



**Presentation to the Finance and Expenditure Select Committee on the
Taxation (Annual Rates, Savings Investment, and Miscellaneous Provisions) Bill
13 September 2006**

Ross Butler – CEO – Institute of Financial Advisers

The Institute is the professional body for needs-based financial advisers in New Zealand.

- It has nearly 1,500 members who act mainly as insurance advisers, investment advisers, and financial planners. Members operate in a broad spectrum of commercial entities – small and medium adviser businesses, larger national advisory groups, banks, fund managers, and insurance companies.
- Like any other professional body, we set and monitor standards, provide education pathways and industry leadership, and promote and reinforce values and principles based on the interests of clients.
- With an average of 250 clients each (mainly employed and self-employed individuals, and small to medium businesses), our members look after an estimated 375,000 New Zealanders.
- The Institute has lodged submissions and papers over the past year on a wide variety of issues, including KiwiSaver, the Securities Legislation Bill, Co-Regulation of Financial Intermediaries, Industry Led Dispute Resolution, Anti Money Laundering, and Extreme Salary Sacrifice.

Simon Hassan – President – Introduction to the Issues

Mr Chairman, ladies and gentlemen.

The Institute supports the main objective of this bill: Encouraging New Zealanders to invest by leveling the tax playing field for those who use managed funds.

- So we like the flow through tax arrangement, and
- We support the removal of capital gains tax on Australasian shares.

But the proposal is too complex – encouraging avoidance.

And the tax on 85% of gains on international shares will reward inappropriate and unhelpful investment behaviour:

- Discouraging sensible diversification, and
- Seeing even more cash flow into our overheated, economically unproductive and inflationary property sector.

Ladies and gentlemen, the proposal is flawed. It will reward Kiwi investors for taking more of the wrong sort of risks - dumping an even bigger burden on future tax payers.

And it will hit all New Zealanders, not just the wealthy, as Rob Dowler will show.

Rob Dowler – Adviser to the Institute

Case Study

The newspaper article provided from the New Zealand Herald outlines the story of a couple who will likely incur significant additional tax under the proposed regime.

Immediately prior to retirement they worked as a cargo planner and occupational therapist – jobs that suggest to me employment earnings were not in the 39% tax bracket. I suggest that their combined annual employment earnings were probably less than the individual earnings of anyone around this table, including the three presenters here on behalf of the Institute.

Yet Adrienne and Renee Rickards were able to purchase a modest home in Auckland, raise their family, pay off their mortgage and accumulate sufficient savings in financial assets to provide for a secure retirement – an outstanding example of aspiration and achievement for all New Zealanders.

These are the hard working New Zealanders who wanted to achieve long term financial security, referred to in the Finance Minister's speech of 11 August as "winners" under this regime, but they aren't winners. These are not the sophisticated direct investors that the Minister also refers to, but they are losers.

Mr Chairman, committee members – I know these investors. They were my clients for more than ten years when I was an investment adviser. They came to me with a mortgage-free home, very little in the way of financial assets, but with a strong desire to save for retirement. I advised them, watched them achieve their goals and helped them put in place an effective well diversified investment portfolio of financial assets in addition to their modest home.

I was surprised to see the newspaper article, which simply reflects the very real and justifiable concern that the Rickards have about the impact of this regime on their savings and future income, a concern reflected in the number of submissions received by this Committee.

I am proud to represent Adrian and Renee's circumstance and achievements and others like them to you today. They are an important part of New Zealand's diverse range of electorate constituents that you claim, quite rightly, to represent. I want to ensure that, together, we correctly represent their interests in the final shape of this legislation.

Just as Adrian and Renee are disadvantaged by this proposal, so are tens of thousands (if not hundreds of thousands) of other New Zealanders saving via managed funds, including the proposed KiwiSaver funds. Further, not just direct investors in overseas shares, but savers previously exempt tax on gains through investments in superannuation funds that utilised passive investments, or investors in passive index funds with binding tax rulings, will now incur either directly or indirectly an increased tax burden, thereby further discouraging prudent diversification of investment into offshore equities.

To quote again from the Minister's speech, "It is unconscionable in a global market that we have tax rules that artificially limit what baskets New Zealand investors place their eggs in." We agree.

Mr Chairman, Members of the Committee, - there have to be other solutions, and they are.

Solutions

To deliver on the policy objectives, the Institute proposes solutions as follows:

- Extend the Australasian exemption to all investment in listed international equities to all investors.
- Subsequently, review and improve the clarity of the distinction between investment on capital and on revenue accounts, capturing all investment assets, including investment property.

Alternatively, if the tax changes must proceed along the lines proposed, then:

- Introduce an option for an investor to elect a fixed statutory deemed return approach (along the lines of Mr John Shewan's presentation).
- Reduce the 85% to a much lower figure.
- Consider the detailed suggestions in our submission to improve the proposal.

Thank you, back to Ross Butler, the Institute CEO.

Ross Butler – CEO – Institute of Financial Advisers

As the proposal stands, our members, acting in the best interests of their clients, will be obliged to recommend investment strategies that minimise the impact of tax. This will affect all forms of tax disadvantaged international share investment, whether direct or through managed funds, including KiwiSaver.

The first solution we have proposed delivers explicitly to the policy objectives, by:

- Removing distortions in the taxation of NZ based managed investments, thereby directly encouraging the use of such vehicles without encouraging the development of strategies based around tax minimisation.
- Supporting our members' ability to recommend properly diversified investment using direct shares or locally domiciled managed funds that invest onshore and offshore as dictated by investment considerations and the needs of the client, and or through KiwiSaver.

The second solution outlined, which includes the deemed return option, is, in our view, still second best, but essential if the legislation is to remain along the existing lines.

Thank you for the opportunity provided to present. We welcome questions from the Committee.