

KIWISAVER & TAX UPDATE



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In a nutshell - the easiest option for advice on Kiwisaver or the Portfolio Investment Equity Tax is to call Sheryl on 0800 64 MONEY (0800 646 6639) or email: sheryl@strategies.co.nz



This newsletter was brought to you by Sheryl Sutherland of Women's Financial Strategies, Author of Girls Just Want to Have Fund\$ and Money Money Money Ain't it Funny.

KIWISAVER

There has been a lot of discussion about Kiwisaver but given the tweaking we have seen over the last period confusion still reigns; the following are some of the questions we have been asked.

Who is allowed to join?

Anyone can join Kiwisaver voluntarily. Those who wish to join voluntarily will need to do so by contracting directly with a provider of the Kiwisaver scheme.

Who has to join?

If you start a job as a new employee you are automatically enrolled.

What if I want to opt out of the scheme?

If you join as a new employee you can opt out within the first 2-8 weeks. You can also take a break from saving after 12 months. This can be for a minimum of three months to a maximum of five years.

You can also apply for a financial hardship holiday.

How much do I have to save?

You have to save 4% or 8% of your gross salary. The definition of gross salary refers to anything which is subject to PAYE, redundancy payments, commissions, overtime and bonuses. You can pay additional regular contributions and lump sums. You can also save 4% of a benefit.

Who is managing the investment for me?

There are six "default" managers. This means they were the first to obtain the Government's official seal of approval. They are AMP, ASB, AXA, ING, Mercer and Tower. Other providers have applied for approval and will come on stream in the future. You can change your provider or portfolio as you wish.

Is my investment safe?

Your values will go up and down as markets move. All savings accounts are ring fenced in a trust so in the unlikely event of a provider going broke your savings are safeguarded.

How long do I have to stay in the scheme?

Your funds are locked in until you are 65 unless you suffer from a serious illness, emigrate permanently after 12 months or undergo a relationship separation or bankruptcy.

What is the government offering me?

The Government offers you a \$1000 kick start, a \$40 fee subsidy, and a tax credit up to a maximum of \$20 a week.

What will my employer do for me?

Your employer, from 1 April 2008 has to match your contributions. This starts at 1% on 1 April 2008 rising by 1% a year to 4% on the 1 April 2011 and continuing on at that level.

Are there home purchase and mortgage incentives?

For first home buyers there is a deposit subsidy of \$1000 per year of saving, after three years, with a maximum of \$5000 per account (caps on household income and local house price apply). In addition you can withdraw your accumulated savings to purchase a first home. If you own an existing home you can divert half of your contributions only to pay your mortgage.

How do I know what is happening to my money?

Each person in Kiwisaver will receive an individual report from your provider.

What if I shift jobs?

Your account is completely portable.

Where can I get more information?

The 8 Best Kiwisaver websites are www.sorted.org.nz, www.kiwisaver.org.nz, www.sstlive.co.nz, www.workplacesuper.org.nz/kiwisaver.asp, www.treasury.govt.nz, www.isu.govt.nz, www.sst.co.nz or you can look at www.ird.govt.nz/Kiwisaver.

NOTE: Your employer cannot give you financial advice, due to Securities Law.



KIWISAVER — STEP BY STEP



Know you should be doing something about KiwiSaver, but don't know where to start? SST Money editor Rob Stock shows you how to cut through your inertia and take an easy 10-step route to getting a KiwiSaver account up and running.



Step One: Repeat three times: "This is going to be easy, this is going to be easy, this is going to be easy." It is.

Step Two: Call to mind that the government will chip in \$1000 when you open your KiwiSaver account, that it will also chip in \$40 towards account fees (covers much of the total cost in the first couple of years), and up to \$20 a week matching contributions. Also recall that after a year of saving, you can divert half your contributions towards your mortgage. Remember though, your cash is locked up at least until you are 65 (that would rise if the age of eligibility for NZ Super rises). There are also home loan subsidies for first home buyers. Think about all your family members and whether they should also have a scheme.

Step Three: Check you can afford it by popping onto the www.sorted.org.nz website and putting your details into the quick KiwiSaver calculator. That'll tell you how much 4% or 8% of your salary would be and how much money you're likely to amass saving that way.

Step Four: OK, once sure the budget can stretch to KiwiSaver contributions, check out what kind of fund you should have - growth, balanced, conservative, or cash. To do this use the "risk recommender" at www.sorted.org.nz/calculators/risk-recommender/.

Step Five: Now think carefully how KiwiSaver fits into your plan for building a retirement nest egg.

Step Six: OK, all going fine. Seek out a pen, a copy of an identifying document (passport, driver licence, etc), your IRD number (call 0800 377 774 if you have no record of yours. They'll tell you over the phone), and where needed bank account details for automatic payments.

