Tax Working Group Public Submissions Information Release

Release Document

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

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

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FUTURE OF TAX: PUBLIC TRUST SUBMISSIONS

Public Trust welcomes the opportunity to comment on the Tax Working Group's Future of Tax: Submissions Background Paper.

About Public Trust
Public Trust is New Zealand's largest and most experienced trustee services organisation. We are best known for our expert Wills and estate administration services, but also offer Kiwis a full range of estate planning services, including legal, financial, investment, trusts, and estate protection. We operate through a network of 23 customer centres around New Zealand.

Our specialist advice has helped thousands of families and businesses look after what's important to them – we're all about encouraging New Zealanders to preserve the present and secure the future.

Impact of proposed new taxes on Public Trust's customers
Public Trust has considered the specific challenges raised in the Working Group's background paper from the perspective of our customers, with a particular focus on the impact of a capital gains tax and land tax. We are concerned that a capital gains and/or land tax may unfairly overburden one group of New Zealanders and may have unintended consequences for many of our customers.

Public Trust manages over 4500 life interest estates and trusts, and the average age of our trust settlors is 59 years. We also manage 25 farms.

Most of our customers have lived through a share market crash and a global financial crisis that have driven them to save and invest in a particular way under the current tax regime. Many of them are also retired or close to retirement age with minimal income and therefore have limited scope to change their current investment approach to accommodate a new tax regime.

We believe that the introduction of a capital gains tax and/or land tax may have unintended consequences for many of our customers, including the following, which we would encourage the Working Group to consider in its assessment of any such taxes.

1. <u>Increased rental costs</u>
   a) Many of Public Trust's customers are elderly and/or vulnerable, so are not in a position to purchase a property. We expect that such customers have limited ability to adjust to

increased rents and will struggle to meet higher rents that could occur as a result of a land tax, with their limited income. As a consequence, they may be forced to rely on social welfare to supplement their income or on the health system for accommodation

2. <u>Impact on vulnerable customers and their family members</u>
   a) A similar situation could occur where a customer moves into residential care but retains their property for a family member (who is often in a vulnerable position) to live in or to provide income to pay for their residential care. If the property is no longer deemed a 'family home' (because it is held in a trust or life interest estate) the customer may be left with a land tax they cannot afford due to limited cash flows, which may result in the sale of the property. Any family member living in the property will need to find alternative accommodation and may also be forced to rely on social welfare for supplemental income or the health system for accommodation.

   b) If the land of a retirement village is subject to land tax, we expect that the cost will be passed on to the retirement village residents. Again, these residents have limited income to cover the increased cost.

3. <u>Potential impact on farms</u>
   a) Public Trust currently manages 25 farms. As tax on farms is within the scope of Working Group, a land tax may significantly increase the cost of owning and operating a farm given the extensive land that they operate on. Farmers may not have the cash flow to pay for any land tax.

4. <u>In the context of a trust or estate, who bears the cost of a land tax or capital gain and when it is paid</u>
   a) As an example, Public Trust has a number of life interest estates where a will maker allows a spouse or other family member to live in their property for the rest of the spouse/family member's life. A life interest estate can last for more than 20 years, over which time the property is expected to increase in value. If the property is no longer considered the 'family home', the final beneficiaries (who receive the property when the life tenant dies) will either be expected to cover land tax for the duration of the life tenancy (without having any benefit of the property), or if capital gains is paid on realisation, they will be left with a large tax bill to pay.

   b) There could be further tension between the income and capital beneficiaries of a trust or estate. For example, if a life interest with a share portfolio is subject to capital gains tax, the life interest holder will receive the income but the final beneficiaries will be taxed on any capital gain on the underlying shares, while not receiving any income benefit during the term of the life interest.

5. <u>Impact on investment approach</u>
   a) A tax on realised gains (consistent with most capital gains tax regimes worldwide) may distort the buy and sell decisions of investors. Such a tax may encourage investors to avoid selling investments in an attempt to delay or forgo the requirement to pay the capital gains tax. This is turn may lead to imprudent asset allocations, especially for aging investors, who may be best served with low-risk, income generating investments, but may be unwilling to sell their high risk, non-income generating investments, especially if these have been held for a long time and have seen significant gains since acquisition.

Administrative challenges with proposed new taxes
We expect that the introduction of a capital gains or land tax will result in increased costs to customers (in addition to the cost of the tax itself). There will also be additional complexity relating to numerous maters, including the following which affect our customers, which would require careful consideration and clarity:

1. the definition of 'family home'. A clear definition is required for 'family home' or 'owner occupied home', particularly in relation to life interest estates and trusts;
2. considering if the cost of property improvements is tax deductible against the capital gain. The cost of a capital gains tax to the customer will include determining/recording the cost of improvements, determining the extent of any tax deduction and obtaining market valuations on a more regular basis; and
3. property held in a trust or life interest estate with multiple beneficiaries. There may be a situation where some beneficiaries dispose of their share which is taken over by the other beneficiaries, and the beneficiaries who maintain or increase their share of the property are subject to capital gains tax.

Other suggestions
We also have a broader change that the Working Group may wish to consider:

1. <u>Tax concessions on passive income</u>
   To incentivise saving and investment and to enable those who are dependent on passive income (especially retirees) to earn greater after-tax income to cover their living costs, the Working Group may wish to consider introducing a tax free savings scheme (such as an Individual Savings Account (ISA) in the UK).

Conclusion
In summary, we would encourage the Working Group to consider that any capital gains or land tax may unfairly overburden one group of New Zealanders and result in unintended consequences and complications for Public Trust's customers, most of whom are not in a position to fund the additional tax. We also encourage the Working Group to carefully consider the impact that a capital gains or land tax would have on New Zealand's vulnerable population in the situations we have outlined above.

Thank you for considering our submission. Please do not hesitate to contact us if you require any further information on the matters raised.

Yours sincerely
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