

**INVESTMENT SAVINGS & INSURANCE ASSOCIATION OF NZ
INC**

Submission
to the
Finance & Expenditure Select
Committee
on
Supplementary Order Paper 130
to the
Taxation (Annual Rates, Business
Taxation, KiwiSaver, and
Remedial Matters) Bill

30 August 2007



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INVESTMENT SAVINGS & INSURANCE ASSOCIATION OF NZ INC

SUBMISSION TO THE FINANCE AND EXPENDITURE SELECT COMMITTEE ON SOP 130 TO THE TAXATION (ANNUAL RATES, BUSINESS TAXATION, KIWISAVER, AND REMEDIAL MATTERS) BILL

1.0 Introduction

The Investment Savings and Insurance Association (“ISI”) appreciates the invitation to comment on Supplementary Order Paper 130 (“SOP 130”) to the Taxation (Annual Rates, Business Taxation, KiwiSaver, and Remedial Matters) Bill (“the Bill”).

ISI represents the issuers and managers of life insurance, superannuation and managed funds that in total have responsibility in excess of \$50 billion of managed fund assets. ISI made a written submission on the Bill in July and made an oral presentation to the Committee on 15 August 2007.

We appreciate the willingness of officials to discuss the industry’s concerns with aspects of the legislation that are considered not to be workable.

We recognise that SOP 130 is intended to address only a limited range of issues and is not a response to the points made in respect of the KiwiSaver-related provisions in the Bill in our earlier submission. However, we feel that the comprehensive solution recommended in that submission would be a more appropriate approach.

As well as providing this written submission ISI requests the opportunity to make a further oral presentation to the Committee.

2.0 Key Points

- Our submission on the Bill recommended amendment of sections 68C (2), (3) and (4) of the Tax Administration Act to replace the requirement for a provider to furnish a claim to IRD with a requirement for providers to supply IRD with sufficient information to enable IRD to calculate the member’s tax credit for the tax credit year;
- SOP 130 provisions regarding fund provider claims for member tax credits would be unnecessary if the calculation were done by IRD;
- The processes necessary for fund providers to claim member tax credits are complex and costly to implement. The proposal would have these costs replicated across 50 odd fund providers and administrators. It is vastly more efficient for the

central administrator to perform this function, particularly as IRD needs to receive all necessary information to calculate the tax credit and ensure that no more than the maximum is claimed – ie IRD as central administrator will be in possession of all of the information and be in a position to perform the calculation;

- In the event that the above recommendation is not accepted, SOP 130 should be amended to provide for only one method for establishing the relevant period of membership for the calculation of the tax credit;
- As many of the issues raised in submissions on the main Bill and the SOP relate to the efficient and practical administration of schemes from 1 October 2007, consideration should be given to speeding the passage of the Bill to reduce the uncertainty that would otherwise result during the period from 1 October until the Bill is passed.

3.0 Claiming Member Tax Credits

3.1 Sections 68C (2) (3) and (4) of the Tax Administration Act require a fund provider to claim a tax credit for a member by making a member tax credit claim to the Commissioner of Inland Revenue, in the form prescribed by the Commissioner.

3.2 The requirement for the claim to be calculated by the fund provider creates a number of risk areas which can only be alleviated by significant additional investment in registry systems, substantially increasing the overall cost of implementation and administration. In comparison to the cost incurred by providers to establish initial KiwiSaver systems and processes, the additional cost is substantial. KiwiSaver project personnel from the group of six default providers have estimated the implementation cost at an additional 50% of the amount required to establish KiwiSaver for commencement of operations on 1 October. Every provider will need to incur this cost.

3.3 The most efficient approach to determining claims across the whole KiwiSaver scheme is for the calculation process to be consolidated with Inland Revenue in its role as central administrator, with providers supplying supporting information. ISI recommends that the calculation of the member tax credit should be undertaken by IRD rather than by the fund provider. Fund providers will be responsible for supplying IRD with information for each eligible member on:

- The contributed value of any eligible contributions for the member tax credit year received directly by the provider and not been received via the IRD.
- The amount of contributions diverted for any mortgage diversion facility in place for the member.

