February 2014

Proposed foreign superannuation tax rules – transitional measures fact sheet

The information in this factsheet is for people who:

- withdraw their foreign superannuation as a lump sum or transfer their foreign superannuation to a New Zealand or overseas superannuation scheme between 1 January 2000 and 31 March 2014 and did not comply with the rules that applied at the time they made the withdrawal or transfer; or

- have filed an income tax return declaring foreign investment fund (FIF) income or loss for their interest in a foreign superannuation scheme before 20 May 2013.

Taxpayers who have not withdrawn or transferred their foreign superannuation do not have to do anything until they do so.

Taxpayers who have made a withdrawal or received a pension and have correctly complied with the rules as they applied at the time do not need to do anything.

Introduction

The current rules for taxing people who move to New Zealand on their foreign superannuation can be complex and difficult to understand, and do not always result in a fair outcome. Some people who have interests in foreign superannuation schemes, or who have withdrawn or transferred their foreign superannuation interests in recent years, have not complied with their New Zealand tax obligations. To address these issues, new rules for taxing foreign superannuation are proposed in the Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Bill. The proposed new rules are intended to be simpler and easier to comply with than the current rules.

Proposed changes

- For people who have made a lump-sum withdrawal or transfer and have not met their tax obligations, a transitional provision is proposed to allow people to meet their past tax obligations by paying tax on 15% of the amount transferred or withdrawn.

- For people who have previously complied with the FIF rules in relation to a foreign superannuation interest, "grandparenting" provisions are proposed which will allow those rules to continue to be available under certain conditions.

15% option for lump-sum withdrawals from 1 January 2000 to 31 March 2014

A withdrawal from a superannuation fund is generally a taxable event (unless the foreign superannuation interest is an interest in a FIF). Withdrawals include transfers to another superannuation scheme in New Zealand or overseas. The proposed legislation contains a transitional provision to help people who have not met their tax obligations in the past to comply with those obligations, that is, paying the required tax on the withdrawal or transfer.

The proposed transitional provision will allow people to meet their past tax obligations by paying tax on 15% of the amount transferred or withdrawn. The remaining 85% of that sum will not attract income tax.

This option will be available for lump-sum transfers and withdrawals made from 1 January 2000 to 31 March 2014.

If the person can show that they have applied to the overseas scheme by 31 March 2014 for release of their funds, they can still use the 15% option even if the overseas scheme does not finalise the transfer until after 31 March 2014.

Taxpayers can choose to calculate their tax liability under the 15% rate option or under the existing law.

Under the 15% option, the income must be included in the person's tax return for either of the 2013–14 or 2014–15 income years. The due date for tax will be the due date for payment for the corresponding 2013–14 or 2014–15 income year tax return in which the lump sum is included. Paying the tax on this 15% amount will satisfy their income tax liability for that transfer or withdrawal. Penalties and interest will not apply from the income year in which the income should have been included in their tax return.

Taxpayers who choose to use the 15% option in subsequent income years would need to have their tax return for the 2014–15 income year reassessed in order to apply that concessionary tax rate.

People who have complied with the existing law and paid the associated tax will not be able to reassess their position using the 15% option.

If a person does not want to use the 15% option to get up to date with their tax obligations in relation to their foreign superannuation withdrawal or transfer, they must apply the law as it applied at the time that they made the withdrawal.

For example, a person could choose to apply the available subscribed capital rules (if allowed under the law at the time) if they think that it will result in a lower tax liability than tax under the 15% option – perhaps because all or the majority of the transfer will be a return of capital rather than a dividend. The original due date would still apply if there is a positive amount of income under reassessment. This means that any relevant penalties and use-of-money interest will apply from the income year in which the transfer or withdrawal occurred.

Further information about the process for disclosing past withdrawals will be available on Inland Revenue's website following enactment.

15% option – example 1:

Jenny transferred $150,000 from her foreign superannuation scheme to a New Zealand scheme in February 2004. She did not include this income in her IR3 return for the 2003–04 income year, and did not pay tax on the interest under the FIF rules.

She decides to use the 15% option for her lump-sum transfer. She declares $22,500 (being 15% of $150,000) as income in her IR 3 return for the 2014–15 income year.

Jenny will be liable for any penalties or use-of-money interest in relation to her 2014–15 tax return, not her 2004–05 tax return.

15% option – example 2:

Catherine transferred $150,000 from her foreign superannuation scheme to a New Zealand scheme in February 2004. She did not include this income in her IR3 return for the 2003–04 income year.

She decides to use the law as it applied at the time that she made the withdrawal to calculate the tax on her lump-sum transfer. In her situation, her interest was not an interest in a FIF, and the majority of her $150,000 was a return of capital, and only $2,000 of the amount is income. She has her 2003–04 IR 3 return amended to include the $2,000.

Catherine will be liable for penalties and use-of-money interest from the 2003–2004 income year.

Application of the foreign investment fund (FIF) rules after 1 April 2014

Generally, the bill proposes that the FIF rules will no longer apply to interests in foreign superannuation schemes. However, the FIF rules will continue to apply where an interest in a foreign superannuation scheme was acquired while the person was resident in New Zealand.

Optional "grandparenting" provisions will also apply to certain taxpayers who have previously complied with the FIF rules in relation to a foreign superannuation interest. "Grandparenting" means that the FIF rules will continue to be available after 1 April 2014 if a number of conditions are met.

A taxpayer must have filed an income tax return including FIF income or loss for an interest in a foreign superannuation scheme before 20 May 2013 (the introduction of the Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Bill).

Grandparenting will be available on an interest-by-interest basis. If a taxpayer has interests in more than one foreign superannuation scheme but has only returned FIF income in respect of one of the interests, the taxpayer will only be grandparented in relation to that interest.

To elect to be grandparented in relation to a foreign superannuation interest, a taxpayer must continue to include FIF income or loss for that interest in their income tax return for all income years ending after 1 April 2014. If a taxpayer fails to do so for any income year, they will no longer be grandparented. They will then be required to account for income tax on any lump sums received from the scheme under the proposed new rules.

Once a taxpayer has lost their grandparented status in relation to an interest, they cannot regain it.

Legislation

These proposed changes are included in the Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Bill introduced on 20 May 2013 and will apply from 1 April 2014.