Tax Working Group Public Submissions Information Release

Release Document

September 2018

taxworkinggroup.govt.nz/key-documents

Key to sections of the Official Information Act 1982 under which information has been withheld.

Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

[1] 9(2)(a) - to protect the privacy of natural persons, including deceased people;

[2] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage.

Where information has been withheld, a numbered reference to the applicable section of the Official Information Act has been made, as listed above. For example, a [1] appearing where information has been withheld in a release document refers to section 9(2)(a).

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

Sharesies

Sharesies Limited
[1]

27th April 2018

Tax Working Group Secretariat
Po Box 3724
Wellington, 6140,
New Zealand

About Sharesies

Sharesies is a low cost investment platform. We give investors with $50 the same investment opportunities as someone with $50,000. We want to make this generation the most financially literate in history, starting with making investing easy.

In the 10 months since launch, Sharesies has attracted over 14,000 investors (80% of who are under the age of 40) and had over $15m invested through our platform across 9 Smartshares ETFs (listed PIEs), and 2 Pathfinder Investment Funds (multi-rate PIEs).

3. Purposes and principles of a good tax system. How would you define 'fairness' in the context of the tax system? What would a fair tax system look like?

Introduction:

The Tax Working Group has asked what a fair tax system looks like, and at Sharesies we do not believe the current tax system is fair in its treatment of Listed PIE and multi-rate PIE (MRP) investments. We would like to bring the following to the Tax Working Group's attention.

A growing group of investors are paying too much tax on Listed PIEs because their effective tax rate is less than 28%. This group doesn't have the same benefit as investors in a MRP who are able to receive cash refunds for excess imputation credits.

Example:

Sarah[1] is 18 years old and earns less than $14,000 annually working holiday jobs while studying at University. Her effective tax rate is 10.5%. She decides to invest $1,000 through Sharesies into a range of Listed PIEs and is subsequently taxed on income at a flat rate of 28%. Sarah ends up overpaying her tax by 17.5% and is unable to receive a cash refund. Instead she has to file personal income tax returns to obtain the benefit of excess imputation credits. Even then, the credit is offset against tax payable on other income and may not be realised until a later

[1] Sarah is a fictional example of what a Sharesies investor could look like.

financial year. If Sarah had invested into a MRP then she would have used her prescribed investor rate (PIR) of 10.5%, paid the correct amount of tax and received a cash refund from Sharesies of excess imputation credits for that financial year.

Discussion:

Sarah's example highlights a situation where investors who have previously been underserved and excluded from participating in the financial markets are being exposed to tax at a much higher rate and having to file an income tax return to arrive at their correct tax liability for the year. There is also potential for deadweight taxation cost where an investor on a low effective tax rate is induced into investing into a MRP over a Listed PIE because they are not in a situation where they overpay tax and receive cash refunds for excess imputations. This problem is amplified if a financial service provider was to offer investments for children as the majority of investors would have no income to offset excess imputation credits when investing in Listed PIEs.

Sharesies strongly believes in making it as easy as possible to pay tax. We also believe that the tax system should be balanced and fair, and make it easy to claim refunds for our investors where tax has been overpaid. Before we started Sharesies, we interviewed over 5,000 people and asked them this question: "If I gave you $50 right now, and you had to do something with it in the next 5 minutes what would you do?" Bills, online shopping, coffees, vouchers, food, cigarettes and beers were all more popular options. None of them said invest it. Because investing isn't something you could do with $50. For someone in this situation investing becomes even less attractive when you realise you're paying tax at a higher rate and that investments are not treated similarly for your income level. In contrast people who are high income earners and pay tax at an effective tax rate of 33% receive benefit from the taxation of Listed PIE and multi-rate PIE investments which have the highest rate of 28%.

Proposal

Sharesies suggested solution to achieving fairness between investing in a Listed PIE and a MRP is to allow companies like us to act as a Portfolio Investor Proxy for Listed PIEs as well as MRPs. The benefit of this approach is that companies like Sharesies will perform tax calculations to facilitate cash refunds of excess imputation credits for investors in Listed PIEs for the year in which the excess imputation credits arise. This would remove the need for investors to file personal income tax returns to obtain the benefit of excess imputation credits.

Why does this matter?

The typical kiwi investing story is largely focused around 'getting on the property ladder'. Saving enough for a deposit for your own home, and then investing in a second 'rental' property once you've knocked off a bigger chunk of the mortgage. But, with property prices rising, home ownership is becoming less attainable and affordable. The reality is most kiwi's will be unable to own their own home (including people who earn really good money). Of the people we spoke with, the majority would choose to spend their money than put that $50 towards house savings — because homeownership just feels too far away. But without an alternative way to invest their money, people are struggling to get ahead.

Historically there have always been investment options available, but they're not accessible to people who don't know anything about investing. Only 25% of people we spoke with said they knew where to go to start investing. They also felt like they needed a lot of money to get started, needed to know more, and there were too many hoops to jump through before they can get started. Traditional fund managers are focused on 'wealth management' not 'wealth development'. But everyone we spoke with, wanted to be an investor.

We saw this as an amazing opportunity and one that brings us to this point. At present, Sharesies must communicate the details of any excess imputation credits received from Listed PIEs to investors, for them to include in their yearly tax returns if they choose. If a tax credit applies, the excess is used to offset against tax on taxable income in that year or a future year. We know that we have investors paying to much tax in this scenario and believe that it is our responsibility to ensure they are served fairly by the New Zealand tax system.

We remain open to contact from the Tax Working Group or Secretariat to discuss points raised.

Kind regards,

Leighton Roberts [1]

Hardy Michel [1]