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WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

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WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION I: DEFINITIONS

(1) What is a **foreign superannuation withdrawal**	A **foreign superannuation withdrawal** means a benefit for a person from a foreign superannuation scheme to which **section CF 3** applies. [**s. YA 1** definition as proposed in **cl. 103(11)** of the Superannuation Tax Bill]
(2) What benefit does **section CF 3** apply to?	**Section CF 3** applies to a benefit (a foreign superannuation withdrawal) that: (a) Is not a pension or annuity; and (b) Is derived by a person from a **foreign superannuation scheme**; and (c) Is income if the benefit is in the form of: (i) An amount derived by the person as a member or beneficiary of the scheme; or (ii) An interest of the person in the scheme, withdrawn for reinvestment as an interest of the person in a superannuation scheme in New Zealand; or (iii) An interest of the person in the scheme, outside Australia, withdrawn for reinvestment as an interest of the person in a superannuation scheme in Australia; or (iv) An interest of the person in the scheme (anywhere) withdrawn, <u>other than on the death of the person</u>, for reinvestment as an interest of another person in a superannuation scheme. (Rollover relief for transfers on death) [**s. CF 3(1)** as proposed in **cl. 8** of the Superannuation Tax Bill]
(3) What does **interest in a foreign superannuation scheme** mean?	For the purposes of **s. CF 3**, an interest of a person in a foreign superannuation scheme consists of rights of the person to benefit as a member or beneficiary from distributions by the superannuation scheme. [**s. CF 3(17)** as proposed in cl. 8 of the Superannuation Tax Bill]

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION I: DEFINITIONS (continued)

<table>
<tr><td>(4) What does foreign superannuation scheme mean?</td><td>A foreign superannuation scheme means a superannuation scheme constituted outside New Zealand.

A superannuation scheme:

(a) Means:
(i) A trust or unit trust established by its trust deed mainly for the purposes of providing retirement benefits to beneficiaries who are natural persons or paying benefits to superannuation funds; or
(ii) [Repealed]
(iii) A company that is not a unit trust, is not resident in New Zealand, and is established mainly for the purpose of providing retirement benefits to members or relatives of members who are natural persons; or
(iv) An arrangement constituted under an Act of the Parliament of New Zealand, other than the New Zealand Superannuation and Retirement Income Act 2001, mainly for the purpose of providing retirement benefits to natural persons; or
(v) An arrangement constituted under the legislation of a country, territory, state, or local authority outside New Zealand mainly for the purpose of providing retirement benefits to natural persons; and

(b) For a superannuation scheme that is a trust, means the trustees of the scheme

[s. YA 1 definitions of foreign superannuation scheme and superannuation scheme]</td></tr>
</table>

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION II: TRANSITIONAL RESIDENT'S EXEMPTION

(1) Transitional resident exemption	A foreign superannuation withdrawal derived by a resident is subject to **s. CW 27** if the person is a **transitional resident**. [**s. CF 3(2)(a)** as proposed in **cl. 8** of the Superannuation Tax Bill] 1. Under **s. CW 27**, income derived by a person who is a **transitional resident** is exempt income if the income is a **foreign-sourced amount** that is none of the following: (a) Employment income of a type described in **s. CE 1** in connection with employment or service performed while the person is a transitional resident; or (b) Income from the supply of services. 2. Under **s. HR 8(2)** a person is a **transitional resident** if: (a) They are resident in New Zealand through acquiring a permanent place of abode under s. YD 1(2) or through the 183-day rule in s. YD 1(3); and (b) For a continuous period of at least 10 years immediately before they meet the residence requirements in s. YD 1(2) or YD 1(3), they: (i) Did not meet those requirements; or (ii) Were not resident in New Zealand; and (c) They were not a transitional resident before the non-residence period; and (d) They have not ceased to be a transitional resident after the end of the non-residence period. 3. A **foreign-sourced amount** is income that is not treated as having a source in New Zealand under sections YD 4 and YZ 1. 4. Income described in **s. CE 1** is: salary or wages, an allowance, bonus, extra pay, or gratuity, expenditure on account of an employee, a benefit received under a share purchase agreement, directors' fees, compensation for loss of employment or service, any other benefit in money, and the market value of accommodation or an accommodation allowance. [**s. CW 27, CE 1 & s. YA 1** definition of foreign-sourced amount]
(2) Period of transitional resident exemption	The exemption period in which a foreign superannuation withdrawal may be exempt income of the person under s. CW 27 is the period for which the person is a transitional resident under s. HR 8(2), disregarding any choice under s. HR 8(4). Under **s. HR 8(3)** a natural person is a transitional resident for a period: (a) Beginning from the 1st day of residence under s. HR 8(2)(a) – see above -; and (b) Ending on the day that is the earlier of: (i) The day before the person stops being a New Zealand resident; and (ii) The last day of the 48th month after the month in which they meet the residence requirements of s. YD 1(2) or YD 1(3).

