charter square

THE COMPARATIVE TAX

TREATMENTS OF INVESTMENTS IN NEW ZEALAND SUPERANNUATION FUNDS

Investors are now more conscious of their post-tax investment returns, especially when recent financial market performance is considered. An investor transferring a pension from the United Kingdom (or indeed someone with an existing New Zealand superannuation scheme that is moving overseas) has a number of factors to consider in determining what after tax performance will be, including:

- Whether they are a transitional resident (or non-resident)
- Whether the fund is a zero-rate portfolio investment entity (PIE), PIE or non-PIE fund
- Whether they will be invested in offshore assets or not
- Are the investments going to be denominated in foreign currency

Each of these points requires careful consideration, which we individually explore in this paper.

Transitional (and non) residency is crucial in determining which schemes to transfer a UK pension to

Transitional (and non) residents accrue a significant tax advantage by transferring their United Kingdom pensions into a zero-rate PIE as opposed to a PIE or non-PIE fund. In a zero-rate PIE the transitional resident can elect to have a 0% tax rate for the period of transitional (or non) residency. This means that their funds can grow free of New Zealand tax during that period. Where significant growth in the funds is expected then this can lead to large tax savings – we discuss this growth later in this paper.

Zero-rate PIEs, PIEs and non-PIEs

A zero-rate PIE is fully invested in offshore investments meaning that investors who are offshore or transitional residents can elect a 0% prescribed investor rate (PIR) of tax. A standard PIE will have a suite of assets that can be invested in, these may include offshore investments. However, because there will also be domestic investments the scheme cannot be zero-rated, this means that there is no 0% PIR available. A foreign investor in a PIE will have a PIR of 28%.

Where the superannuation scheme is not a PIE then the investors marginal tax rate is applied to tax the investment growth on the funds. For offshore investors their marginal tax rate will be 33%. Therefore, if a member of a New Zealand superannuation scheme is considering moving overseas for a period of time it would make more sense for them to be invested in a zero-rate PIE as they would be tax advantaged by moving (paying 0% tax on growth versus between 28% and 33%.)

charter square

THE COMPARATIVE TAX TREATMENTS OF INVESTMENTS IN NEW ZEALAND SUPERANNUATION FUNDS

Foreign investments versus domestic investments

A foreign investment is one that is held outside of New Zealand. For the purposes of clarification, a sterling bank account held with HSBC NZ for example, is not a foreign investment as the account is effectively held in New Zealand.

It is important to understand the distinction between foreign held investments and domestic investments as it affects the tax treatment. Truly foreign held investments, such as overseas bonds, unit trusts etc, fall under the foreign investment fund rules. Therefore, once an individual becomes a resident in New Zealand they can apply to have their foreign investments taxed under the Fair Dividend Regime (FDR)

If the individual is invested in a scheme that has a combination of foreign units and domestic units the individual will be taxed on the holding as if all investments are in New Zealand. Under the foreign investment fund rules the individual can elect to pay tax based on the FDR. Under the FDR the investment is assumed to grow at 5% a year and the investor pays tax at their marginal tax rate or PIR on this assumed 5% growth. Therefore, if the assets are growing at greater than 5% a year the investor has a tax advantage. Any growth less than 5% and the investor is tax disadvantaged.

Investments in foreign currency denominated funds

Under New Zealand law New Zealand superannuation schemes are required to revalue the investors' funds into New Zealand dollars for the purposes of calculating tax (regardless of whether the gain is realised or not). Foreign currency denominated funds includes, sterling bank accounts, which have been popular in the past for receiving the transfer of UK pensions.

The growth in foreign currency investment funds can come in two forms:

- Investment growth in the underlying funds
- Exchange rate growth (where the funds are invested in sterling – either investments or bank accounts)

It is the second point that is most pertinent in this example as a movement in the exchange rates could see the fund appreciate in New Zealand dollar terms by say 20%-30% (as volatility in exchange rates has shown recently).

THE COMPARATIVE TAX

TREATMENTS OF INVESTMENTS IN NEW ZEALAND SUPERANNUATION FUNDS

The tax consequences of all of the previous page are mapped onto the table shown below. This table shows the tax for a year on a $100,000 investment (the investment type is not determined – it could be a sterling bank account) nor is the growth (which is determined by the growth in the funds in New Zealand dollar terms – investment or exchange rate growth).

TAX ON GROWTH ON $100,000 @ HIGHEST RATE

	ZERO-RATE PIE	PIE		NON-PIE	
TRANSITIONAL (OR NON) RESIDENT	PIR 0%	PIR (10.5% > 28%)		MARGINAL TAX RATE (10.5% > 33%)	
> 3% GROWTH	-	840		990	
> 5% GROWTH	-	1,400		1,650	
> 7% GROWTH	-	1,960		2,310	
> 10% GROWTH	-	2,800		3,300	
> 20% GROWTH	-	5,600		6,600	
> 50% GROWTH	-	14,000		16,500	
		OFFSHORE INVESTMENTS	**NEW ZEALAND BASED INVESTMENTS**	**OFFSHORE INVESTMENTS**	**NEW ZEALAND BASED INVESTMENTS**
RESIDENT	PIR ON FDR	PIR ON FDR	PIR ON GROWTH	MARGINAL ON FDR	MARGINAL ON GROWTH
> 3% GROWTH	1,400	1,400	840	1,650	990
> 5% GROWTH	1,400	1,400	1,400	1,650	1,650
> 7% GROWTH	1,400	1,400	1,960	1,650	2,310
> 10% GROWTH	1,400	1,400	2,800	1,650	3,300
> 20% GROWTH	1,400	1,400	5,600	1,650	6,600
> 50% GROWTH	1,400	1,400	14,000	1,650	16,500

TABLE 1: Tax consequences on fund growth in New Zealand Superannuation schemes