3.4 Our reasons for this recommendation are as follows:

3.4.1 IRD, as the central administrator, needs to maintain a comprehensive picture of member details and contributions as, at the end of each year, it will need to determine that no more than the maximum member tax credit is claimed. The calculations referred to in new section KJ3 define "member credit contributions" as inclusive of both KiwiSaver and Complying Superannuation Funds ("CSFs"). Members may be with more than one fund provider (KiwiSaver and CSF) and therefore a single fund provider has no way of knowing the 'whole client' view.

3.4.2 As IRD could potentially hold 3 months worth of eligible KiwiSaver contributions that have not yet been paid to a KiwiSaver provider, the fund provider would not be able to make a claim for the full entitlement until all contributions for the Member Tax Credit year were received from IRD. The fund provider can only base a claim on information held by them at the time of calculation. Consequently, some members will not receive their full credit unless the claim is delayed for 3 months or a subsequent claim is made. This will inevitably cause confusion and concern amongst members and result in increased call centre workload. There is also the possible loss of investment earnings on tax credits that could be claimed earlier but are delayed under the current structure.

- 3.4.3 IRD would be able to do the calculation immediately upon receipt of information regarding contributions received direct and details of any mortgage diversion facility and the full tax credit payment could be made shortly after the end of the year. This is because IRD has full visibility of any KiwiSaver contributions received but held in its holding account at the end of the claim year and, having been furnished with the directly received contribution details and mortgage diversion figures from providers, is in possession of all the information needed to calculate a claim.
- 3.4.4 In order for KiwiSaver providers to calculate member tax credit claims, every contribution will need to be flagged to identify which member tax credit year it applies to and whether it has already been claimed for. This is a significant structural change to registry systems and will be expensive to implement. Further, the structural changes will need to be made by each and every provider.
- 3.4.5 In order to manage member tax credit claims, each fund provider will need to put in place administration systems to track eligible contributions and member tax credits received so that these can be advised to new providers when the member transfers. If the member transfers to another provider, that information will need to be transferred to the new provider. The transfer of information between fund providers creates an opportunity for error that is unnecessary as IRD holds the information required for it to both perform the calculation and see the value that was given to each member
- 3.4.6 This requirement for fund providers to calculate the member tax credit claim will increase the complexity and ongoing administrative cost of running all KiwiSaver and Complying Superannuation Funds. The attached diagrams illustrate that complexity in comparison with the simplicity of having the calculation done by the central administrator.