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION III: INITIAL PERIOD OF RESIDENCY EXEMPTION

(1) Initial period of residency exemption	(a) A foreign superannuation withdrawal derived by a resident is subject to **s. CW 28B**, if the person: (i) Is a resident under s. YD 1; and (ii) Acquired the person's interest in the scheme when a non-resident under s. YD 1 or under an applicable double tax agreement; and (iii) Is not a transitional resident; and (iv) Derives the foreign superannuation withdrawal in an exemption period given by s. CF 3(4) – see below -. [**s. CF 3(2)(b)** as proposed in **cl. 8** of the Superannuation Tax Bill] (b) Under **s. CW 28B**, a foreign superannuation withdrawal is exempt income of a person if the person: (i) Is not a transitional resident; and (ii) Meets the requirements of s. CF 3(2)(b) – see above -; and (iii) Derives the foreign superannuation withdrawal in the exemption period given by s. CF 3(4) for the person – see below -. [**s. CW 28B** as proposed in **cl. 18** of the Superannuation Tax Bill]
(2) Eligibility for exemption period	A person has an exemption period under s, CF 3(4) for an interest in a scheme that the person acquires <u>before</u>: (a) The person is a transitional resident under s. HR 8(2), disregarding any choice under s. HR 8(4); or (b) The person is a New Zealand resident who is not a non-resident under a double tax agreement, <u>at a time</u> (the **exemption commencement**) when the person: (i) Is not a transitional resident; and (ii) Has not had an exemption period previously. [**s. CF 3(3)** as proposed in **cl. 8** of the Superannuation Tax Bill] **Note:** <u>The exemption period will not be available for interests that were acquired while the person was resident in New Zealand</u>
(3) Period of initial residency exemption	Under **s. CF 3(4)**, the period of the initial residency exemption is the period from the exemption commencement to the earlier of: (a) The end of the period 48 months beginning after the month of the exemption commencement; or (b) The date on which the person becomes a non-resident again. [**s. CF 3(4)** as proposed in **cl. 8** of the Superannuation Tax Bill]

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION IV: OTHER EXEMPTIONS

(1) Australian superannuation withdrawals not included in income	**Australian superannuation scheme withdrawal exemption** Section CF 3(1) does not include withdrawals from Australian superannuation schemes. It stated on page 6 of the *Commentary* to the Bill that: "Withdrawals from Australian schemes and transfers from Australian schemes to New Zealand schemes, are generally not taxed under the Australia-New Zealand double tax agreement or under the forthcoming trans-Tasman superannuation portability agreement (which will take effect from 1 July 2013). This treatment will continue under the new rules." [**s. CF 3(1)** as proposed in **cl. 8** of the Superannuation Tax Bill]
(2) Transfers between two foreign schemes not included in income	**Exemption (rollover relief) for transfers between two foreign (non-Australian) superannuation schemes** Section CF 3(1) does not include transfers between two foreign superannuation schemes. It stated on page 6 of the *Commentary* to the Bill that: "A transfer between two foreign superannuation schemes typically gives rise to a taxable event under current law, being a disposal of rights in the first scheme and an acquisition of rights in the new scheme. Proposed new section CF 3(1) provides that a transfer from one foreign superannuation scheme to another foreign superannuation scheme will not be taxable. This may occur, for example, when a person disposes of their interest to purchase an annuity with a different provider, or if a person transfers from one foreign scheme to another foreign superannuation scheme in order to obtain better returns. Instead, the person will be taxed on the eventual withdrawal or payment (or transfer to an Australian or New Zealand scheme) based on the length of their New Zealand residence from when they initially acquired the interest (in the first scheme). As transfers from Australian schemes are typically exempt, as noted above, transfers from a foreign scheme to an Australian scheme will be taxable as if the transfer was made to a New Zealand scheme. **Example** Sarah, a New Zealand resident, has an Individual Retirement Account in the United States. She wants to purchase an annuity with a different scheme provider. Under normal circumstances this would be taxable as it is a disposal and reacquisition. However, under the proposed new rules Sarah will get rollover relief so does not need to pay tax on the amount she withdraws to purchase the annuity. Any pension received while resident will be taxable under the current law." [**s. CF 3(1)** as proposed in **cl. 8** of the Superannuation Tax Bill]

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION IV: OTHER EXEMPTIONS (continued)

(3) Transfers upon death not included in income	**Exemption (rollover relief) for transfers upon death** Section CF 3(1) does not include an interest withdrawn on the death of a person, for reinvestment as an interest of another person in a superannuation scheme. It stated on page 6 of the *Commentary* to the Bill that: Rollover relief will also be provided when a deceased person's interest in a foreign superannuation scheme is transferred directly to a New Zealand resident. The transfer will not be taxed. Instead, the recipient will be taxed on the eventual withdrawal or transfer (subject to the rollover relief discussed above), based on the duration of New Zealand residence of both the recipient and the deceased. **Example** Matthew moved to New Zealand in 2016 to be closer to his New Zealand-based daughter Jenny. Matthew died in 2023, seven years after migration. Matthew had an interest in a foreign superannuation fund which was acquired while non-resident. His foreign superannuation was transferred to Jenny under his will, and was not taxed at that time. Jenny withdraws the foreign superannuation in 2026, after her father's death. She is treated as having acquired the foreign superannuation interest in 2016, which is when Matthew first became resident after acquiring the interest." [**s. CF 3(1)** as proposed in **cl. 8** of the Superannuation Tax Bill]
(4) Exemption for an amount exceeding the assessable withdrawal amount	**Exemption for amounts in excess of the assessable withdrawal amount** A foreign superannuation withdrawal derived by a resident is exempt income of the person under **s. CW 28C**, if the foreign superannuation withdrawal is derived in the person's **assessable period** given by **s. CF 3(5)**, to the extent to which the foreign superannuation withdrawal exceeds: (a) The amount given by **s. CF 3(7)** as the assessable withdrawal amount, if the person uses the <u>schedule method</u>; or (b) The amount given by **s. CF 3(13)** as the assessable withdrawal amount, if the person uses the <u>formula method</u>. [**s. CF 3(2)(c)** as proposed in **cl. 8** and **s. CW 28C** as proposed in **cl. 18** of the Superannuation Tax Bill] **Note:** 1. What is meant by the assessable period is covered in pages 10 - 11 below. 2. What is meant by the formula method is covered in pages 12 - 16 below. 3. What is meant by the schedule method is covered in pages 17 - 20 below.

