

*Why we  
need fairer  
taxes for  
savers*

[www.fairtaxforsavers.org.nz](http://www.fairtaxforsavers.org.nz)

# What is the Fair Tax for Savers Campaign asking for?

The Fair Tax for Savers Campaign is asking all the political parties to consider removing the over-taxation of long term savings.

- It wants the effective tax rate paid on KiwiSaver funds to be the same as the marginal income tax rates KiwiSavers would pay on their other income
- It wants term deposits to be taxed only on the real interest rate (actual interest rate less the rate of inflation) rather than the nominal interest rate (the actual interest you receive) as the compensation for inflation is not really economic income.

**New Zealanders are paying some of the highest tax rates in the world on long term savings.**

The amount lost through over taxation is large: in some cases, over a lifetime of retirement savings, retirement earnings are halved.

**The potential gains from reform are equally large: an extra \$100,000 or more for an average wage earner saving for 40 years into KiwiSaver.**

Correcting the over taxation will boost KiwiSavers' retirement nest eggs and the incomes of those with term deposits.

**In one of the most positive, polite, non-partisan, policy requests made in New Zealand political history the campaign offers New Zealanders a personal opportunity to ask their Member of Parliament and party leaders and finance spokesperson for change.**

The policy changes suggested: making the effective tax rates on savings the same as the marginal tax rate savers pay on their other income.

*This is not a KiwiSaver tax rate concession. It just means paying the same effective tax rates as paid on your other income.*

**Taxing only the real part of interest income (the interest rate received less the inflation rate.)**

Those e-mailing and petitioning their MPs are saying: "Like more than 750,000 adults with term deposits and nearly 2 million adults in KiwiSaver, I look forward to your reply."

**FAIR TAX  
FOR  
SAVERS**

## What are the issues the Campaign addresses?

Over taxing, cuts KiwiSaver earnings in half.

Over-taxation of compound interest over 40 years of saving in KiwiSaver creates effective tax rates much higher than someone's marginal tax rate.

Over 40 years saving in KiwiSaver, your earnings are cut 54.7% by the impact of tax for someone in the 33% income tax bracket. This compares with a 7.9% effective tax rate for someone investing in rental property that is 80% debt funded. Effective tax rates measure the difference between what you would have received if no tax was paid on your investment earnings and what you will receive with the tax imposed.

Over-taxation of term deposits occurs by taxing all the interest you receive rather than just real interest (interest less inflation) and doing so each year (thereby reducing the amount you can reinvest).

## What are we suggesting?

- KiwiSaver: That KiwiSaver fund tax rates be reduced so the effective tax rate is the same as the saver's marginal income tax rate paid on their other income.
- Term deposits: That only the real part of interest rates (received over-and-above inflation) be taxed.

The longer you save in KiwiSaver the higher is your effective tax rate so cutting them is of particular benefit for younger KiwiSavers. Bank term deposits are particularly favoured by seniors either close to or in retirement.

## Why is there over-taxation of KiwiSaver compound interest investments?

Pension experts have calculated that if you paid no tax on your pension fund income then for every \$1 you made in contributions you would receive up to \$10 back in retirement income. So for each \$10 of retirement pension \$9 comes from the compounding returns (interest on interest) from your initial \$1, earning returns over the next 40-65 years. In New Zealand if you save in KiwiSaver your retirement income is cut in half by the impact of the tax you pay on the earnings in your KiwiSaver fund.

Roughly you therefore have to save \$2 to get the same nest egg from saving for 40 years or more compared with what you would get by saving \$1 if you paid no tax on the earnings in your fund.

This situation has led to suggestions that KiwiSaver fund tax rates should be reduced so that KiwiSavers only face the same effective rate as their marginal tax rate they pay on their other income.

## Does anyone else support this reform?

In its 2011 report the Savings Working Group recommended the reduction of the KiwiSaver fund tax rates to address the issue of the over-taxation of compound interest products such as bonds held in KiwiSaver funds and in bank term deposits. The Consumers Institute and the Taxpayers Union are supporting this campaign alongside the Financial Services Council.

## What the changes would be worth for typical KiwiSavers

In the examples below the current \$521 Member Tax Credit stays in place.

The impact of lower KiwiSaver fund tax rates over 40 years on retirement nest eggs results in a massive increase.

For example, if a person on the average wage saves 6% of income (3% from them and 3% from their employer) for 40 years in a balanced fund, the retirement nest egg is increased by more than \$100,000.

If the contribution rate or the KiwiSaver's income is higher or the savings are invested in a growth fund the benefits are even greater.

