i-Select

SUPER SCHEME TAX - November 2020

iSelect
SUPERANNUATION

Tax within the i-Select Superannuation Scheme

Introduction

The purpose of this brief article is to explain how taxation works within the i-Select Superannuation Scheme (Scheme).

Trust tax

The Scheme is set up as a trust and pays tax in the same way as a trust. Every trust has a trustee, who looks after the assets, collects the income, and pays the bills. They are also the trust's single taxpayer and it is their responsibility to work out the taxable income, complete a tax return, and pay any tax liability arising.

A beneficiary is a person who will ultimately benefit from the trust's assets and income, but before they do, they must rely on the trustee to deal with all of the trust's affairs on their behalf. They therefore have no responsibility to collect income, work out the trust's tax liabilities, report them, or pay them.

In the i-Select Superannuation Scheme, Public Trust is the Trustee, and i-Select Ltd (i-Select) is the Manager. It is the responsibility of i-Select, on behalf of Public Trust, to do all of the income tax calculations, complete the tax return, and organize the payment of any necessary tax.

How Trust tax affects Members

This is why members of the scheme do not have to put any of the income arising from their portfolio within the Scheme onto their tax return. Essentially it is not their taxable income, it is the trustee's, and if they put any scheme income on their tax return it will result in a double charge to tax.

Scheme tax

We calculate the tax position of the Scheme for a year by collating all of the tax reports for each of the members' portfolios within the scheme at the end of the tax year. The taxable income of the scheme is generally made up of income that is fully taxed, income that is not fully taxed and the Scheme's expenses.

Income that is fully taxed includes things like New Zealand interest and dividends and Portfolio Investment Entity (PIE) income. Income that is not fully taxed is mainly foreign interest, foreign investment fund (FIF) income, and currency gains and losses. The expenses of the Scheme include the fees of i-Select (which pays many of the scheme's expenses) and advisers.

Most of the Scheme's tax liabilities are therefore paid at source, leaving only the untaxed income and the expenses. In any given year, this will either produce a net amount of taxable income, or a net loss. Where it produces a loss, the Scheme receives tax refunds and may have losses to carry forward. Where it produces income, it will either consume losses or will result in an overall tax liability that must be paid directly.

On the one hand, the vast majority of FIF income can be reasonably estimated at the start of the year as it depends upon the value of FIFs held on the first day of the year. On the other hand, currency gains or losses in many cases will not be capable of calculation until the end of the tax year, as it depends upon the exchange rate on the last day of the year, 31 March.

The Scheme's tax rate is 28% (as opposed to a family trust's rate of 33%) as it qualifies as a widely held superannuation scheme.

How Scheme tax affects Members

On an individual basis, every member's portfolio has a share of the Scheme's income and deductions each year, which may produce taxable income, or a tax loss, and will contribute proportionately to the Scheme's overall tax position. Regardless of whether the Scheme has an overall tax liability or is due a refund, within the membership at any one time there will be members with liabilities and members with losses. Here's a simple illustration of this:

1,000 members with total tax liabilities of →	$1,000,000
400 members with losses reducing the tax liability by →	$250,000
The Scheme's overall tax liability would be: →	$750,000

Each member will also have tax credits of some sort (e.g. Resident Withholding Tax, Imputation Credits, or foreign tax) which may mean that direct tax payments are not required. Using the above example:

The Scheme's overall tax liability would be: →	$750,000
Total tax credits on income →	$800,000
Net refund to the Scheme →	$50,000

In this way, a person with a tax liability may not be called on to settle their share of the liability immediately because other member's losses and tax credits have deferred the need to make direct tax payments. At some future date when the Scheme's tax position makes it necessary to make a direct tax payment to the IRD, then we may require a full or partial payment of a member's share of the Scheme's taxes. In the interim, they enjoy a tax deferral.

On the other hand, if a member takes full benefits, or if they transfer out of the Scheme, then full payment of tax liabilities is required, and this can cover a number of years of tax liabilities and can be large or small.

In order that members know their tax position each year, we prepare an annual report in which we set out their accrued tax position. This will make clear what tax liabilities have been deferred in the manner described above.

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