

PRODUCT RULING - BR Prd 05/02

This is a product ruling made under section 91F of the Tax Administration Act 1994.

Name of the Person who applied for the Ruling

This Ruling has been applied for by BNZ Investment Management Limited as Trustee (“the Trustee”) of the superannuation fund known as the BNZ 25 NZ Equity Index Fund.

Taxation Laws

All legislative references are to the Income Tax Act 2004 unless otherwise stated.

This Ruling applies in respect of section HH 3(5) and the definitions of “superannuation fund” and “qualifying trust” in section OB 1.

The Arrangement to which this Ruling applies

The Arrangement is the operation by the Bank of New Zealand of a superannuation fund known as the BNZ 25 NZ Equity Index Fund (“the Fund”). The operation of the Fund is governed by the Trust Deed dated 24 February 1997 (“the Trust Deed”) as amended on 23 March 2001, 31 July 2002 and the Deed of Amendment which will be the same as, or not materially different from, the draft deed provided to the Commissioner on 21 June 2005 (“the Amending Trust Deed”).

Further details of the Arrangement are set out in the paragraphs below:

1. The Fund is registered under the Superannuation Schemes Act 1989, as are the “retail” superannuation funds which invest in it.
2. The Sponsor of the Fund is the Bank of New Zealand. The Trustee is also the Manager of the Fund.
3. The Fund acts as a “wholesale” superannuation fund into which other “wholesale” and “retail” superannuation funds invest. The Fund also operates for the purpose of providing retirement benefits to the limited number of natural persons who invest directly in it.
4. Members of the Fund are only treated differently in relation to the application fees, issue price and exit price (to the extent that such prices change over time to reflect the change in value of the Fund) and costs associated with entry into, and maintenance of, the Fund.
5. The “retail” funds investing in the Fund are superannuation funds (both employee and personal) which have previously been (or may in future be)

established completely independently from the establishment of the Fund. For example, an existing BNZ “retail” fund—the Bank of New Zealand Future Lifestyle Plan—currently invests in the Fund. Superannuation funds other than superannuation funds established by or managed by the Bank of New Zealand have also invested in the Fund.

6. The Fund was established for the purposes of being a “wholesale” investment vehicle for other “wholesale” funds and “retail” superannuation funds and for the purposes of providing retirement benefits to the limited number of individual natural persons who invest directly in it. All the “wholesale” and “retail” superannuation funds which invest in the Fund have been or will be established for the purposes of ultimately providing retirement benefits for individual natural persons.
7. The Fund is a passive investment vehicle, investing only in a portfolio of equity securities each of which is listed on the New Zealand Stock Market (“NZSX”) operated by New Zealand Exchange Limited (“NZX”), together with a small cash pool. The Fund will be managed so as to track the composition of a set of listed equity securities which together form the constituent part of an Index known as the BNZ 25 Equity Index (“the Index”).

The Index

8. The Index comprises up to 25 of the largest New Zealand equity securities listed on the NZSX, based on average weekly market capitalisation. The Fund will not be subject to any active management as such. Rather, it will be managed to track the composition of a set of listed equity securities that together form the constituent parts of the Index. The weighting of each security in the Index will reflect its respective market capitalisation at the relevant date.
9. The “home” exchange of each stock can be any of the “grey list” countries as they are defined in New Zealand tax law. If the equity security is listed on the NZSX and meets the other criteria, it will be included in the Index. There is no discretion as to whether a grey-list country security listed on the NZSX is included in the Index. The equity securities will normally be shares but there may also be convertible notes.
10. The market capitalisation for securities is calculated as follows:
 - (a) securities that have the NZX as their “home” exchange will be calculated in accordance with the formula:

number of shares (or convertible notes) on issue x closing price of the share (or convertible note) –

where “number of shares (or convertible notes) on issue” does not include treasury stock;

- (b) securities that have their “home” exchange outside New Zealand will be calculated in accordance with the formula:

number of shares (or convertible notes) listed in New Zealand x closing price of the share (or convertible note)

Cash investments of the Fund

11. Approximately 99% of the net asset value of the Fund will be invested in such investments as the Trustee considers necessary to track the Index. While the majority of available funds will be invested to track the Index, a “cash pool” of up to 1% of the net assets of the Fund will be maintained subject to the exceptions listed in condition (a) of the existing binding private ruling for the Fund (BR Prv 05/16). The pool is only invested in bank accounts or money market deposits.
12. Although it is not an objective of the Fund to invest in cash securities, the Fund may hold cash to facilitate easier administration of the Fund. In any event the cash pool will not exceed what is strictly necessary in order to fulfil the following purposes:
- (a) Allow for cash outflows due to expenses and net withdrawals.
- (b) Allow for net cash inflows from investments and dividends to accumulate to a level sufficient to minimise the transaction and administrative costs associated with analysing which stocks are to be purchased and making the necessary purchase orders.