These tax rates are not a concession they represent what savers would pay on any income earned outside of their KiwiSaver fund. KiwiSaver funds are locked away until scheme members reach 65 apart from withdrawals to buy a first home. So each year, savers reinvest the interest earned on interest for up to 40 years.

Removing this over-taxation will reduce the Governments overall tax take. The FSC had earlier suggested a package of changes including defaulting KiwiSavers into balanced or growth funds rather than into conservative funds and cutting KiwiSaver fund tax rates, mainly funded by removing the \$521 Members Tax Credit (MTC) but keeping the \$1000 upfront sign on incentive.

No political party has expressed enthusiasm for removing the \$521 MTC or cutting the KiwiSaver fund tax rates. Our projections which are based on reducing KiwiSaver fund tax rates to boost retirement nest eggs therefore retain the \$521 MTC.

The Impact of Tax Changes on KiwiSaver Balances at Age 65 after 40 Years Saving

		Increase in your KiwiSaver Nest Egg Balance		
		Conservative Fund	Balanced Fund	Growth Fund
	Incomes 2013	Contribution rate 6% (3% from you +3% from your employer)*		
Average wage	\$54,600	79300	109700	150400
Median wage	\$46,900	68700	116200	138500
Minimum* wage	\$28,200	32400	55600	71500
		Contribution rate 7% (4% from you +3% from your employer)		
Average wage	\$54,600	87500	128200	174400
Median wage	\$46,900	78800	128000	147700
Minimum wage	\$28,200	38000	65100	77900
		Contribution rate 9% (4.5% from you + 4.5% from your employer)		
Average wage	\$54,600	94900	167000	230400
Median wage	\$46,900	98100	143900	174100
Minimum wage	\$28,200	46400	75600	95800
		Contribution rate 11% (8% from your employer +3% from you)		
Average wage	\$54,600	113200	219000	281100
Median wage	\$46,900	117500	161600	222800
Minimum wage	\$28,200	54800	86400	116900

\* For someone on the minimum wage contributing 3% the MTC is \$423, not the full \$521. With a 4% contribution rate the full MTC is available. For someone on the mean or median wage the full MTC is available with a contribution rate of 3%.

Source - Infometrics 2014

## Does anyone else think bank term deposits are over-taxed?

The Savings Working Group set up by the Government in 2010 and more recently the Retirement Commissioner have both recommended that only the real part of interest should have income tax paid on it. At the moment savers are taxed on all the actual interest received, not just the real part (the actual interest rate less the rate of inflation). Age Concern also plans to support this reform which particularly affects New Zealand seniors who often rely on term deposits as an income source in retirement in addition to their NZ Superannuation.

### What is the difference between actual interest paid and real interest and why does it matter?

If a term deposit pays 5.75% then that is the nominal interest rate but if inflation is 2% then the real interest rate is (5.75% less 2.00%) or 3.75%.

Economists have long argued that the part of interest paid to compensate for inflation while the money is being used by someone else is not really income and should not be taxed.

**Think about this example.** You lend \$10,000 to the bank for 5 years at an interest rate of 5.75% a year. Over the next 5 years inflation is 2% a year so

when you get your \$10,000 back it then only buys what would have cost you \$9,000 when you lent it. So about \$1,000 of the interest you will receive over 5 years is simply to compensate you for the loss of purchasing power of your original \$10,000 invested. If you apply your marginal income tax rate to that \$1,000, say 33%, you have paid about **\$389** too much tax over the five years.

From the table below you can see how much more after tax income you would receive over 5 years based on the value of your term deposit and your marginal tax rate if you were only taxed on the real interest income you will receive rather than the nominal interest income you are currently taxed on. To be even handed and not reduce the Government's overall tax take only the real component of interest would have to be allowed as a deduction for businesses and property investors as well.

The table below shows you how much you would receive extra over 5 years if we didn't tax the part of your interest that compensates you for inflation and is therefore is not really income, using a bank term deposit invested for 5 years at 5.75%.

If you had a bank term deposit of \$40,000 and your income was about \$18,000 (say National Super) you would be **\$848** better off. Remember people in retirement often roll over their term deposits several times over 15 to 25 years of retirement so the actual savings may be 3 to 5 times these amounts.