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION V: ASSESSABLE PERIOD

(1) Defining the assessable period	The period (the **assessable period**) in which a person's foreign superannuation withdrawal for an interest in a scheme is not subject to sections CW 27 or CW 28B is the period: (a) Beginning from the last of: (i) When the person is treated under s. CF 3(18) as acquiring the interest in the scheme; or (ii) When the person becomes a New Zealand resident; or (iii) When the person's exemption period under s. CF 3(4) ends; and (b) Ending when the person becomes a non-resident.
(2) Calculating the assessable period when an interest in a foreign superannuation scheme is acquired	**Calculating the assessable period when an interest in a foreign superannuation scheme is acquired** In calculating under **s. CF 3(5)** the assessable period for a person who acquires an interest in a foreign superannuation scheme, the person is treated as acquiring the interest: (a) If none of **paragraphs (b) to (d)** apply, when the first contribution is made to the superannuation scheme, in relation to the rights, by or for the person; or (b) If the person is converting existing rights in another superannuation scheme (the **former scheme**) to corresponding rights of the person in the superannuation scheme, when the person acquired the rights in the former scheme; or (c) If the person is acquiring rights in the superannuation scheme from another person, other than by a transaction to which **paragraph (d)** applies, when the person acquires the rights; or (d) If the person is acquiring existing rights in the superannuation scheme by a transfer from the estate of a deceased New Zealand resident after the beginning of the assessable period for the rights for the deceased person, the beginning of that assessable period. [**s. CF 3(18)** as proposed in **cl. 8** of the Superannuation Tax Bill]

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION V: ASSESSABLE PERIOD (continued)

<table>
<tr>
<td>(3) Explanation in the Commentary to the Bill</td>
<td>Explanation in the Commentary to the Bill

It is stated on page 9 of the Commentary that:

“If the person acquired the interest while they were non-resident, the assessable period will start when their exemption period ends.

If the person acquired the interest while they were resident, they are not eligible for an exemption period. Their assessable period will start when they acquire the interest.

The assessable period ends when a person becomes non-resident. …

As noted above, section CF 3(1) provides that transfers between two foreign schemes will generally not be taxed. Instead, the amount will be taxed under the schedule or formula method either when it is finally withdrawn or when it is transferred to a New Zealand or Australian superannuation scheme. The schedule and formula methods are based on the duration of residence since the interest in the first scheme was acquired, so the assessable period will begin on the date the interest in the first scheme was acquired.

When an interest in a foreign superannuation scheme is transferred to another person, the transfer will be taxable to the transferor based on their years of residence, if the transferor is a New Zealand resident. The recipient’s assessable period will begin when they first acquire the interest from the transferor, if they are a New Zealand resident. This will apply in situations such as a relationship split, where a relationship property agreement may transfer all or part of an interest in a foreign superannuation scheme from one party to the other.

For someone who loses residency and then becomes resident again, it is possible to have more than one assessable period. In this situation, the applicable assessable periods will be aggregated.

The assessable period will be determined for each specific foreign superannuation interest, based on the number of years of residence since the interest in that particular interest was acquired.

It is possible that a person might have different assessable periods for different interests. For example, a person migrates to New Zealand with an interest in a foreign superannuation scheme and they acquire an interest in another scheme while they are New Zealand-resident. The assessable period for the first interest will begin when their four-year exemption period ends and for the second interest it will begin when the second interest is acquired.

This will ensure that the new rules will still work as intended if an individual has interests in multiple schemes and transfers amounts at different points in time.

[s. CF 3(5) as proposed in cl. 8 of the Superannuation Tax Bill]</td>
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</table>

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VI: FORMULA METHOD

<table>
<tr>
<td>(1) Requirements to use the formula method</td>
<td>
The part (the assessable withdrawal amount) of a foreign superannuation withdrawal, derived in the assessable period, that is treated as not being exempt income is given by the formula method under s. CF 3(13) if:
(i) The scheme is a foreign defined contribution scheme; and
(ii) The person has the information required for the application of the formula method; and
(iii) The person derives no withdrawal, other than a pension or annuity, from the scheme before 1 April 2014; and
(iv) The person has not used the schedule method for the interest in the scheme; and
(v) For a person who acquires the interest in the scheme as a bequest from a deceased New Zealand resident, the deceased person did not use the schedule method for the interest in the scheme; and
(vi) The person chooses to use the formula method for the interest in the scheme.
[s. CF 3(6)(b) as proposed in cl. 8 of the Superannuation Tax Bill]
Foreign defined contribution scheme means a foreign superannuation scheme that operates on the principle of allocating contributions to the scheme on a defined basis to individual members.
[s. YA 1 definition proposed in cl. 103(10) of the Superannuation Tax Bill]
It is stated on page 13 of the Commentary that:
“The formula method is an alternative to the schedule method for people with a foreign defined contribution scheme if they have sufficient information. This method will tax actual investment gains derived while a person is a New Zealand resident (after the end of their exemption period). It was introduced following submissions on the issues paper.
Proposed new sections CF 3(6)(b), CF 3(9), (10), (11), (12), (13), (14), (15) and (16), and section YA 1 “foreign defined contribution scheme” provide for the formula method.
To use this approach, a person is required to obtain the market value of the foreign superannuation interest at the time the exemption period ends, as well as information about contributions made and other necessary information. Requirements relating to the quality of information will apply.
</td>
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WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VI: FORMULA METHOD (continued)

(2) The formula method calculation	For the foreign superannuation withdrawal, the amount (the **assessable withdrawal amount**) not exempt under **s. CW 28C** is the amount calculated using the formula: $$\textbf{gain out} \times (\textbf{grow rate} - 1) \times \textbf{tax rate} \times (\textbf{assessable years} - 1) + \textbf{gain out}$$ [**s. CF 3(13)** as proposed in **cl. 8** of the Superannuation Tax Bill]
(3) Formula items: Gain Out	Gain out: Is the amount of the **distributed gain** given by s. CF 3(9) for the foreign superannuation withdrawal. Under s. CF 3(9), the **distributed gain** is the part of a foreign superannuation withdrawal that is treated as consisting of gains made by the scheme during the assessable period, and is calculated as: $$(\textbf{super withdrawal} \times \textbf{calculated gains fraction}) - \textbf{gains out}$$ Super withdrawal: Is the amount of the foreign superannuation withdrawal Gains out: Is the total amount of distributed gains given by s. CF 3(9) for foreign superannuation withdrawals in an assessable period before the distribution time. Calculated gains fraction: Is the greater of zero and the amount calculated as: $$\frac{\textbf{predistribution} + \textbf{withdrawals} - \textbf{transit} - \textbf{contributions}}{\textbf{predistribution}}$$ Predistribution: Is the value of the interest in the scheme immediately before the distribution time. Withdrawals: Is the total amount of withdrawals from the interest in the scheme before the distribution time. Transit: Is the value of the interest in the scheme at the beginning of the assessable period. Contributions: Is the amount of contributions to the interest in the scheme made before the distribution time. [**s. CF 3(9), (10), (11) & (12)** as proposed in **cl. 8** of the Superannuation Tax Bill]

