

# TAX INFORMATION BULLETIN

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September 2007

## CONTENTS

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Get your TIB sooner on the internet	3
This month's opportunity for you to comment	5
<b>Binding rulings</b>	
Product ruling – BR PRD 07/04	6
<b>New legislation</b>	
Order in Council: Deemed rate of return set	10
<b>Regular features</b>	
Due dates reminder	11
Your chance to comment on draft taxation items before they are finalised	13



## GET YOUR TIB SOONER ON THE INTERNET

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This *Tax Information Bulletin* is also available on the internet in PDF. Our website is at **[www.ird.govt.nz](http://www.ird.govt.nz)**

The website has other Inland Revenue information that you may find useful, including any draft binding rulings and interpretation statements that are available.

If you prefer to get the *TIB* from our website and no longer need a paper copy, please let us know so we can take you off our mailing list. You can do this by completing the form at the back of this *TIB*, or by emailing us at **[tibdatabase@ird.govt.nz](mailto:tibdatabase@ird.govt.nz)** with your name, details and the number recorded at the bottom of the mailing label.



## **THIS MONTH'S OPPORTUNITY FOR YOU TO COMMENT**

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Inland Revenue produces a number of statements and rulings aimed at explaining how taxation law affects taxpayers and their agents.

Because we are keen to produce items that accurately and fairly reflect taxation legislation, and are useful in practical situations, your input into the process—as perhaps a “user” of that legislation—is highly valued.

The following draft item is available for review/comment this month, having a deadline of 30 September 2007:

<b>Ref.</b>	<b>Draft type</b>	<b>Description</b>
IS0097	Interpretation statement	GST – Apportioning supplies under section 5(14)

Please see page 13 for details on how to obtain a copy.

## BINDING RULINGS

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This section of the *TIB* contains binding rulings that the Commissioner of Inland Revenue has issued recently.

The Commissioner can issue binding rulings in certain situations. Inland Revenue is bound to follow such a ruling if a taxpayer to whom the ruling applies calculates tax liability based on it.

For full details of how binding rulings work, see our information booklet *Adjudication & Rulings, a guide to binding rulings (IR 715)* or the article on page 1 of *Tax Information Bulletin* Vol 6, No 12 (May 1995) or Vol 7, No 2 (August 1995).

You can download these publications free from our website at [www.ird.govt.nz](http://www.ird.govt.nz)

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### PRODUCT RULING – BR PRD 07/04

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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 Assure Funds Management Limited as Administration Manager of the International Equity Index Fund.

#### Taxation Laws

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

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

#### The Arrangement to which this Ruling applies

The Arrangement is the operation of the International Equity Index Fund (“the Fund”) pursuant to the Trust Deed of the Fund, dated 1 July 2001, as amended by a Deed of Amendment dated 21 December 2001 (“the Trust Deed”), and further amended by a Deed of Amendment and the final Deed of Amendment (as previously submitted in draft to the Rulings Unit on 11 June 2004 (“the Amending Deed”). Subsequently by way of Deed (undated) the Trustee of the Fund was changed from BNZ Investment Management Limited to Tower Trust Superannuation Limited. Further, by way of deed dated 31 January 2006 the sponsor of the Fund was changed from Bank of New Zealand to Arcus Investment Management Limited.

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

- 1) The Fund invests in equity securities that correspond to the composition of the Morgan Stanley Capital International World Index (“MSCI”), modified such that the securities

invested in will be of those countries specified in Part A of Schedule 3 to the Act (“grey-list countries”) that each comprise 1% or more of the MSCI (“the Modified World Index”). The Fund has been designed to enable investors to obtain, through one security, the same financial results that can be obtained through the direct investment in the securities of those companies that make up the Modified World Index.

- 2) The Trustee of the Fund (“the Trustee”) is Trustees Executors Superannuation Limited.
- 3) The Administration Manager of the Fund is Assure Funds Management Limited (“the Administration Manager”). The Investment Manager of the Fund is State Street Global Advisors, Australia, Limited (“the Investment Manager”).
- 4) The Sponsor of the Fund is Arcus Investment Management Limited (“the Sponsor”).
- 5) The Fund is a wholesale superannuation fund into which other wholesale and retail superannuation funds invest. The Fund was established for the purpose of being a wholesale investment vehicle for retail superannuation funds, other wholesale superannuation funds and for the purpose of providing retirement benefits to the limited number of natural persons who invest directly in it. Unless the prior approval of the Trustee, with the consent of the Sponsor, is obtained, the minimum initial investment into the Fund is NZ\$200,000.
- 6) The Fund is registered under the Superannuation Scheme Act 1989.
- 7) The Trust Deed states that:

