September 30th 2024

Submission Response to IRD Consultation
Income tax – Share investments (and related fact sheets)

The NZ Shareholders' Association ("NZSA") appreciates the opportunity to comment on the Consultation paper related to the proposed guidance for investors to be published by Inland Revenue ("IRD") related to share investments.

NZSA is a non-profit entity that advocates for all investors, regardless of age or experience. Our aims are to protect, enable and reward investing, and to promote fair markets.

NZSA'S VISION IS TO BE A TRUSTED AND RESPECTED VOICE FOR ALL RETAIL INVESTORS

OUR AIMS:
- To represent, protect and promote the interests of investors in shares and other Investment Products
- To promote and encourage an active, efficient, fair and transparent market for raising capital and trading shares and other Investment Products

*…supported by our **Values***

Independence	Advocacy	Respect	Inclusiveness	Evidence-based	Outcome-focused
Our independence is our key point of difference, driving our credibility and objectivity	*Our advocacy supports all investors and the constructive improvement of listed markets*	*The way we behave earns respect*	*We are a friendly, welcoming space for all investors, no matter their background, status or experience*	*We make decisions based on evidence and best practice*	*We remain focused on delivering our mission*

NZSA Context and General Policy Commentary

NZSA has been vocal in stating that taxation structures should **not** take a significant role in investment decision-making. This does not mean that tax becomes irrelevant for investors – but that taxation is levied appropriately on individuals or entities, regardless of investment structure.

We recognise that the IRD must apply taxation based on legislation – nonetheless, we believe it is relevant to set out NZSA key positions related to tax policy in addition to commenting on the proposed guidance materials.

NZSA would welcome further engagement with Government on these matters.

1. **Tax rates and structures:** We note the recent changes to rates of taxation applied to Trusts, as part of the *Taxation (Annual Rates for 2023-24, Multinational Tax, and Remedial Matters) Bill* enacted by Parliament in March 2024.

   NZSA made a submission on this proposal in July 2023 (see link) and also appeared at the Select Committee hearing in January 2024.

   In that submission, NZSA noted the following:

   a) that the introduction of a trust tax rate of 39% would introduce a level of differentiation with the lowest tax option for investors (PIE funds at 28%) that would further disadvantage individual direct investors;

   b) that top tax-rate investors operating through different structures now faces tax rates between 28% – 39%, with the proposed Trust tax rate at the top of that range;

   Our conclusion in this particular submission reflected our key policy position: that **"a more holistic review of taxation rates is required to address imbalances and biases between different investment approaches and create a level playing field for different investment structures. This should include consideration of simplification of tax structures to encourage fairness and minimise scope for tax minimisation."**

2. **Unconscious Bias**: Linked to our comments above, we note that over time, taxation rates have come to incentivise professional 'fund' structures (and their fees) rather than individual investors. For example:

   a) While individual investors pay up to 39% on taxable income, PIE rates are capped at 28%.

   b) While individual investors are subject to an "intention test" on purchasing shares as to whether any capital gains are taxable, institutional investors, fund managers and wealth managers are not subject to that same test.

3. **Capital Gains:** NZSA believes that the current 'fear' of individual investors to be subjected to taxable income (at their marginal income tax rate) when selling shares for a capital gain has played a significant role in listed companies and other issuers prioritising delivery of dividend income over the longer-term growth provided by capital re-investment.

   NZSA believes this has had a long-term impact on capital and/or investment productivity, reflecting poorly on New Zealand's wider productivity performance.

   This reinforces the NZSA view noted above, in advocating for a holistic review of taxation rates and structures.

4. **Foreign Investment Fund (FIF) regime**: The FIF regime is New Zealand's only wealth tax. While its original intent was laudable, we believe this now acts as a disincentive for New Zealand investors to fully diversify their portfolios.

   Additionally, NZSA fields much feedback from investors relating to the complexity of its administration.