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VI: FORMULA METHOD (continued)

(4) Formula items: Tax Rate	Tax rate: Is the tax rate given by Schedule 1, Part A, Table 1, Row 4. This is currently the top marginal rate of 33%. [**s. CF 3(15(b)** as proposed in **cl. 8** of the Superannuation Tax Bill]
(5) Formula items: Assessable Years	Assessable years: Is the greater of: (a) 1; and (b) The number of tax years beginning in an assessable period and before the distribution time. [**s. CF 3(15)(c)** as proposed in **cl. 8** of the Superannuation Tax Bill]
(6) Formula items: Grow Rate	Grow rate is: $\left(\frac{\textbf{accrued total}}{\textbf{transit}}\right)^{\frac{\textbf{1}}{\textbf{assessable years}}}$ Transit: Is the value of the interest in the scheme at the beginning of the assessable period. Accrued total: Is the value of the interest in the scheme immediately before the distribution time, increased by the value of distributions from the interest in the scheme before the distribution time, and reduced by the value of recognised contributions under s. CF 3(16) made to the scheme in an assessable period before the distribution time. [**s. CF 3(14) & (15)** as proposed in **cl. 8** of the Superannuation Tax Bill]
(7) Formula items: Contributions	The value of a payment to the scheme is taken into account in the formulas in **s. CF 3(7), (11), and (14)** as a contribution (a **recognised contribution**) if the payment: (a) Is made when the person is a New Zealand resident and is a non-resident under no double tax agreement; and (b) Is made by the person, by the person's employer, or for the benefit of the person; and (c) Is required by the rules of the scheme; and (d) Is subject to employer superannuation contribution tax or fringe benefit tax if made by the person's employer. [**s. CF 3(16)** as proposed in **cl. 8** of the Superannuation Tax Bill]

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VI: FORMULA METHOD (continued)

(8) *Commentary* on the Bill	It is stated on pages 13 to 14 of the Commentary that: "The formula in section CF 3(9) is: *Distributed gain = (super withdrawal x calculated gains fraction) – gains out* "Super withdrawal" is the amount of the foreign superannuation withdrawal and "gains out" is the total amount of distributed gains previously calculated under this formula for previous withdrawals in the assessable period. The "calculated gains fraction" is given by the formula in section CF 3(11): $\dfrac{\textit{Predistribution + withdrawals - transit - contributions}}{\textit{predistribution}}$ "Predistribution" is the value of the person's interest in the scheme immediately before they made their foreign superannuation withdrawal. "Withdrawals" is the total amount of previous foreign superannuation withdrawals made in the assessable period. "Transit" is the opening value of the person's interest in the scheme at the beginning of their assessable period. "Contributions" is the total amount of recognised contributions under section CF 3(16), as described above. Interest will be charged on the amount of taxable New Zealand gains to account for the deferral benefit that the person obtains by not paying tax on accrual (similar to the use-of-money interest rules). The interest will be payable at the same rate as the average growth of the person's superannuation interest over the number of years of residence. The interest component is contained in section CF 3(13) to (15). Taxpayers will not be able to switch from the schedule method to the formula method.

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VI: FORMULA METHOD (continued)

(9) ***Commentary*** **on the Bill: Example on page 15**	**Example on page 15 of the** ***Commentary*** Thomas migrates to New Zealand with a foreign superannuation scheme worth NZ$100,000. Ten years after Thomas' assessable period begins, his scheme is worth $180,000 and he withdraws a lump-sum amount of $60,000. Five years after this, his scheme is worth $150,000 and he withdraws the full amount. Thomas has made no contributions to the scheme while he has been New Zealand-resident.

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VI: FORMULA METHOD (continued)

(9) ***Commentary*** **on the Bill: Example on page 15 (continued)**	*Gain out* is the *distributed gain*, which under s. CF 3(9) is the part of a foreign superannuation withdrawal that is treated as consisting of gains made by the scheme during the assessable period, and is calculated as: $$(\textbf{super withdrawal x calculated gains fraction}) - \textbf{gains out}$$ *Super withdrawal* is the foreign superannuation withdrawal: Thomas' first withdrawal 10 years after his assessable period begins is \$60,000; Thomas' second withdrawal 15 years after his assessable period begins is \$150,000; *Calculated gains fraction* is the greater of zero and the amount calculated as: $$\frac{\textbf{predistribution + withdrawals - transit - contributions}}{\textbf{predistribution}}$$ (a) *Predistribution* is the value of Thomas' interest in the scheme immediately before each withdrawal: for Thomas' first withdrawal, the predistribution is \$180,000; for Thomas' second withdrawal, the predistribution is \$150,000. (b) *Withdrawals* is the total previous withdrawals made in the assessable period: for Thomas' first withdrawal, "withdrawals" is zero; for Thomas' second withdrawal, "withdrawals" is \$60,000. (c) *Transit* is the opening value of the person's interest in the scheme at the beginning of the assessable period: for Thomas, this is \$100,000, being the value of his interest when he migrated to New Zealand. (d) *Contributions* for Thomas, this is zero. <u>For Thomas' first withdrawal, his "calculated gains fraction" is</u>: $$\frac{\$180,000 + \$0 - \$100,000 - \$0}{\$180,000} = \frac{4}{9}$$ <u>For Thomas' second withdrawal, his "calculated gains fraction" is</u>: $$\frac{\$150,000 + \$60,000 - \$100,000 - \$0}{\$150,000} = \frac{11}{15}$$ *Gains out* is distributed gains previously calculated under this formula for previous withdrawals in the assessable period: For Thomas' first withdrawal, previously calculated "gains out" is zero. For Thomas' second withdrawal, gains out are \$26,667, calculated as below. (a) For Thomas' first withdrawal, his "distributed gain" or *gain out* is: $$\left(\$60,000 \text{ x } \frac{4}{9}\right) - \$0 = \$26,667$$ (b) For Thomas' second withdrawal, his "distributed gain" or *gain out* is: $$\left(\$150,000 \text{ x } \frac{11}{15}\right) - \$26,667 = \$83,333$$