Index changes

13. Changes will only be made to the Index composition in the following circumstances:
- (a) At the end of each quarter (being a three month period ending on, respectively, 15 April, 15 July, 15 October and 15 January, a “quarter”), securities will be ranked according to their average weekly market capitalisation for the previous 6 month period (i.e., the 6 month period ending on the end of the month preceding the quarter end). If a security not previously included in the Index has risen at the end of the 6 month period above 21st position, that security will be included as a constituent security in the Index at the quarter end and the lowest ranked Index security held at the quarter end will be removed. If a security that is currently included in the Index at the quarter end has dropped below a ranking of 30th by the end of the 6 month period, that security will be removed as a constituent security from the Index and the highest ranked security at the quarter end not already included in the Index will be included.

- (b) At the end of each quarter, securities are reviewed with regard to compliance with the necessary minimum liquidity requirements. In order to be included and to maintain inclusion in the Index, a constituent security must meet a minimum liquidity requirement. Liquidity is defined as the average daily trading volume (over a 6 month period leading up to the end of the month preceding the end of the relevant quarter after eliminating the highest and lowest months), expressed as a percentage of the total issued and quoted securities of the same class. The minimum liquidity measure for inclusion in the Index is 0.75% per month. In the event that there are not 25 securities that meet the liquidity requirement, the number of securities in the Index would be less than 25.

This liquidity test does not apply to a new listing, which falls within the concessionary rule in paragraph (c) below, until the end of the second complete quarter following the quarter in which listing occurs.

- (c) If a security is listed on the NZSX for the first time, it will be included in the Index immediately if:
- (i) it ranks, in terms of market capitalisation, above 21st position (compared with other Index securities ranked according to their average weekly market capitalisation for the 6 month period ending with the month end preceding the previous quarter end); and
 - (ii) at least 25 percent of the security is freely tradeable at the time of listing.

For the purposes of calculating the market capitalisation of a security listed on the NZSX for the first time, the “closing price” of the security will be the undiscounted issue price, as advised to NZX, to be paid by investors who subscribe to the security’s public offering.

The security previously ranked 25th within the Index at that time will be removed.

If a security listed on the NZSX for the first time does not meet the 25% free float test at the time of listing but meets that 25% test at the end of the quarter in which listing occurs or the following quarter, it will be included in the Index at the relevant quarter end (subject to ranking above 21st at that time). Again, the security previously ranked 25th will be removed at that time.

- (d) If the Trustee recommends, and the independent monitor referred to in paragraph 19 agrees, then the Index must be altered to reflect a material change to NZX’s market capitalisation calculation rules.
- (e) If there is a merger, takeover offer, scheme of arrangement sanctioned by the High Court or other offer under the Takeovers Code for all of the issued securities of a company:

- (i) If the merger, takeover, scheme of arrangement or other offer proceeds and as a result (regardless of whether it has 100% acceptance) less than 25% of the company's securities are freely tradeable, the company's securities will be removed from the Index; and
- (ii) The company's securities will be immediately removed from the Index when the acquirer becomes entitled to, and an announcement is made that it will, proceed with compulsory acquisition.

The highest ranked security not already in the Index at that time will be added.

- (f) If there is one or more partial offers under the Takeovers Code for control (50% or more) of a company included in the Index and at any time after such offer or offers less than 25% of the company's securities are freely tradeable, the company's securities will be removed from the Index.

The highest ranked security not already in the Index at that time will be added.

- (g) If there is one or more partial offers under the Takeovers Code for less than 50% of a company included in the Index and at any time after such offer or offers less than 25% of the company's securities are freely tradeable, the company's securities will be removed from the Index.

The highest ranked security not already in the Index at that time will be added.

- (h) If, under the Takeovers Code, a company's shareholders approve an allotment of securities and, at any time after that approval is given, less than 25% of the company's securities are freely tradeable, the company's securities will be removed from the Index.

The highest ranked security not already in the Index at that time will be added.