Step Seven: Choose your route into KiwiSaver. There are in essence three routes in. Step seven describes the first, which is just for employees. Step eight describes the second route, and step nine, the third. The first is to join a scheme at your work. To find out about this simply ask the boss. Many bosses have selected a "preferred" scheme and they will tell you all about it, and give you the paperwork. You fill it in, choose whether to stick in 4% or 8%, select a fund (generally growth, balanced, conservative or cash - those with a long working life ahead of them should choose one of the first two) and hand it back. All the rest is done for you. If you are an employee and there's no preferred scheme, and you are really not up for doing any research yourself, simply fill in the forms and let the IRD pick a "default fund" for you. It will be a "low-risk" fund, which will be pretty tame.

Step Eight: OK, there's no work scheme, you are not an employee or you want to choose a different scheme to the one your boss is offering. Simple. You have two routes: 1. Pay for professional advice, or 2. Take a good look at the guide opposite and use it to draw up a shopping list. Then download the investment statements (which are also the application forms) and give them a good read (Tip: they are dull, so put on a pot of coffee first. Focus on the investment fund, charges and fund managers). There'll be a contact phone number too, if you want to ask any questions. If that all sounds too hard for you move on to step nine.

Step Nine: So that's too hard. Well, just pop into the bank. Each one has a KiwiSaver scheme and can sign you up. All are pretty standard.

Step Ten: Breathe a sigh of relief. It's done. The government has \$1000 to bung into your account and will start chipping in up to \$20 a week, depending on what you save.

Key points:

- Anyone under 65, not just those earning wages, can have a Kiwisaver account providing they have an IRD number.
- Each new account, regardless of who opens it, will get a \$1000 "kick-start" from the government.
- For those over the age of 18, the government will contribute \$40 a year towards fees and up to \$20 in matching contributions.
- The cash is locked up until retirement age, just as for workers.
- Accounts opened for children or grandchildren are held in trust for them until they reach the age of 18.
- Anyone can make contributions to someone else's account. The only limit on contributions is the minimum set by the fund manager.
- Employers have a duty to enable their workers to join Kiwisaver.
- From April 1, 2008, employers will need to match their employee's contributions to Kiwisaver. The contributions will be phased in over four years, starting at 1% of an employee's gross salary and increasing to 4% by April 1, 2011.
- Employer contributions to a Kiwisaver scheme (or a complying superannuation fund) are exempt from Specified Superannuation Contribution Withholding Tax (SSCWT), subject to a cap, the lesser of the employee's contribution or 4% of the employee's gross salary.
- The government will reimburse employers for their contributions to Kiwisaver (or a complying superannuation fund) by providing a matching tax credit up to a maximum of \$20 per week (\$1040 per year) per employee. Employer tax credits will be paid to employers through their PAYE system.
- Sadly for the self employed, they can't claim to be their own boss and make tax subsidised matching contributions, meaning they get less benefits than employees.
- Employers do not have to choose a fund manager to look after all their employee's accounts, but they can. Employees are free to ignore this fund manager and choose their own, while still saving from their pay packet.

Summary

On the face of it, it's a no brainer; we should all be saving 4% of our income to maximise employer's contributions and gain the very rare tax advantages offered by the government. Remember however "salary" includes everything subject to PAYE, such as redundancy, commission, overtime and bonuses, thus your 4% contribution could be around 5-6%, and your 8% contribution could be as much as 10%. Also your savings are locked in until age 65 and you will have a universe of 140 to 180 funds, so advice pertinent to your own situation could be vital in obtaining the best portfolio for your risk profile.

PORTFOLIO INVESTMENT ENTITY TAX

What is it?

The new tax relates to taxation on offshore investments. The new law will tax investors on the first 5% of the change in value of their portfolio each year. It is called the Fair Dividend Rate or FDR. The tax you will pay will be based on your marginal rate.

- ⇒ Commences October 2007.
- ⇒ No capital gains tax irrespective of the amount of trading.
- ⇒ Certainty of tax position.
- ⇒ Maximum tax of 33% (compared with 39% for individuals).
- ⇒ Managed funds now can have some advantages over individual investment.
- ⇒ Many managed funds will look at changing to PIE's.
- ⇒ Cost of an individual direct investor's shares is less than \$50,000.
- ⇒ Does not apply to most family trusts.
- ⇒ Can use 50% of market value at 1.4.07, if shares purchased before 2000.
- ⇒ In a relationship (good, bad or indifferent, marriage, de facto or civil union) you can qualify for a doubling of the threshold to \$100,000. Holdings need to be registered appropriately.
- ⇒ You cannot split your shareholding with your pet cat, no matter how close the relationship.
- ⇒ The \$50,000 is a threshold, not an exemption. At \$51,000-\$51,000 is in the regime not \$1,000



EXCLUSIONS

- ⇒ De minimus.
- ⇒ Certain Australian listed companies.
- ⇒ GPG (5 years).
- ⇒ NZIT (2 years).
- ⇒ Certain Australian unit trusts (ask provider).
- ⇒ Numerous other obscure possibilities.

Who will it effect?

It will affect every investor with more than \$50,000.00 in offshore investments.

