judge the public interest in the communication being disclosed is outweighed by the public interest in withholding the communication. The Commissioner relied on previous New Zealand decisions to substantiate this approach: the Court of Appeal decision in *Squibb*[15] and the New Zealand High Court decision of *Avowal*[16] had both dealt with applications by the taxpayer for the production of documents obtained through the process of exchange of information under a double tax agreement in respect of which the Commissioner claimed privilege and confidentiality.

The Court of Appeal in *Squibb* had held that communications between the New Zealand Inland Revenue and the Australian tax office made pursuant to the Australia-New Zealand DTA[17] should remain privileged and were unable to be supplied to the taxpayer in the context of judicial review proceedings. The information had been supplied to the New Zealand Commissioner by the Australian tax authorities with a specific request that it remain confidential. Richardson J had delivered the majority judgment in a full five-judge court. He held that a single taxpayer was not concerned with the assessment of "the taxes" to which the DTA applied.[18]

> A single taxpayer is concerned with its own tax liability. It cannot be said to be concerned with the assessment of the taxes to which the agreement applies.

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the current "foreseeably relevant" found in the current OECD Model Tax Convention (Condensed), Paris, 2014.

11. This is required by article 25(2) of the DTA.
12. *Chatfield* (2015), at [35].
13. Id., at [4] and [40].
14. NZ: Evidence Act 2006, sec. 70.
15. *E R Squibb & Sons (New Zealand) Ltd* (1992).
16. NZ: HC, 10 Jan. 2008, *Avowal Administrative Attorneys Limited v. North Shore District Court*, 1 NZLR 675 (HC).
17. Australia-New Zealand Double Taxation Relief Order 1972.
18. *E R Squibb & Sons (New Zealand) Ltd* (1992), at 608-609.

Later on in his judgment he concluded:[19]

> But there is no justification in the language, scheme or purpose of para 2 *(of article 26 of the OECD Draft Double Taxation Convention on Income and Capital of 1963)* for diluting the confidentiality obligations under the Article and requiring information exchanged in confidence to be released in pre-trial discovery to a litigant in judicial review proceedings. To do so would contravene the understanding reached with the Commonwealth of Australia and would be contrary to the well-grounded express objection of the Australian Tax Office.

Of course, the decision in *Squibb*, to the extent to which it is directly relevant, is binding on the High Court in this case.[20]

Chatfield's counsel argued that to the extent required or permitted by domestic law, article 25 of the DTA contemplates that information received pursuant to the DTA may be disclosed to a court and communicated to the taxpayer or his or her proxy.[21] She relied on the principle that section 81 of the Taxation Administration Act 1994 (TAA) itself sets out a balancing act between tax secrecy and fairness to taxpayers.[22] She referred the court to the New Zealand Supreme Court decision in *Westpac*, where the Supreme Court authorized the Commissioner to give discovery as a necessary incident of tax litigation:[23]

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19. Id., at 609-610.
20. Because of its status as an appellate court. For example, Baragwanath J in another High Court decision (*Avowal Administrative Attorneys limited*) had held that the decision in *Squibb* was indistinguishable from the circumstances he was considering and so refused information exchanged to be released in a pre-trial discovery to a litigant in judicial review proceedings. This information exchange in *Avowal* arose again under the Australian DTA (although a later version) in circumstances where requests were made by the Australian Tax Office which were directed at securing information to assist its own tax-gathering function (*see Avowal* (2008)).
21. *Chatfield* (2015), at [42].
22. Section 81 of the TAA outlines an obligation upon Inland Revenue offices to maintain secrecy on all matters relating to tax legislation but it provides a series of exceptions from this proscription. For example, an Inland Revenue officer may communicate, outside these secrecy constraints, if the matter is for the purpose of executing or performing a duty of the Commissioner and the Commissioner considers that such communication is reasonable having regard to the obligation to protect the integrity of the tax system, promote voluntary compliance by taxpayers and personal or commercial impact of the communication. Furthermore, factors such as the resources available to the Commissioner and the public availability of the information are also relevant (section 81 (1B) of the TAA).
23. NZ: Supreme Court, 14 Apr. 2008, *Westpac Bank Corporation Ltd v Commissioner of Inland Revenue*, NZSC 24, NZLR 709.

> [71] On this basis, section 81 of the Act itself addresses comprehensively the conflicting principles of taxpayer secrecy and the interests of justice. It sets the basis upon which they are reconciled. This involves confining use of taxpayer material in a manner which discloses identity of other taxpayers to situations where that is reasonably necessary.