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VI: FORMULA METHOD (continued)

<table>
<tr>
<td>(9) Commentary on the Bill: Example on page 15(continued)</td>
<td>
Interest will be charged, at the same rate as the average growth of the person's superannuation interest over the number of years of residence, on the amount of taxable New Zealand gains to account for the deferral benefit that the person obtains by not paying tax on accrual. The interest component is given by:

$$\textbf{gain out x (grow rate - 1) x tax rate x (assessable years - 1)}$$

(a) Grow rate is:

$$\left(\frac{\textbf{accrued total}}{\textbf{transit}}\right)^{\frac{1}{\textbf{assessable years}}}$$

(b) Accrued total is the value of the interest in the scheme immediately before the distribution time, increased by the value of distributions from the interest in the scheme before the distribution time, and reduced by the value of recognised contributions made to the scheme in an assessable period before the distribution time.

(c) Assessable years is the greater of 1 and the number of tax years beginning in an assessable period and before the distribution time.

(d) Tax rate is the tax rate given by Schedule 1, Part A, Table 1, Row 4. This is currently the top marginal rate of 33%.

Thomas' grow rates for the first and second withdrawals are calculated as follows:

(a) For Thomas' first withdrawal, the accrued total is:

$$\textbf{Predistribution value + earlier distributions - contributions = \$180,000 + 0 - 0 = \$180,000}$$

(b) For Thomas' second withdrawal, the accrued total is:

$$\textbf{\$150,000 + \$60,000 - 0 = \$210,000}$$

(c) Transit is $100,000 for both the first and the second withdrawal.

(d) The assessable period is 10 for the first withdrawal and 15 for the second withdrawal.

(e) For the first withdrawal:

$$\textbf{grow rate} = \left(\frac{180{,}000}{100{,}000}\right)^{\frac{1}{10}} = 1.0605$$

(f) For the second withdrawal:

$$\textbf{grow rate} = \left(\frac{210{,}000}{100{,}000}\right)^{\frac{1}{15}} = 1.0507$$
</td>
</tr>
</table>

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VI: FORMULA METHOD (continued)

(9) ***Commentary*** **on the Bill: Example on page 15 continued)**	Thomas' assessable withdrawal amount for each of the first and second withdrawals is calculated as follows: (a) For Thomas' first withdrawal, the assessable withdrawal amount under the formula method is: $\textbf{gain out x (grow rate - 1) x tax rate x (assessable years - 1) + gain out}$ **= $26,667 x (1.0605 -1) x 0.33 x (10 - 1) + $26,667 = $31,458.66** (b) For Thomas' second withdrawal, the assessable withdrawal amount under the formula method is: **= $83,333 x (1.0507 -1) x 0.33 x (15 - 1) + $83,333 = $102,852.42** Taxpayers will not be able to switch from the schedule method to the formula method.

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VII: SCHEDULE METHOD

(1) Default method	The schedule method must be used to calculate a person's assessable withdrawal amount if: (a) The person cannot use the formula method; or (b) The person chooses not to use the formula method. [**s. CF 3(6)(a)** as proposed in **cl. 8** of the Superannuation Tax Bill]
(2) The schedule method calculation	The assessable withdrawal amount under the schedule method is calculated using the formula: $$(\textbf{super withdrawal - contributions left}) \textbf{ x schedule year fraction}$$ <u>Super withdrawal:</u> Is the amount of the foreign superannuation withdrawal: <u>Contributions left:</u> Is the lesser of: (a) The amount of the item super withdrawal; and (b) The total amount of **recognised contributions** under s. CF 3(16) – see page 14 above - made in the assessable period before the distribution time, reduced, for each foreign superannuation withdrawal (the **earlier withdrawal**) made in the assessable period before the distribution time, by an amount equal to the lesser of: (i) The amount of the earlier withdrawal; and (ii) The value of the item contributions left, immediately before the time of the earlier withdrawal. <u>Schedule year fraction:</u> Is the fraction given in **schedule 33**, column 2 of the row for which the entry in column 1 corresponds to the greater of 1 and the number of income years beginning: (a) In an assessable period for the person under **s. CF 3(5)**; and (b) After the time when the person acquires the interest; and (c) Before the time (the **distribution time**) when the person derives the foreign superannuation withdrawal. [**s. CF 3(7) & (8)** proposed in cl. 8 of the Superannuation Tax Bill]

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VII: SCHEDULE METHOD

(3) Following the example on page 15 of the *Commentary*	**Let's follow the Example on page 15 of the Commentary as we did on pages 16 to 19 for the formula method:** Thomas migrates to New Zealand with a foreign superannuation scheme worth NZ$100,000. Ten years after Thomas' assessable period begins, his scheme is worth $180,000 and he withdraws a lump-sum amount of $60,000. Five years after this, his scheme is worth $150,000 and he withdraws the full amount. Thomas has made no contributions to the scheme while he has been New Zealand-resident. For Thomas' first withdrawal, the schedule year fraction for year 10 is 44.39%. Therefore, Thomas' assessable withdrawal amount under the schedule method will be $26,634. This compares with $31,458.66 under the formula method, as calculated in paragraph 16 of last week's *Weekly Comment*. For Thomas' second withdrawal, the schedule year fraction for year 15 is 64.08%. Therefore, Thomas' assessable withdrawal amount under the schedule method will be $96,120. This compares with $102,852.42 under the formula method, as calculated in paragraph 16 of last week's *Weekly Comment*. In this case, the schedule method provides better answers for both withdrawals. A comparison between methods will need to be made for the first withdrawal. Remember that taxpayers will not be able to switch from the schedule method to the formula method.