- (i) If a company's securities are acquired under rule 7(e) of the Takeovers Code and, at any time after the securities are acquired, less than 25% of the company's securities are freely tradeable, the company's securities will be removed from the Index.

The highest ranked security not already in the Index at that time will be added.

- (j) If there is a rights issue or bonus issue (other than a bonus issue election scheme for reinvestment of dividends) to existing security holders, the Index will be changed to reflect the issue of shares on the issue's "ex" trading date. (If the rights issue is not fully underwritten, the adjustment is calculated as if all rights were exercised.)

- (k) If any other capital adjustment event such as a share issue (including under a dividend reinvestment scheme) or share buy-back occurs which increases or decreases the number on issue of any constituent security and that increase or decrease, measured by market capitalisation on a cumulative basis since the

last adjustment, is less than 0.03% of the Index, then any adjustments to the Index will be made at the end of the quarter in which the number of listed securities are increased or decreased. In the event that an increase or decrease represents more than 0.03% of the Index, then an adjustment to the Index will be made as at the close of the NZSX on the 15th day of the month in which the number of listed securities is increased or decreased.

- (l) If there is any other form of capital reconstruction in relation to a constituent security which impacts on the security's Index weighting, the Index will be adjusted on the same date to reflect the capital reconstruction.
- (m) Any changes to the Index composition that are described in paragraphs (a) – (l) (other than where the timing of the change is specified in the relevant paragraph) will be made at the close of business on the 15th of the month, subject to five (5) business days notice of the event occurring.
- (n) The Fund currently owns shares in Westpac (NZ) Investments Limited (WPT). Westpac Banking Corporation Limited (WBC) has decided to exercise its rights to convert these WPT shares to WBC shares. WPT is to be delisted from NZX on 1 July. The WPT shares will be removed from the Index. The WBC shares will be capitalised on the NZSX on 11 July and, as a result of this, are likely to rank above 21st position in the Index. Therefore, the Fund will continue to hold the WPT shares until after delisting and will hold the converted shares (the WBC shares), when issued, until the new capitalisation on 11 July. On 11 July the Index will be altered in accordance with paragraph 13(c) as if the capitalisation of the WBC shares were a new listing and the Fund will be rebalanced. Any residual rebalancing required due to the WBC shares being outside the tolerance levels will be completed at the end of the quarter (15 July). The WBC shares will be held from 1 July to 11 July as part of the Index notwithstanding that these shares will have no value on the NZSX until 11 July.

Rights issues

14. In the event of any rights issue by an Index company, the Manager will retain the entitlement and take up the securities if the securities the subject of the entitlement will be immediately included in the Index.
15. Notwithstanding paragraph 14, if the securities the subject of the entitlement are over-represented, the Manager will sell the entitlement and reinvest the proceeds in securities to track the Index.
16. If the Manager does not know whether the securities the subject of the entitlement will be included in the Index, the Manager will sell the entitlement at the earliest possible time and reinvest the proceeds in securities to track the Index.

Rebalancing

17. The Fund is rebalanced in the following circumstances:
- (a) When the quarterly adjustments are made to the Index;
 - (b) When the Index changes other than quarterly due to market driven changes or corporate actions such as merger, takeover, bonus issue, rights issues and capital reconstructions;
 - (c) If the Fund's holding of a security will be (or is) outside the tolerance levels provided for in paragraph 18 of this Ruling.
18. The Manager will use best endeavours to track the Index as closely as possible. Rebalancing will only occur in accordance with condition (b) of the existing private ruling for the Fund (BR Prv 05/16) and any deviation from the Index remaining after rebalancing will not exceed 1% of the Index.
19. The Trustee has appointed an independent party (the Fund's auditors) to provide an annual confirmation that the operations of the Fund have conformed to these criteria.
20. The Trustee is authorised to accept from an investor a subscription in kind, i.e. a subscription in the form of a basket of securities that achieves a result of the Fund tracking the then Index composition.
21. Disposition of securities by the Trustee on behalf of the Fund (other than those in the cash pool) will only occur in the following circumstances:
- (a) If the Fund is ever wound up.
 - (b) If, at any time, the Index composition changes and as a result the composition of the securities in the Fund no longer tracks the weightings in the Index.
 - (c) If, on any day, there is a net withdrawal of funds from the Fund by investing superannuation funds or natural persons which cannot be met out of the cash pool.
 - (d) If there is a claim on the Trustee in respect of the Fund that cannot be met other than as a result of liquidating some securities. This is not anticipated, but the Trustee needs some ultimate protection against extraordinary circumstances such as, say, a change in taxation law or an unanticipated liability or expense.
 - (e) If the Fund is rebalanced in accordance with paragraph 17 of the Arrangement.