In essence, it was argued that the law had moved on from the *Squibb* decision and that for a variety of different reasons, including the approach taken by the New Zealand Supreme Court in *Westpac*, section 81 of the TAA does the "work" that might otherwise be done by doctrines of more general application (which are reflected in sections 69 and 70 of the Evidence Act).

1.3. The court decision

This decision favoured the taxpayer as the Commissioner's flat refusal to supply the information[24] to the taxpayer was rejected as being acceptable behaviour by the court. Her Honour, Ellis J, did not order that the information be immediately supplied to the taxpayer, however; rather, she set in train a course of action which would involve a two-stage process. The first stage of that process involved ascertaining whether the Korean NTS had an objection to the disclosure of the information (i.e. would they refuse consent to it being passed to the taxpayer?). The second stage, which would only occur in the event of such an objection and refusal, involved a further referral of the matter back to the High Court in order to balance the interests of public disclosure against the benefits of confidentiality and public withholding.

Ellis J did not regard the High Court as being bound by the Court of Appeal's decision in the *Squibb* case for three major reasons. These are set out below.

1.3.1. The evolving law of taxpayer secrecy and no blanket confidentiality obligation

Ellis J largely accepted the arguments made by the counsel for Chatfield. She refused to accept the approach suggested by the Commissioner's legal team – that section 70 of the Evidence Act is automatically engaged

24. Being the documents containing the NTS request for exchange of information provided to Inland Revenue.

whenever documents that are the subject of a DTA exchange are sought in court proceedings then they are immune from discovery. In her view, "the days of class immunity are almost, if not entirely, over".[25] Accordingly, she took the view that the legal landscape in relation to taxpayer secrecy had changed since the *Squibb* decision, particularly given the approach taken by the New Zealand Supreme Court in *Westpac*. The preferred approach is to rely on section 81 of the TAA, which itself addresses the conflicting principles of taxpayer secrecy and the interests of justice. She accordingly was open to the possibility of evaluating whether the information request should be supplied to the taxpayer.

1.3.2. The difference between the Australian DTA (1972) and the Korean DTA (1983)

Her Honour began by returning to some first principles on the interpretation of treaties. Negotiated through a bilateral process against the general background of the OECD Model Tax Convention, she acknowledged that some differences between DTAs were simply due to the "background of the particular languages, legal systems, historical influences, tax law, and wider economic policies and expectations of the respective countries".[26] Because of the background of treaty negotiations it is to be expected that the terms of the DTAs will not be expressed with the same precision as ordinary domestic tax legislation nor will they be consistent and how the terms of a particular article are expressed in various DTAs. The question, as always, is whether changes arise through the incidence of negotiation and the factors Her Honour outlined above (such as language and economic influences) or whether the difference of expression is intended to have another consequence or purpose.

The way Ellis J approaches the interpretation of article 25 of the 1983 Korean DTA is not to focus expressly on the differences from the earlier 1972 Australian DTA but rather to examine in great detail the meaning of the words in the Korean DTA. In doing so, she uses the OECD Commentary to assist in the interpretation. In performing this interpretive analysis, she concludes that there is a difference in meaning between the Korean DTA and the earlier Australian DTA that was considered in the *Squibb* case.

25. *Chatfield* (2015), at [49].
26. Id., at [53].

1.3.3. Making sense of the Korean DTA using the OECD Commentaries

Her Honour commenced the analysis in the judgment in a very traditional way by citing the Court of Appeal decision in *JFP Energy*,[27] which validates the use of the OECD Commentary as follows:[28]

> The OECD Convention rules have an international currency used as they are by and in countries throughout the world and accordingly the language of the rules should be construed on broad principles of general acceptation and having appropriate regard to the Commentary and any travaux preparatoires.

She then sets out in full articles 31 and 32 of the VCLT before expressly acknowledging that article 32 is authority for the use of the Commentaries in the interpretation of DTAs based on the OECD Model. This is confirmed both by the Court of Appeal in *JFP Energy* and in the cases referred to in that decision and subsequently.[29]

Should we be limited only to the OECD Commentaries which are in existence at the time the DTA is negotiated and entered into or can reference be made to subsequent Commentaries? Ellis J refers to the introduction to the OECD Model and Commentaries[30] and concludes:[31]

> On that approach, any changes to the Commentaries (where there has been no relevant substantive change to the Model Convention) are to be viewed not as recording an agreement about a new meaning but as reflecting a common view as to what the meaning is and always has been.

