Equity Trust International

The New Zealand Finance Company – an offshore banking solution and now tax free

INTRODUCTION

The 21st century has seen an escalating regulation of the banking and financial industry. It has become increasingly difficult to obtain a license for financial services with increasing government controls and requirements.

The use of the word bank creates immediate compliance issues including capital/lending ratios, minimum founding capital requirements and central bank regulation of the institution. So that few can now meet the onerous requirements of most jurisdictions including the traditional offshore tax havens.

New Zealand has however legislated for the fast and relatively uncomplicated creation of a corporation, which can operate virtually in the same manner as a bank, whilst avoiding the restrictive controls of banking legislation.

This Brochure briefly explores the utilization of the New Zealand finance company as an alternative banking and financial structure for the offshore industry.

THE NEW ZEALAND FINANCE COMPANY OR FINANCIAL SERVICES PROVIDER (FSP) - LEGISLATIVE FRAMEWORK.

Under section 11 of the Financial Service Providers (Registration and Dispute Resolution) Act 2008, a New Zealand company can be incorporated as a financial services provider. This means that the company is effectively issued permission by the Ministry of Economic Development to offer financial services or in the words of the legislation becomes a responsible financial services provider.

As long as the finance company does not offer financial services to the New Zealand public and does not take deposits from the New Zealand public [there are other and stricter requirements if this is the case] under section 15 of the Financial Service Providers (Registration and Dispute Resolution) Act 2008 an application to be registered as a financial service provider must be made to the Registrar and—

- (a)state the following (as relevant to the applicant):
  - (i)the name and business address of the applicant:
  - (ii)the name and business address of the approved dispute resolution scheme or the reserve scheme of which the applicant is a member:
  - (iii)whether the application relates to a licensed service, and if so, which particular licensed service; and
- (b)be in the form (if any) required by the Registrar; and
- (c)confirm that the applicant is not disqualified under section 14; and
- (d)contain, or be accompanied by, any other prescribed information or documents; and
- (e) Be accompanied by the prescribed fee or levy (if any).

If the application relates to a licensed service, it must be accompanied by any information required, by or under the licensing enactment, to become a licensed provider.

The FSP obtains registration as a New Zealand FSP when the above information is provided and accepted by the Registrar.

Once registered the FSP can offer virtually all the services of a bank. Thus it can:

- Borrow or lend money at interest;
- Offer brokerage services including Forex trading;
- Take deposits and act as escrow agent;
- Act as a merchant bank;
- **Act as non-bank deposit taker**
- Offer banking type services via the internet including PayPal;
- A financial adviser service;
- A broking service;
- Acting as a deposit taker as defined in the Reserve Bank of New Zealand Act 1989;

-**dealing in futures**

- Keeping, investing, administering, or managing money, securities, or investment portfolios on behalf of other persons;
- Providing credit under a credit contract;
- Operating a money or value transfer service;
- Issuing and managing means of payment (for example, credit and debit cards, cheques, travelers' cheques, money orders, bankers' drafts, and electronic money);
- Giving financial guarantees;
- Participating in an offer of securities to the public in either of the following capacities (within the meaning of those terms under section 2(1) of the Securities Act 1978);
    - **As an issuer of the securities;**
    - **As a promoter**;
- Acting in any of the following capacities (within the meaning of those terms under section 2(1) of the Securities Act 1978) in respect of securities offered to the public;
    - **As a trustee;**
    - **As a statutory supervisor;**
    - **As a unit trust;**
    - **As a superannuation trustee;**
    - **As a manager**;
- Changing foreign currency;
- **Entering into derivative transactions, or trading in money market instruments, foreign exchange, interest rate and index instruments, transferable securities (including shares), and futures contracts on behalf of another person**;
- **Providing forward foreign exchange contracts**;
- **Acting as an insurer**;
- Providing any other financial service that is prescribed for the purposes of New Zealand complying with the FATF Recommendations, other recommendations by FATF, or other similar international obligations that are consistent with the purpose of this Act.
- Fund management companies
- Funds

(I*t must be noted and understood that currently registration as an FSP authorizes the company to provide most financial services , however in addition to registration as an FSP extra licensing may be required depending on the nature of the product being offered, we have set out in black the current financial products that require extra licensing –thus for example offering derivatives requires license from the Financial Markets Authority and acting as a non-bank deposit taker requires licensing from the Reserve Bank of New Zealand. Since these licensing requirements are recent, Equity Trusts International legal advisers and experts are here to help you with all stages of the process including*

completing the application forms applying for minimal capital requirement exemptions and liaising with government departments)

Therefore the activities a FSP can undertake are virtually unlimited and (subject to the laws of the jurisdiction where it operates).

CURRENT REQUIREMENTS AND FUTURE REGULATORY TIGHTENING

Prior to late 2014 applying for registration as an FSP required minimal documentation and little regulatory oversight from the New Zealand Authorities. Unfortunately due to the unscrupulous use of finance companies by a number of international firms leading to loss of client funds, New Zealand's authorities took measures to protect New Zealand's reputation as a reliable non blacklisted jurisdiction by increasing regulatory controls over FSP applications and registration.