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VII: SCHEDULE METHOD (continued)

(4) Explanation of the Schedule Method in the Commentary	The Proposed new sections CF 3(6)(a), CF 3(7), (8) and (16) provide for the schedule method. The schedule method is the default method for taxing foreign superannuation withdrawals. The schedule method deems a certain amount of the lump-sum receipt to be investment gains, based on the person's years of residence. The approach uses fractions that represent the proportion of the lump-sum receipt to be included in assessable income. The schedule year fractions increase with years of residence. The remainder of the lump-sum receipt is not assessable. The fractions in proposed schedule 33 are set at the rate necessary to put a person who leaves their foreign superannuation overseas in the same position as if they had instead transferred their superannuation to New Zealand and paid tax on investment gains as they accrued. Given the assumptions (including a 5% post-tax interest rate in the foreign scheme), a person should conceptually be indifferent between keeping their superannuation overseas and transferring it to New Zealand. Further discussion of the policy rationale behind the schedule method can be found in the annex to the issues paper. [1] A person's assessable income will be calculated as follows: *Assessable income = (super withdrawal – contributions left) x schedule year fraction* The term "super withdrawal" is the amount of the transfer or withdrawal made by the person. The appropriate "schedule year fraction" to use is identified by calculating the number of income years beginning in the assessable period, before the person receives the lump sum. In short, this is the number of income years which begin after the person is a New Zealand resident and after their four-year "exemption period" ends. The effect of counting a person's years of residence from the end of the exemption period is to treat them as being non-resident during the exemption period. Gains which accrue during those four years will not be clawed back and taxed on receipt. **Example** Lucy's assessable period begins on 1 August 2020. She withdraws a lump sum of \$50,000 on 27 January 2024. There are three income years beginning in Lucy's assessable period, so Lucy is required to use the schedule year fraction for year three. The corresponding schedule fraction is 14.06%, so her assessable income will be \$7,030 (being \$50,000 x 14.06%). Assuming Lucy's tax rate is 33%, she will be liable to pay \$2,319.90 of tax on her \$50,000 lump-sum withdrawal

[1] *Taxation of foreign superannuation*, released on 24 July 2012.

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VII: SCHEDULE METHOD (continued)

(4) Explanation of the Schedule Method in the Commentary (continued)

If the number of income years beginning in their assessable period is zero (that is, in the part-year in which their exemption period ended but before the start of the next income year), the person should use the schedule year fraction associated with year one.

Example

Karen's assessable period begins on 1 October 2020. She withdraws a lump sum of $50,000 on 5 February 2021, which means that an income year has not yet started during her assessable period. Karen is required to use the schedule year fraction for year one because the withdrawal was made between 1 October 2020 and 31 March 2022. The corresponding schedule fraction is 4.76%, so her assessable income will be $2,380 (being $50,000 x 4.76%). Assuming Karen's tax rate is 33%, she will be liable to pay $785.40 of tax on her $50,000 lump-sum withdrawal.

Proposed new schedule 33 provides the full schedule of rates per year of residence:

Schedule year	Schedule year fraction
1	4.76%
2	9.45%
3	14.06%
4	18.60%
5	23.07%
6	27.47%
7	31.80%
8	36.06%
9	40.26%
10	44.39%
11	48.45%
12	52.45%
13	56.39%
14	60.27%
15	64.08%
16	67.84%
17	71.53%
18	75.17%
19	78.75%
20	82.28%
21	85.74%
22	89.16%
23	92.58%
24	95.83%
25	99.08%
26+	100%

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VII: SCHEDULE METHOD (continued)

(4) Explanation of the Schedule Method in the Commentary (continued)	The "contributions left" item in the formula is effectively a deduction for contributions made for or on behalf of a person while the person is a New Zealand resident, if the contributions satisfy certain conditions. The schedule method may otherwise treat some of the New Zealand contributions as gains and would result in over-taxation. Proposed new section CF 3(16) sets out these conditions: • At the time the contribution is made, the person must be a New Zealand resident under section YD 1 and not non-resident under a double tax agreement; • The contribution must be required under the rules of the foreign superannuation scheme (that is, voluntary contributions will not be eligible); • The contribution has been subject to New Zealand tax, such as being paid out of after-tax income or subject to employer superannuation contribution tax or fringe benefit tax (for an employer contribution); and • The contribution must not have previously been deducted under the schedule method. The contributions that are able to be deducted are restricted in this manner because the schedule rates already include an implicit allowance for contributions. For example, for the year one schedule rate, 4.76% of the withdrawal is treated as taxable New Zealand-sourced gains and the remainder is treated as non-taxable amounts (that is, contributions as well as gains derived while non-resident). A number of submitters on the issues paper argued that there should be no restrictions on the types of contributions that are deductible. This would not be appropriate, as it could lead to contributions being effectively deducted more than once – first, by being deducted as "contributions left" in the formula and, secondly, by then being allocated out using the schedule rates.

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VIII: KIWISAVER WITHDRAWAL TO MEET TAX LIABILITY

<table>
<tr>
<td>(1) KiwiSaver scheme withdrawal to meet superannuation tax liability</td>
<td>New Schedule 1, cl.14A of the KiwiSaver Act 2006 provides for a withdrawal to meet the tax liability on a foreign superannuation withdrawal:

1. A member may, on application to the trustees (in the case of a restricted KiwiSaver scheme) or the manager (in the case of any other KiwiSaver scheme), withdraw an amount for the payment of the member's liability for tax, other than interest or penalties, arising under the Income Tax Act 2007 from the member's withdrawal of an interest in a foreign superannuation scheme and conversion of the interest into an interest in a KiwiSaver scheme.