NZSA would prefer to see the FIF regime included within the scope of wider taxation reform.

5. **Mutual recognition of Imputation and Franking Credits across New Zealand and Australia**: Again, NZSA considers that the lack of recognition acts as a disincentive for New Zealanders / Australians to invest in each other's listed entities. This lack of recognition is effectively a form of 'double taxation' across both jurisdictions.

NZSA Response to Consultation

1. **Overall Commentary:** NZSA is concerned that a heavily-worded guidance will result in exacerbating the continued transition of 'DIY' investors to managed funds. As such, we believe the guidance document should focus on communication of obligations, education and engagement. Longer-term, we believe a vibrant pool of investors is healthy for the New Zealand economy and its investment productivity.

2. **Clarity**: NZSA appreciates any documentation or guidance that creates **clarity** for investors.

   a) We believe that any guidance provided will add value to ALL investors – regardless of experience.

   b) We recognise that 'new' investors are those most likely to be in need of information as regards their tax obligations. On this basis, we believe that materials should be more focused on a "communications" approach rather than legalistic principles (while of course reflecting the spirit and intent of the law).

   c) We believe that the use of simple "1 page" flowcharts (as contained within the FIF rules fact sheet) will help to add clarity to the wider document.

   d) References to case law, while great for lawyers, is unlikely to be helpful to most individual investors, and is likely to lead many to conclude there is greater complexity than in reality.

2) **Enforcement Approach:** NZSA believes that the IRD should state the extent to which any enforcement action associated with these guidelines will be balanced between education, remediation of wrong and punitive action.

3) **Taxable Share Gains:** As noted above, we believe that the current tax regime related to capital gains for share investors is confusing (pages 12-20 in the consultation document), even for experienced investors.

   a) NZSA believes there should be a clear series of tests that are able to be relied upon by investors. We note that the guidelines provided offer some clarity in the context of current legislation, although would benefit from a 'flowchart' approach (see above) to support communication.

   b) Nonetheless, we believe that significant interpretation is still required by investors, that may lead to differences of opinion between the Commissioner and investors. The example below is from section 11 of the consultation document (emphasis added):

      > *An investor who acquires shares for the **dominant purpose of disposal** is subject to tax under s CB 4 when the shares are sold. When deciding what an investor's dominant purpose was at the time they acquired shares, what they say their purpose was is tested against a combination of objective factors. This includes the **nature of the asset***

***(that is, the type of shares purchased and what rights they give the holder)**, the **length of time** the shares were held, the **circumstances of the purchase and disposal** of the shares, and whether there is a **pattern of purchases and sales** suggesting there was a dominant purpose of sale.*

c) While some of these concepts are further defined in later sections, NZSA believes there remains significant grounds for interpretation.

d) For examples, section 14 states that there is no bright-line test for share sales, so there is no set amount of time shares are held or number of trades required for sales to be taxable. While a statement of fact, it is still possible for an investor who believes they are not liable for taxable income on selling shares to be assessed by IRD as incurring taxable income.

4) **Deductions where taxable income from share sales is not the dominant purpose:** We believe that further clarity should be provided around deductions able to be claimed under different scenarios. Specific questions may include;

   a) If an individual (or company or trust) is acquiring shares with the dominant purpose of receiving taxable income from dividends either now or in the long-term, can brokerage be claimed?

   b) If an individual (or company or trust) takes out a loan to further long-term investment objectives, with the dominant purpose associated with building a long-term taxable dividend stream or long-term wealth, is the interest deductible?

   While the document offers clarity on deductions in the context of taxable income from share sales (s.77), there is no statement as to the treatment of expenses relating to where taxable income from share sales is not the dominant purpose.

Thank you for your consideration of NZSA's submission. I am very happy to follow-up with any questions, commentary or support for further developing these materials as required.

Regards,

Oliver Mander
CEO, NZ Shareholders' Association

September 30th 2024