In respect of the events under these subparagraphs, sales of securities will only be made to the extent required in each case.

22. A fee will be payable to the Trustee by each member of up to 0.3% per annum of the value of the units held by that member (plus GST, if any).
23. Each investing superannuation fund must make a minimum initial contribution to the Fund of \$200,000 or such lesser amount as the Trustee with the written consent of the Sponsor may approve.
24. Under the Trust Deed for the Fund, members of the Fund have an individual Member Account, into which is credited any contributions by the member together with any growth in value of the funds invested. It is anticipated that the Member Accounts will be calculated and recorded on a unitised basis, i.e. the total value of the Fund will be divided into units and each member will be allocated the number of units which reflects their respective contributions and earnings.
25. The Fund is required to buy and sell shares as required to ensure that it continues to correspond to the Index. Such buying and selling will not be motivated by any intention to derive a profit or gain from such sales. In this regard, the Trust Deed states:

The Fund and the Trustee do not have an intention to profit from holding, acquiring or selling Index Company securities.
26. The powers contained in clause 10.1(h) of the Trust Deed will only be exercised to facilitate the purposes of the Fund and in any event will only be used in accordance with paragraph 25 of this Ruling.
27. Members may from time to time elect to withdraw funds from the Fund. A substantial withdrawal from the Fund could be in the millions of dollars. In that circumstance, the Fund may not be able to fund the withdrawal in one portfolio trade as, depending on the market circumstances (including liquidity), brokers are likely to be limited as to the size of the trade they will accept at all. Even if a broker (or brokers) did accept a trade of significant size, they would not be able to guarantee that the trade would be completed or settled within 3 business days. In these circumstances the Fund will accumulate funds to the full withdrawal amount.
28. The Manager does not have the power to purchase units from Members.
29. The Applicant has confirmed that all aspects of the previous private ruling (BR Prv 02/33) and the private ruling prior to that (BR Prv 01/17), relating to the Fund, have been complied with, except that:
 - in regard to the previous ruling, on the takeover of Powerco Limited by Prime Infrastructure Networks (New Zealand) Limited, the Manager did not rebalance the Fund to include a replacement security until the following quarterly rebalancing. As a result, there was a period where the number of securities held by the Fund was 24. For the avoidance of doubt, this has been

disclosed as a circumstance of non-compliance even though the previous ruling was silent on the date of reintroduction of a replacement security; and

- in regard to BR Prv 01/17, the Fund received a compulsory share acquisition by court order which required the Fund to hold non-Index shares. This occurred during the Fletcher Energy acquisition when the Fund was issued shares in a company that did not track the Index. (The shares were in a United States company called Capstone. Each Fletcher Energy shareholder was issued with a small number of Capstone shares as well as other consideration.) As it was a court approved compulsory acquisition, the Manager had no choice but to receive those shares. The terms of the issue of the Capstone shares meant that all the recipients had to hold the shares for a period of time before they could sell them and use the proceeds to invest in the Index.

30. There has been no change to the Trust Deed of the Fund (except for the noted amendments dated 23 March 2001, 31 July 2002 and the Amending Trust Deed), nor any change to the management or operation of the Fund since its establishment.

Conditions stipulated by the Commissioner

This Ruling is made subject to the following conditions:

- a) The Fund is a registered superannuation scheme under the Superannuation Schemes Act 1989.
- b) The existing binding private ruling for the Fund (BR Prv 05/16) (or any such replacement ruling) remains in force and continues to apply in all respects to the Arrangement.
- c) The Amending Trust Deed provided to the Commissioner on 21 June 2005 will be executed by 31 August 2005 so that it is the same as, or not materially different from, the draft deed provided to the Commissioner.

How the Taxation Laws apply to the Arrangement

Subject in all respects to any assumption or condition stated above, the Taxation Laws apply to the Arrangement as follows:

- The Fund is a “superannuation fund” as defined in section OB 1.
- The Fund is a “qualifying trust” under paragraph (b) of the definition of “qualifying trust” in section OB 1.
- Amounts derived by investors as a result of withdrawals from the Fund are excluded from income by virtue of section HH 3(5).

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 1 July 2005 and ending on 30 June 2008.

This Ruling is signed by me on the 30th day of June 2005.

David Kelly
Manager (Financial Sector)