What offshore investments are subject to the new rules?

Basically its most shares in companies outside NZ as well as unit trusts and investment trusts.

I have less than \$50,000. What does this mean for me?

See flow chart on next page.

I invest directly, how will it affect me?

You will have to calculate your tax payable once a year.



I invest in a unit trust, how will this effect me?

The tax will be calculated and paid by the fund manager, you don't have to do anything. This tax is good for managed funds if they are classified as a PIE as there will be no capital gains tax irrespective of the amount of trading.

PORTFOLIO INVESTMENT ENTITIES (PIE)

The second big change in tax rules is Portfolio Investment Entities (PIEs). Put simply, PIE is the new name for a type of managed fund. Funds can elect to become PIEs if they meet certain criteria. If a managed fund does become a PIE, there will be some changes to the way it is taxed. Those that do not become PIEs will be taxed in the same way as before. The changes will come into effect on 1 October 2007.

The main change is that PIEs will be taxed at an individual investor's tax rate, rather than at the fund level as before. There are a number of positives for investors, and a few changes to be aware of.

Currently, most managed funds pay tax at 33%, regardless of an investor's tax rate. Under the PIE regime, managed funds that elect to become PIEs will no longer pay tax, but will deduct tax on behalf of investors. The tax will be deducted at the investor's own tax rate (however, this is capped at 33%). This means investors will either be tax-exempt, or pay tax at 19.5% or 33% (depending on their previous year's income).

In addition, under the PIE regime, investors will not pay tax on capital gains on NZ and certain Australian-listed shares.

In a nutshell - the easiest option for advice on Kiwisaver or the Portfolio Investment Equity Tax is to call Sheryl on 0800 64 MONEY (0800 646 6639) or email: sheryl@strategies.co.nz .

PORTFOLIO INVESTMENT ENTITY TAX FLOW CHARTS

Do you have more than \$50,000 in offshore investments?

New FDR rules apply

Has your Total offshore portfolio risen by more than 5% in value during

Yes? Pay tax on the first 5% of gains only

No? Pay tax on the actual gain (as it's under 5%).

Do you have less than \$50,000 in offshore investments?

Exempt from the new rules. The old rules apply

If manager 'redeems' investment, gains are a dividend and taxed.

If manager 'repurchases' investment, gains are a capital gain, not usually taxable.

What is your PIR?

For the year 1 April 2007-31 March 2008, your PIR is the same as your personal tax rate (capped at 33%). After 1 April 2008, a new method of calculation will apply.

The default PIR is 33% and this will apply to all individual and joint investors who:

- ⇒ Have personal annual income from all sources of more than \$38,000 in **both** of the past 2 years.
- ⇒ Are non resident in New Zealand for tax purposes.
- ⇒ Do not provide their PIR to their fund manager
- ⇒ Do not provide their IRD number to their fund manager
- ⇒ The PIR of 19.5% applies to individuals who have personal annual income from all sources of less than \$38,000 in either of the last two years.

The PIR is 0% for Trusts, companies and charities and investment income will need to be included in their own returns. Note that Trusts may elect to use 33% PIR.

How will you benefit from the tax changes in managed funds?

Under the PIE regime:

No tax on capital gains on investments in New Zealand and certain Australian listed shares.

Investors will be taxed at their own tax rate (Prescribed Investor Rate) instead of 33% on both income and capital gains.

39% taxpayers will be taxed at the default rate of 33%.

Direct investments in international shares will be taxed at the Fair Dividend Rate (FDR) of 5% pa of the opening market value irrespective of the actual return.

Are there exclusions?

Yes - there is an exclusion for Australian Shares held in listed companies on certain ASX indices which are tax resident in Australia.

Where can I get help with this?

Contact me on 0800 64MONEY or email sheryl@strategies.co.nz.

SUMMARY

It's not too bad - it gives investors a fairly level playing field. In fact it will benefit some investors.

The first benefit of the PIE regime is for investors on a 19.5% marginal tax rate, as this will be applied to fund returns instead of 33% as at present. Tax payers on a 39% marginal tax rate will continue to enjoy tax on their funds at 33% only.

The second area of benefit from the PIE regime relates to a capital gains derived from New Zealand and Australian shares which will no longer be subject to tax. This is a big improvement on the 33% tax rate that is currently applied.

A third benefit possible through the new tax regime relates to funds holding an offshore investment in a PIE. They will pay tax on a deemed "fair dividend rate" (FDR) of 5% of the value of investments at the start of the year. For managed funds with offshore investments such as some of those managed by Asteron, this tax on 5% of the value at year commencement replaces a 33% tax on the capital gains on offshore holding.

What do investors need to do in respect to these tax changes?

For most investors, the tax changes are not material enough to need to change their investment strategy or holdings in managed funds. As with all new legislation numerous obscure possibilities exist and will surface.

This is a very brief description of the rules which apply to individuals. This information should not be construed as individual tax advice. Investors should seek advice from a tax professional regarding their specific circumstances.