2. The amount withdrawn may not exceed the lesser of:

(a) The member's liability for tax; and

(b) The value of the member's accumulation less the amount of the Crown contribution.

3. An application under cl. 14A(1) must:

(a) Be made by the member:

(i) Before 1 April 2016, if the member's foreign superannuation withdrawal is derived before 1 April 2014; or

(ii) Within 24 months of the member's foreign superannuation withdrawal, if the withdrawal is derived on or after 1 April 2014; and

(b) Be in the form required by the trustees or manager (as the case may be); and

(c) Must include a completed statutory declaration giving the relevant details of the foreign superannuation withdrawal, the reinvestment, and the resulting liability of the member for tax under the Income Tax Act 2007; and

(d) Must include any documents and other information that may be required by the trustees or manager (as the case may be) in support of the statutory declaration.

[Cl. 14A proposed to be inserted into Schedule 1 of the KiwiSaver Act 2006 by cl. 115 of the Superannuation Tax Bill]</td>
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</table>

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION VIII: KIWISAVER WITHDRAWAL TO MEET TAX LIABILITY (continued)

(2) Explanation of the KiwiSaver withdrawal in the Commentary	In some cases, foreign superannuation may be transferred into a locked-in superannuation scheme, such as KiwiSaver. This may lead to cashflow difficulties for the person as they cannot access any of the transferred amount to pay the resulting tax liability. To address this, new clause 14A will be inserted into schedule 1 of the KiwiSaver Act 2006. This will allow a person to withdraw an amount up to the value of the tax due from their KiwiSaver scheme. If a taxpayer wishes to use this facility, they will be required to provide a statutory declaration to their KiwiSaver provider. The manager of the KiwiSaver scheme must be sufficiently satisfied that the requested amount does not exceed what a hypothetical tax liability could be for that person in relation to that interest. The money will be paid to the individual rather than directly to Inland Revenue, so the individual will be responsible for ensuring that their tax liability is paid. **Example** Hannah transfers her interest worth $100,000 in a UK scheme into a KiwiSaver scheme on 1 July 2014. She makes an application to the manager of her KiwiSaver scheme on 6 October 2015 to withdraw the amount of her tax liability arising from the transfer. She provides a signed statutory declaration and the documents required by the manager. The KiwiSaver manager approves the withdrawal and Hannah uses the funds to pay her tax liability.

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION IX: FOREIGN INVESTMENT FUND (FIF) RULES CHANGES

<table>
<tr><td>(1) Changed 2nd category of attributing FIF interests</td><td>Section EX 29(3) is being replaced as follows:

CATEGORY 2: FIF SUPERANNUATION INTEREST The second category is a FIF superannuation interest, held as a beneficiary or a member.

[Replacement s. EX 29(3) proposed in cl. 40 of the Superannuation Tax Bill]

FIF superannuation interest means, for a person and an income year (the current year), an interest held by the person, in a foreign superannuation scheme as a beneficiary or member:

(a) That is an attributing interest for an income year (the qualifying year) ending before 1 April 2014; and

(b) Producing, for the qualifying year, FIF income or loss <u>included by the person in a return of income filed before 20 May 2013</u>, the day on which the Taxation (Annual Rates, Foreign Superannuation, and Remedial Matters) Bill was introduced; and

(c) Held by the person for the period (the qualifying period) from the end of the qualifying year to the beginning of the current year; and

(d) For which the person includes all FIF income or loss under the FIF rules in returns of income for the qualifying year and income years after the qualifying period.

[s. YA 1 definition proposed in cl. 103(9) of the Superannuation Tax Bill]</td></tr>
<tr><td>(2) Repeal of existing exemptions for Australian superannuation and new resident's accrued superannuation</td><td>The following existing exemptions are to be repealed:

(a) The exemption for Australian regulated superannuation savings in s. EX 33; and

(b) The exemption for new resident's accrued superannuation entitlement in s. EX 42.

Sections CQ 5 and DN 6 are to be correspondingly amended.

[Amendment of s. CQ 5 proposed in cl. 9, amendment of s. DN 6 proposed in cl. 30, and repeal of s. EX 33 & s. EX 42 proposed in cl. 41 and 42, respectively, of the Superannuation Tax Bill]</td></tr>
<tr><td>(3) New exemption for superannuation interest that is not a FIF superannuation interest</td><td>Under new s. EX 42B, a person's right to benefit from a foreign superannuation scheme as a beneficiary or member will not be an attributing interest in the foreign superannuation scheme if the right is not a FIF superannuation interest for the person.

[s. EX 42B proposed in cl. 43 of the Superannuation Tax Bill]</td></tr>
</table>

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION IX: FOREIGN INVESTMENT FUND (FIF) RULES CHANGES (continued)

<table>
<tr>
<td>(4) Explanation in the Commentary</td>
<td>
Transitional measures: FIF rules can continue to apply for certain interests (grandparenting)
A new definition of a “FIF superannuation scheme” has been inserted in section YA 1 to enable the FIF rules to continue to apply to interests when the person has complied with the FIF rules by the introduction date of the new legislation. These people will have the option to either continue to return income under the FIF rules (that is, they will be grandparented), or to apply the new rules instead.

If a person continues to apply the FIF rules, any withdrawals or transfers in relation to that foreign superannuation interest will not be taxed under the proposed new rules.

There are certain requirements that must be satisfied in order for a person to use the FIF rules in relation to a particular foreign superannuation interest. Some will be determined based on past behaviour. These criteria must be met each time a person seeks to apply the FIF rules (that is every income year from 1 April 2014):
• The person must have had an attributing interest in a FIF under section EX 29 for an income year up to and including the 2014 income year (the qualifying year);
• For the relevant income year, the FIF must have been a foreign superannuation scheme;
• The person must have calculated their FIF income or loss resulting from that attributing interest under one of the methods specified in section EX 44; and
• The FIF income or loss must have been included in a tax return filed with Inland Revenue by the date of introduction of this bill.