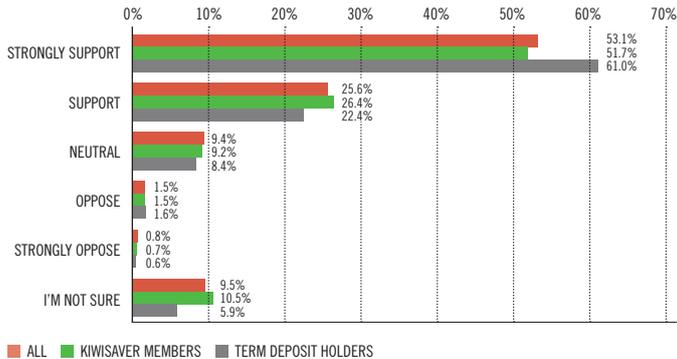
What Extra Income You Would Earn on Your 5 Year Bank Term Deposit Investment Earning 5.75% If Only Real Interest Was Taxed and inflation was 2% each year												
Your Taxable Income	Your Marginal Tax Rate	\$5,000	\$10,000	\$20,000	\$30,000	\$40,000	\$50,000	\$100,000	\$200,000	\$500,000	\$1,000,000	
\$0- \$14,000	10.5%	\$64	\$129	\$258	\$387	\$515	\$644	\$1,289	\$2,577	\$6,443	\$12,885	
\$14,001 to \$48,000	17.5%	\$106	\$212	\$424	\$636	\$848	\$1060	\$2,121	\$4,241	\$10,603	\$21,206	
\$48,001 to \$70,000	30.0%	\$178	\$355	\$711	\$1,066	\$1,421	\$1,777	\$3,554	\$7,107	\$17,769	\$35,537	
Over \$70,000	33.0%	\$194	\$389	\$778	\$1,166	\$1,555	\$1,944	\$3,888	\$7,776	\$19,439	\$38,878	

Source - Infometrics 2014

## The findings

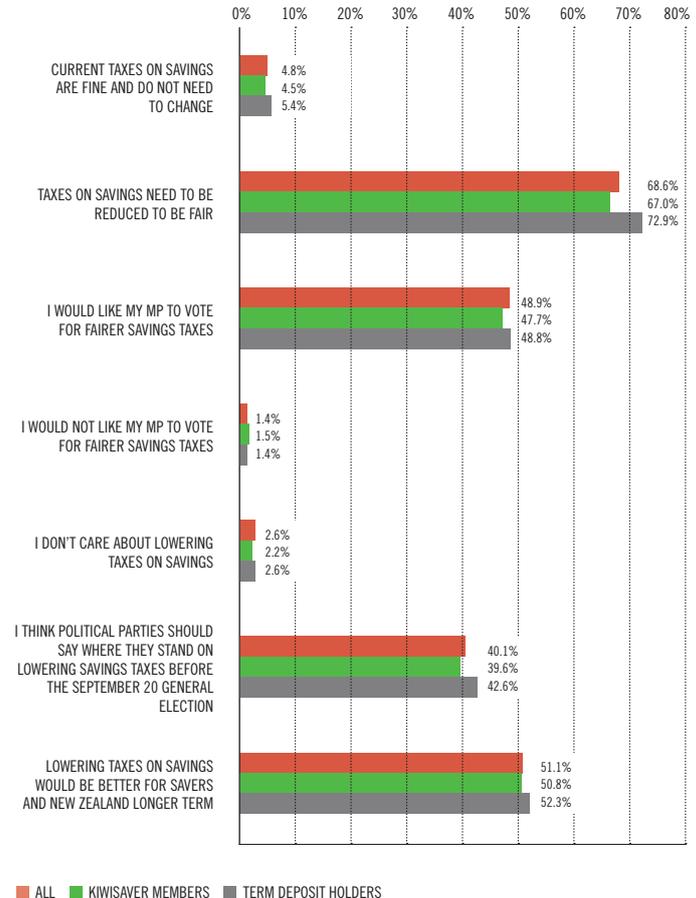
- More than two million New Zealanders have funds in KiwiSaver.
- More than 750,000 adults currently have term deposits.
- 79% want lower taxes on their savings, according to independent polling conducted for the Financial Services Council in June-July, 2014.
- Only 2% oppose lower taxes on long-term savings investments.
- The Horizon Research survey of 2,188 respondents, representing the adult population nationwide (maximum margin of error +/- 2.1%) finds even stronger support for fair savings taxes among those with term deposits with 83% supporting (61% strongly support and 22% support).

DO YOU **SUPPORT** OR **OPPOSE** REDUCING TAX RATES ON LONG TERM SAVINGS INVESTMENTS, SUCH AS TERM DEPOSITS AND KIWISAVER?



- There is a clear view that taxes “need to be reduced to be fair”.
- The majority agree that lowering taxes on savings would be better for savers and New Zealand.
- 48% want their MP to vote for fairer savings taxes.

WITH WHICH OF THESE STATEMENTS ABOUT SAVINGS TAX REFORM DO YOU AGREE?



# *Please cut the taxes on my savings*

E-mail your MP, party leaders  
and spokespeople at  
[www.fairtaxforsavers.org.nz](http://www.fairtaxforsavers.org.nz)

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