Looking at article 25 of the Korean DTA, she then breaks down the article as follows:[32]

(a) any information received by New Zealand or Korea pursuant to the agreement;
(b) shall be treated as secret in the same manner as information obtained under the domestic laws of that state; and
(c) shall be disclosed to persons or authorities (including courts) involved in the assessment or collection of, the enforcement or prosecution in

27. NZ: CA, 14 June 1990, *Commissioner of Inland Revenue v. JFP Energy Inc*, [1990] 3 NZLR 536.
28. Id., at 540 (per Richardson J).
29. *Chatfield* (2015), at [60].
30. *OECD Model Tax Convention on Income and on Capital*, Introduction paras. 35-36 (15 July 2014).
31. *Chatfield* (2015), at [62].
32. Id., at [63].

respect of, or the determination of appeals in relation to, the taxes covered by the Convention;

(d) such persons or authorities (including courts) shall use the information only for such purposes; and

(e) such persons or authorities (including courts) may disclose the information in public court proceedings or in judicial decisions.

The key interpretive issue is the relationship between b) and c) above. If b) stood alone, then the information request currently at issue in this case could be disclosed in the proceedings, provided such disclosure was permitted under the domestic law of New Zealand (pursuant to section 81 of the TAA). But when b) is read together with c), the position is less clear. The decision in *Squibb* suggesting that disclosure in certain types of court proceedings is permitted, but that those proceedings are limited to those which directly relate to the collection and enforcement of taxes and would not extend to court proceedings involving judicial review. Given this interpretive difficulty,[33] Ellis J then considered what light can be shed on the matter by reference to the OECD Commentaries.

Article 25 of the Korean DTA and article 26 of the OECD Model Convention[34] are similar as both use the problematic conjunction "and" to link the requirements of secrecy to the limited disclosure to certain people in certain types of court proceedings. Article 26 of the OECD Model, however, has extra words. After the secrecy requirement and the limited disclosure "only to persons or authorities (including courts and administrative bodies) concerned with the assessment or collection of, the enforcement or prosecution in respect of, the determination of appeals in relation to the taxes referred to in paragraph 1," come an additional six words, "*or the oversight of the above*" (emphasis added).

Ellis J was attracted to the idea that the "oversight" of the assessment, collection and enforcement of taxes would include the exercise by the New Zealand High Court of its supervisory jurisdiction over all executive action (including the exercise of statutory powers of decision) permitting actions in judicial review to be included within the scope of the exchange of information article. Accordingly, she proposed that article 25 of the Korean DTA should be read as if the extra six words above were included and used

33. Presumably upon the basis that article 32 of the VCLT enabled recourse to be had to supplementary means of interpretation such as the Commentary in circumstances where the meaning according to article 31 of the VCLT was ambiguous or obscure.

34. OECD (2014), *Model Tax Convention on Income and on Capital: Condensed Version 2014*, OECD Publishing; http://dx.doi.org/10.1787/mtc_cond-2014-en.

the current OECD Commentary (which had been amended in 2012) to provide helpful background as to how this interpretation would dispense with the interpretive difficulty she encountered. She particularly referred to the following part of the OECD Commentary:[35]

> If, however, court proceedings or the like under the domestic laws of the requested State necessitate the disclosure of the competent authority letter itself, the competent authority of the requested State may disclose such a letter unless the requesting State otherwise specifies. The maintenance of secrecy in the receiving Contracting State is a matter of domestic laws….

Subsequently, Ellis J highlighted the following part of the OECD Commentary, when discussing that information obtained may be disclosed only to "persons and authorities involved in the assessment or collection of, the enforcement or prosecution in respect of, the determination of appeals in relation to the taxes with respect to which information may be exchanged according to the first sentence of paragraph 1, or the oversight of the above":[36]

> This means that the information may also be communicated to the taxpayer, his proxy or to the witnesses. This also means that information can be disclosed to governmental or judicial authorities charged with deciding whether such information should be released to the taxpayer, his proxy or to the witnesses.

Using the OECD Commentary in this way (reading in the additional six words relating to oversight and the clarification provided in the text of the Commentary), Ellis J decided that the impediment in the Court of Appeal's decision in *Squibb* to the discovery of DTA material in judicial review proceedings could be overcome.[37] She notes, however, that the Commentary suggests that such requests may be disclosed in the relevant domestic court proceedings unless the requesting state otherwise specifies. This is a matter of common sense and she noted:[38]

> It will be on the requesting State which knows the purpose of the request and whether disclosure of its details in New Zealand proceedings might prejudice (for example) the conduct of some investigation by the requesting State. Or it may be that the requesting State has disclosure rules that are generally less (or more) liberal than New Zealand's. In any event, logic suggests that specific enquiry should be made.

35. Id., at [11].
36. Id., at [12].
37. *Chatfield* (2015), at [71].
38. Id., at [73].