These new regulations essentially give the Financial Markets Authority (FMA) far greater powers to refuse registration or deregister financial service providers who are seen as a threat to New Zealand's reputation. Whilst this new framework creates far greater compliance consequences one advantage is that the international financial community sees New Zealand as a reliable first world jurisdiction with proper protection of investors' funds and proper anti-money laundering and countering financing of terrorism legislation in place.

The new legislation implemented in late 2014 is the following:

- The **Anti-Money Laundering and Countering Financing of Terrorism Act 2009**: Essentially means that every financial service provider must have prior to registration a proper Anti Money Laundering (AML) policy and manual which conforms to New Zealand Standards as well as an AML officer responsible for implementing this. The requirement is new but is being strictly enforced by the Department of Internal Affairs who visit newly registered FSP's and recommend deregistration if the AML policy is not being properly implemented and the AML officer has not been properly trained.

- The **Financial Markets Conduct Act 2013**: The Act provides the Financial Market Authority (FMA) and the Companies Office wide powers to oversee that financial companies or FSP's are complying with their obligation and not misleading the public. This Act means that an FSP will need to be in the position of regular contact with the FMA and have an office and staff in New Zealand sufficiently capable of dealing with issues as they arise.

- Finally and most importantly the amendment to the **Financial Service Providers (Registration and Dispute Resolution) Act 2008** section 15B means that now the FMA has the power to either refuse registration or deregister any FSP which it considers

  "……will have, or is likely to have the effect of

(a) creating, or causing the creation of, a false or misleading appearance with respect to the extent to which the FSP —

(i) provides, or will provide, financial services in New Zealand; or

(ii) provides, or will provide, financial services from a place of business in New Zealand; or

(iii) is, or will be, regulated by New Zealand law in relation to a financial service; or

(b) otherwise damaging the integrity or reputation of—

(i) New Zealand's financial markets; or

(ii) New Zealand's law or regulatory arrangements for regulating those markets."

This last point is perhaps the most conceptually difficult since the current view is that the financial services must be sufficiently connected to New Zealand via having New Zealand bank accounts, staff and preferably clients. Unfortunately this legislation creates uncertainty since it is uncertain what reputational reasons mean. However that challenge is common to many reputable jurisdictions which grant their governing bodies wide powers to assess whether the financial company should be allowed to provide its services. In our view the real threat of this legislation comes down to the issue of whether the proposed entity will be sufficiently reputable to be allowed on the registry.

Because the legislation is new and involves the cooperation of the different government departments and their legal teams it is expected that initially there will be some confusion surrounding the interpretation of the legislation and its implementation. Having continuously liaised with the various government departments concerning the said legislation Equity Trust now recommends that any application for registration should at least address or implement the following steps:

In order to be registered as a financial service provider in New Zealand a corporation must complete the following steps:

1. It must have a registered and operating office in New Zealand that is defined as a place of business. This means an office set up and established with appropriate brochures, telephone systems, etc to demonstrate that it is a proper and functioning office and not just a premises rented "for show".
2. It must have membership of a dispute resolution scheme, where consumers can complain under section 48 of the Financial Service Providers (Registration and Dispute Resolution) Act 2008.
3. Staff capable of providing their services from New Zealand and capable of being accountable to the regulator. So far as minimum this has meant an office manager in New Zealand doing the AML checks and policy and being ready to comply with the legislation, but ideally a director in New Zealand running the company.
4. It must comply with New Zealand's new anti-money laundering rules, which mean having AML policy in place.
5. It must provide a detailed business plan that addresses the background and reputation of its founders, why New Zealand registration is sought, how it will source New Zealand clients, bank accounts in New Zealand and generally addressing issues which the regulator is interested in.

The above rules are strictly enforced, because New Zealand does not want to be seen as a tax haven and does not want to have its image blackened by international fraud or money laundering. Therefore if you are a genuine international business, who wishes to have an office in New Zealand providing international financial services and are prepared to take the time to go through serious checks as to your credibility, reputation and background, then there are few jurisdictions that are comparable to New Zealand for ease of transaction safety and reliability.

That is because New Zealand is rapidly positioning itself as the Switzerland of the South Pacific with a highly professional and trained population of professionals, who are still relatively affordable, developed infrastructure, extremely reliable legal system, no currency controls and low taxation for non-residents. Over the last few years New Zealand has created a legislative regime to encourage the establishment of funds, look-through companies, trusts and other entities which receive tax free status as long as they are owned by non-residents and do not trade in New Zealand.

With the looming European crisis and the increasingly draconian United States legislation, New Zealand is rapidly becoming a destination of choice for the world's wealthiest companies and individuals looking for stability and safety.

Offshore insurance companies, stock brokers, merchant banking operations, Forex traders and all corporations involved in the finance industry are increasingly considering New Zealand as the jurisdiction of choice for their operations.

Equity Trust has the expertise to take you through all steps of the registration process. We do not take all potential clients, but with those that we do take on we are proud that we have close to a 100% success rate in registration and keeping clients registered.