A person who does not meet these criteria by 1 April 2014 may not continue to use the FIF rules for the 2015 income year (commencing 1 April 2014) or subsequent years.

The effect of these criteria is straightforward. A person who complied with the FIF rules for a prior year, and filed that return before the introduction of this bill, may be grandparented under the FIF rules. If a person has two or more interests in foreign superannuation schemes, the criteria are assessed per interest (not just once for that person).

That person must then continue to return FIF income or losses in relation to that grandparented interest for all income years after 1 April 2014. If FIF income or loss is not returned in a year (in which the person still holds the interest), the interest will cease to be grandparented. The person must pay tax under either the schedule method or the formula method on any subsequent withdrawal.

A person whose foreign superannuation assets are valued at less than the $50,000 minimum threshold in section CQ 5(1)(d) may choose to apply the FIF rules in this manner, as long as the above criteria are satisfied.

Example

Aaron is a migrant to New Zealand and acquired a permanent place of abode in May 2006. He was a transitional resident until the end of May 2010. For the 2011 income year, Aaron complied with the FIF rules in relation to his foreign superannuation interest, and included the FIF income in his tax return before the filing date. He does not return FIF income in relation to this interest in the 2012 to 2014 income years because the interest qualified for a FIF exemption following a change in the foreign superannuation scheme’s rules which made it locked-in. As at 1 April 2014, the criteria are still satisfied as Aaron correctly returned FIF income in the 2011 income year. Despite the exemption, Aaron will have to return FIF income in relation to his interest for the 2015 income year in order for it to remain grandparented.]
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WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION X: CONSEQUENT CHANGES TO THE DIVIDEND AND TRUST TAX RULES

(1) Foreign superannuation withdrawal is not a dividend	New s. CD 36B will provide that: A foreign superannuation withdrawal derived by a person from a company is not a dividend. [**s. CD 36B** as proposed in **cl. 6** of the Superannuation Tax Bill]
(2) Foreign superannuation withdrawal is not a taxable distribution from a foreign trust	New s. HC 15(4)(cb) will provide that a foreign superannuation withdrawal will not be a taxable distribution from a foreign trust. [**s. HC 15(4)(cb)** as proposed in **cl. 66** of the Superannuation Tax Bill]
(3) A contributor to a foreign superannuation scheme is not a settlor	New s. HC 27(3B) will provide that: A person who makes a contribution to a trust that is a foreign superannuation scheme is not a settlor of the trust. [**s. HC27(3B)** proposed by **cl. 67** of the Superannuation Tax Bill]

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION XI: TEMPORARY AMNESTY FOR PRE-1 APRIL 2014 WITHDRAWALS

(1) Optional treatment of withdrawals from foreign superannuation schemes	1. An optional treatment of withdrawals from foreign superannuation schemes applies when a person: (a) Derives an amount from a foreign superannuation scheme as a withdrawal other than a pension or annuity in the period beginning on 1 January 2000 and ending with 31 March 2014; and (b) Does not include the withdrawal (the **omitted withdrawal**) in a return of income for the income year in which the amount was derived; and (c) Is not assessed before 1 April 2014 for income included in the omitted withdrawal; and (d) Chooses to include in a return of income for an income year (the **return year**) ending on or after 31 March 2014 an amount of assessable income as relating to the omitted withdrawal. 2. The person is treated as deriving from the omitted withdrawal an amount of assessable income (the **withdrawal income**) equal to 15% of the amount of the omitted withdrawal. 3. The amount of the liability of the person for income tax (the **withdrawal tax liability**) arising from the omitted withdrawal is the difference between the person's income tax liability for the return year, with the withdrawal income included in the person's assessable income for that year, and the income tax liability that the person would have for the return year if the withdrawal income were not included in the person's assessable income for that year. 4. The amount of the withdrawal tax liability arising from the person's return of income for the return year has a due date for payment corresponding to the due date for payment of the person's terminal tax for the earlier of the return year and the person's 2014–15 income year. 5. This section overrides the law applying to the taxation of the omitted withdrawal when the person derived the omitted withdrawal. [**s. CZ 21B** proposed in **cl. 25** of the Superannuation Tax Bill]

WITHDRAWALS FROM FOREIGN SUPERANNUATION SCHEMES

SECTION XI: TEMPORARY AMNESTY FOR PRE-1 APRIL 2014 WITHDRAWALS (continued)

<table>
<tr>
<td>(2) Explanation in the Commentary</td>
<td>
Transition – low cost option for withdrawals from 1 January 2000 to 31 March 2014
Proposed new sections CZ 21B of the Income Tax Act 2007, CF 3 of the Income Tax Act 2004, and CC 4 of the Income Tax Act 1994 allow an optional method in addition to the current provisions for lump-sum transfers and withdrawals up to 31 March 2014, including past transfers that have not complied with the current law.
The alternative to using the current provisions is the option to pay tax on only 15 percent of the lump-sum amount. The remainder of the lump sum will not be assessable. This is a simple option which is intended to encourage compliance before the introduction of the new rules.
People who have complied with the existing law and paid the associated tax will not be able to reassess their position using the 15 percent option.
To use the option, a person will need to return 15 percent of the lump-sum amount in their 2013–14 or 2014–15 tax returns. Penalties and interest will not apply from the tax year in which the withdrawal or transfer was made. The 15 percent option will continue to be available in later years, but the legislation proposes that penalties and use-of-money interest will be calculated from the 2014–15 tax year. The proposed legislation will be changed to clarify that this will be done by amending the person's 2014–15 income tax return.
As with other forms of income, it should be noted that the portion of the lump sum that is assessable income may impact a person's entitlements and obligations for that tax year, such as child support, Working for Families, and student loans.
If the person does not use the option to pay tax on 15 percent of the amount, then they must apply the law as it was at the time that they made the withdrawal. The original due date for payment of tax 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.
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