4.0 The Member Tax Credit Start Date

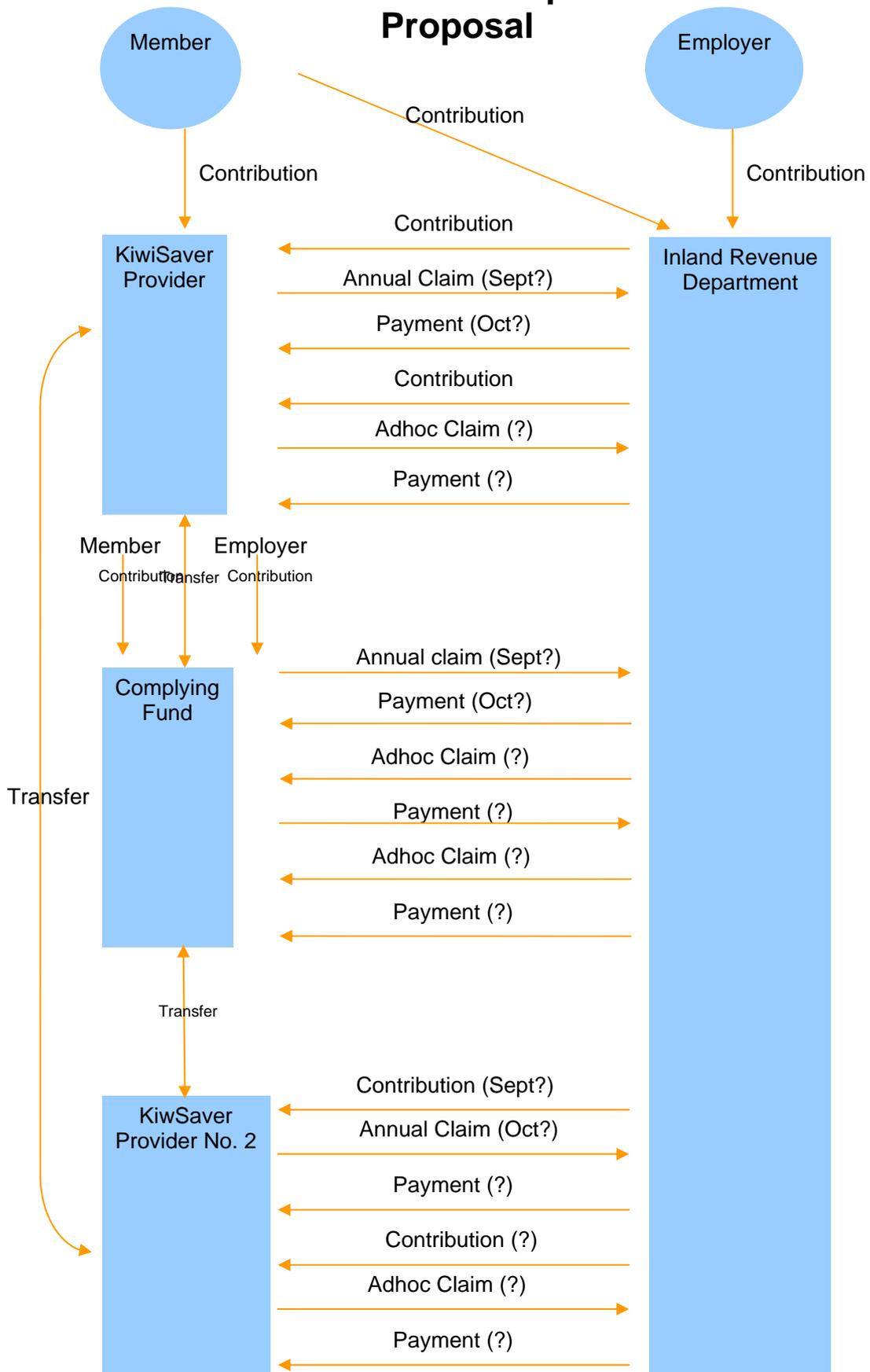
- 4.1 SOP 130 establishes rules to determine the date on which a member's eligibility for the member tax credit starts. In order to ensure that no one is able to pay a one-off contribution of \$1042.86 in June 2008 and claim eligibility for a full year's tax credit, separate rules apply for certain members.
- 4.2 While for most members their member tax credit start date will be the first day of the month in which deductions commence from wages, those members joining via a chosen provider in the period from 1 July 2007 to 1 October 2007 (where the fund provider has received a valid membership application form) will have a different tax credit start date depending on when their first contribution was received.
- 4.3 That will require KiwiSaver fund providers to set up additional systems to distinguish those members who join before 1 October 2007 and contribute before 31 October 2007 from those who join before 1 October but do not contribute before 31 October. Those processes and system changes set up for the interim period will then become obsolete.

4.4 The substantial additional administrative burden that this requirement will cause for fund providers is out of proportion to the benefit for the Government of preventing a limited number of people from paying \$1042.86 in June 2008 and receiving member tax credits for a full year rather than one month.

4.5 We strongly recommend that SOP 130 should be amended to create only one rule for determining the member tax credit start date.

4.6 As noted above, the need for fund providers to set up additional systems to distinguish members joining before 1 October but not contributing before 31 October would be removed if the member tax credit calculation was done by IRD rather than by the fund provider and we strongly urge the Committee to consider our recommendation to that effect. Removal of the interim period requirement would not remove the need for fund providers to categorise members so that they can establish their start date and store that start date.

Inland Revenue Department Proposal



Providers Proposal (courtesy of ING)