However with the increasing demands of legislative control and uncertainty many of our valued clients are asking what happens if my registration is denied or delayed, or in the future legislative and regulatory restrictions become too difficult to meet? How do I protect my business from the whims of the registrar?

The real question in all of this is how do I avoid the risks of New Zealand registration whilst keeping the reputational benefits and continuing to trade?

We have worked with our legal advisers and tax consultants to bring you what we believe are the best possible solutions to your structure and one that is forward looking.

CONCLUSION

Although this may be a more costly and cumbersome process than "cheaper" jurisdictions, the advantage of working in a well regulated, reputable and accountable jurisdiction is more than compensated by the respect and trust of clients.

Structure

The best structure for your FSP

There are a number of challenges being faced by the financial services industry in New Zealand which you should be aware of. These include:

- Constant increasing regulation where the regulators wish to be convinced that the FSP is actually doing business in New Zealand;

- Tax compliance and increasing oversight of the income and profits of the FSP and an attempt to deem all income as New Zealand sourced income thus exposing the structure to tax liability; and

- Increased surveillance of anti-money laundering legislation.

In order to mitigate the risks of your structure being deregistered due to non-compliance with any of the above and as well to provide an effective tax solution, we have come up with a structure that optimizes the benefits of a New Zealand FSP registration whilst minimizing the risks and costs associated with a New Zealand jurisdiction.

The Limited Partnership

The limited partnership was designed as an investment vehicle for offshore investors to fund international transactions through a New Zealand structure. Essentially it involves two or more companies connected by a partnership agreement which regulates the distribution of profits .

Under the Limited Partnerships Act the requirements are that:

A. There must be at least one general partner who is a New Zealand resident (usually a New Zealand company) - however there can be other general partners from other jurisdictions; and
B. There must be at least one limited partner from any jurisdiction physical or legal persons, bodies or trusts.

The general partner runs the business of the limited partnership but the limited partners are deemed by law not to be actively involved in the conduct of the business and their details are secret on the registry. Thus the limited partnership provides ideal confidentiality and protects the limited partners from liability for decisions of the general partner.

The limited partnership agreement also can allocate the share of profits between the New Zealand general partner and the limited partner thus minimizing tax liability or in some cases eliminating it all together.

Thus the FSP is registered as a Limited Partnership with its documentation tailored in such a manner that its profits are attributed to an offshore limited partner –the structure can become zero tax rated from all non-New Zealand sourced income.

Further if the FSP is registered as a limited partnership and the general partner as a look-through company and the partners or shareholders are not taxed, domiciled or resident, then the profits of the FSP can be attributed to its shareholders, and this tax is paid at the place of registration of the partner or shareholder. According to the Limited Partnerships Act 2008 and the Income Tax Act 2007 the limited partnership and look-through company attribute the losses and income to their shareholders not to the company.

As long as the shareholders are not tax residents of New Zealand, they will pay tax in their country of residency.

As long as the Company does not make money from New Zealand sources, it follows that the FSP is not taxed in New Zealand in the same manner as the trust regime for non-resident trusts.

The potential for tax structuring created by this regime is immense. The FSP can borrow money from its own shareholders and then invest this money into property, shares, etc, and then repay the loan at interest to a non-resident trust, whose beneficiaries are the shareholders, thus providing both tax minimization and asset protection simultaneously.

We suggest registering a limited partnership made up of at least two companies

A) a New Zealand general partner; and

B) a Vanuatu or Belize limited partner (please note you can have more than two e.g. add a physical individual such as a trader or other physical person to the partnership).

The Vanuatu or Belize limited partner will themselves obtain a license to be registered as an FSP in their home jurisdiction. In this way generally trades can be deemed to be carried through the limited partner structure and thus zero tax is paid on profits via trading.

The general partner is a New Zealand company which will carry out the role of marketing, client relations and client conduct. The general partner will generally receive a fee for the conduct of the business and have its office, staff, etc in New Zealand.

Either the limited partnership itself or the general partner will be registered on the New Zealand FSPR.

This structure has the following general benefits:

A. Tax Minimization: since the relevant contractual documentation and partnership deed will reflect the fact that all profits are paid to the limited partner via offshore activities, there will be generally no New Zealand tax consequences apart from the fee paid to the general partner (which can be small) on which it deducts wages, office expenses, etc. to basically pay little tax. Since Belize or Vanuatu do not tax international income it follows that all income from trading will be tax free.

B. Regulatory and compliance streamlining: The New Zealand regulator can be demonstrated that trading activity is carried out by an offshore licensed entity (the limited partner) and thus AML issues and other regulatory issues are minimized. At the same time the regulator can see that the New Zealand office is carrying out the functions of marketing and administration, thus ensuring the need for a New Zealand entity and FSPR registration. The added benefit is that even if the regulator does attempt to deregister the entity, business is not affected at all since the limited partnership is still trading through its limited partner's license.

For current clients we are offering this structure for a minimal fee and we guarantee it will save you far more in compliance and tax issues. Further the same set of accounts can be created for the limited partnership that can be used both by the general and limited partner, thus saving you further.

Below is a diagram as to how this will look like.

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