

Investing in PIEs

Understanding how your Portfolio Investment Entities (PIEs) are taxed

Many New Zealand managed funds are now registered with the Inland Revenue Department as PIEs or Portfolio Investment Entities. Usually the tax paid by PIEs is the final tax, and you do not need to include anything in a tax return for these investments. However there are a few things that you need to be aware of, and to communicate to your fund manager.

Overview

The tax for Portfolio Investment Entities (PIE) works differently than other types of investments. The tax paid at the PIE level is usually a final tax, so the individual investors do not have to return their PIE income or pay further tax.

When an individual invests into a PIE, the PIE manager is required to collect a declaration from the individual recording their 'prescribed investor rate' (PIR). Income that the PIE earns is attributed to each investor.

The investor will then receive the benefit of the income derived by the PIE on their behalf, less any tax paid on that income (at their prescribed investor rate).

When a PIE makes a loss, a tax rebate is paid to the PIE equivalent to its loss at the investors' PIRs.

The income of a PIE will be reflected in the unit price, with units being cancelled, or issued to reflect the tax paid to, or refunded by Inland Revenue.

Listed PIEs operate slightly differently and are taxed under different rules.

Background

A major driving force behind the PIE regime was the introduction of the Kiwisaver scheme. This prompted the Government to remove some of the disadvantages of investing through managed funds. The PIE regime allows individuals to invest into Kiwisaver (and other PIEs) and not have to worry about filing personal tax returns.

Prescribed Investor Rate (PIR)

When you have a PIE investment, you need to calculate the tax rate, or the PIR, that applies to you. It's your responsibility to advise your fund manager of your rate.

Your PIR will depend on your taxable income, such as salary and interest, and your PIE income over the last two income years. The table on the next page shows the PIR rates that apply, and gives an example of how to determine your current rate.

Getting your PIR right

It's important to choose your correct prescribed investor rate, otherwise you could end up paying too much tax.

PIE income is excluded income. This means you do not include the income in your tax return and the PIE tax is the final tax. The exception to this is when a rate which is lower than your prescribed rate has been applied – see below.

Too high a rate

If you elect too high a rate – for example the 28% rate when you should have elected the 17.5% rate – you will be paying too much tax. There is no mechanism to recover the excess tax.

As soon as you realise you should be on a lower rate you should notify your PIE, as they may be able to reduce your tax for the rest of the year.

Too low a rate

If you elect too low a rate – for example 17.5% when you should have elected 28% – the PIE income attributed to you from your PIE investment will not be excluded income. In other words, it will be taxable income.

This taxable income will need to be included in your tax return. Although the tax paid by the PIE will be allowed as a credit against your tax liability, you will not get the benefit of having your tax capped at 28%. Instead tax will be paid at the marginal rate, currently up to 33%.

No election

If you do not choose a PIR, you will default to the rate of 28%.

Other matters

Benefits of the PIE Regime Investing through a PIE has several additional tax benefits:

- Your PIE income is taxed at a maximum rate of 28%, if taxed appropriately.
- PIE income (if taxed at a high enough rate in the PIE) does not mean you'll need to file an income tax return, if prior to investing in a PIE you did not have to.
- PIE income is excluded income so it does not automatically increase your marginal tax rate.

Some things to watch

There are several tax issues to be aware of when investing in a PIE and filing your tax return (if needed):

If you have tax losses from other sources, your PIR will still be at least 10.5%. If investment income was earned directly, the losses would offset the taxable income and no tax would be paid.

- The mechanism to correct an incorrect PIR operates only if too little tax is paid by the PIE. If too much tax is paid, there is no ability to recover it.
- Make sure you understand the nature of your investment. PIE income is not generally returned, but other investments, including non-PIE managed funds, could give rise to taxable income that needs to be returned.

Income level in the two preceding years (i.e. 2014 or 2015 income years)	PIR for 2016
In BOTH two preceding income years: \$48,000 or more taxable income; AND/OR \$70,000 or more of taxable income plus PIE income	28%
In EITHER of two preceding income years: Between \$14,000 and \$48,000 of taxable income; AND \$70,000 or less of taxable income plus PIE income	17.5%
In EITHER of two preceding income year: \$14,000 or less of taxable income; AND \$48,000 or less of taxable income plus PIE income	10.5%

EXAMPLES		
One An individual earns \$45,000 taxable income in each of 2014 and 2015, and invests in a PIE in 2016. Because their income in either of the two preceding years (2014 or 2015 qualify) did not exceed \$48,000, and their taxable income plus PIE income did not exceed \$70,000, their prescribed investor rate is 17.5% for the 2016 tax year.	Two An individual earns \$45,000 taxable income in 2014, and invests in a PIE in 2015. In 2015, they earn only \$10,000 taxable income and \$30,000 PIE income. Because their income in either of the two preceding years (i.e. in 2014) did not exceed \$14,000, and their taxable income plus PIE income in that year (2014) did not exceed \$48,000, their prescribed investor rate is 10.5% for 2016.	Three An individual earns \$45,000 taxable income in 2014, and \$50,000 taxable income in 2015. They then invest in a PIE in 2016. Their prescribed investor rate in 2016 is 17.5% (because in 2014 they earned less than \$48,000 and didn't exceed the \$70,000 threshold). If in 2016, they earn \$50,000 taxable income again, or their PIE income added to their taxable income exceeds \$70,000, then their prescribed investor rate for 2017 will be 28% (because in 2015 and 2016 they will have exceeded the thresholds).

Know the difference

In some cases there is little obvious difference between investing in a PIE and investing in a bank account, such as a term deposit. Yet the tax effect and your compliance obligations can be quite different.

Listed PIEs

While most PIEs are not listed, some are listed (particularly property trusts). Listed PIEs are taxed differently from unlisted PIEs.

A listed PIE is taxed as a company, i.e. subject to tax in its own right at 28%. Distributions from a listed PIE will be imputed, like a dividend from a New Zealand company.

To the extent that a distribution is considered to be fully imputed, you can choose to return the distribution. You would typically only do this if your marginal tax rate is lower than the level of imputation credits attached, i.e. 28%. The unimputed portion of the distribution is not taxable.

If in doubt about the nature or correct treatment of PIE income, you should obtain professional tax advice.

Bank Account	PIE
Interest is taxable to you as an investor.	Income derived by the PIE is taxable in the PIE.
Resident Withholding Tax (RWT) will be deducted and can be claimed in your tax return	You need to advise the manager of the PIE of your correct tax rate (PIR),
If you are a non-resident, Non- Resident Withholding Tax (NRWT) should be deducted. You may be eligible to be subject to Approved Issues Levy (AIL) of 2 per cent as a final tax, if you are not associated with the payer.	Provided your PIR is correct, you do not need to include any income derived through a PIE in your tax return. The PIR for a non-resident is 28%, unless the PIE qualifies for lower tax rates for non-residents.
If you are a New Zealand tax resident your investment may be subject to the financial arrangement rules. Maximum tax rate for 31/3/2016: 33%	Maximum PIR for 31/3/2016: 28%

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