*The investment policy of the Fund will be:*

- a) *to invest the Fund (other than the Cash Pool) in accordance with Schedule 2 to this Deed only in such investments as the Trustee considers necessary to track the modified grey list components of the World Index; and*
- b) *to invest the Cash Pool in restricted investments, being deposits with banks, and*

- 8) The Fund buys and sells shares as required to ensure that it continues to correspond to the Modified World Index. Such buying or 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 Trustees do not have an intention to profit from holding, acquiring or selling Index Company securities.*

- 9) The Applicant has confirmed that all material aspects of the previous rulings (Prv 97/125, Prv 01/11, Prv 01/65, Prv 01/114, Prv 04/28, Prd 97/38, Prd 01/30, Prd 02/01 and Prd 04/10), relating to the Fund, have been complied with, except that:
- a. The earliest rulings did not refer to the Investment Manager's ability to sell securities where an individual security was outside its tracking weight; and
  - b. In some cases investments from natural persons have been below \$200,000.
- 10) The only amendments to the Trust Deed are those contained in the Amending Deed. There has not been any material change to the management or operation of the Fund since its establishment.

*Date of Adjustments*

- 11) The Fund is re-balanced in the following circumstances:
- If a security is outside its Modified World Index weight by the lesser of–
  - 0.5% of the total Fund, whether positive or negative; or
  - three times the Modified World Index weight of the individual security; and
  - When the periodic (currently quarterly) adjustments are made to the MSCI; and
  - If there are any MSCI market driven changes (as identified in clause 3.3 of the current *MSCI Methodology Book: MSCI Standard Index Series Methodology*) or corporate actions such as a merger, takeover, new listing or reduction or increase in capital affecting any index company in the Modified World Index.
- 12) Such re-balancing will occur at the earliest practicable time after the above events have occurred and in any event within five business days.

*Events that trigger acquisitions or realizations*

- 13) There are certain reasons or events when investments held by the Fund will have to be bought or sold. The Trustee will only dispose of securities (other than cash pool investments) if:

- the Fund is wound up;
- there is a change in the Modified World Index and composition of the securities of the Fund no longer tracks the Modified World Index (whether as a result of a change to the countries included or a change to the securities included);
- there is a compulsory acquisition of one of the Fund's securities or a security is acquired on a compulsory acquisition, merger or takeover which does not track the Modified World Index;
- there is a net withdrawal of funds from the Fund by members;
- there is a claim on the Trustees in respect of the Fund which cannot be otherwise satisfied; or
- the Fund is re-balanced in accordance with the first bullet point in paragraph 11, above.

*Rights Issues*

- 14) In the event of any rights issue by an index company, the Investment Manager will retain the entitlement and take up the securities if the securities the subject of the entitlement will be immediately included in the Modified World Index.
- 15) Notwithstanding paragraph 14, if the securities the subject of the entitlement are over-represented, the Investment Manager will sell the entitlement and reinvest the proceeds in the index companies to track the Modified World Index.
- 16) If the Investment Manager does not know whether the securities the subject of the entitlement will be included in the Index the Investment Manager will sell the entitlement at the earliest practicable time (and in any event within five business days) and reinvest the proceeds in the index companies to track the Modified World Index.

*Mergers, Takeovers and Share Buy-backs*

- 17) The Modified World Index may be adjusted from time to time because of mergers, takeovers, share buy-backs, distributions of capital, cash issues, and substitutions of companies in the Modified World Index.
- 18) In the event of a merger or takeover of a Modified World Index company the Investment Manager will adjust the Fund portfolio at the earliest practicable time (but in any event within five business days) to the time the Modified World Index is adjusted. The Fund will not accept an offer unless as a consequence of not accepting the offer the Fund would track the Modified World Index less accurately than if it had accepted the offer.

- 19) The Investment Manager will not participate in an optional share buy-back by a Modified World Index company.

*Hedging*

- 20) There is no specific provision in the Trust Deed that allows the Fund to hedge foreign exchange risks.
- 21) The Fund will not take any action to hedge or manage foreign exchange risks or exposures that arise from the investments of the Fund being held in non-New Zealand currencies.

*Borrowing*

- 22) Clause 10.0 (c) of the Trust provides:

*...The Trustee may:*

*borrow money for the purpose of the Fund upon terms and conditions agreed by the Sponsor and the Trustee and charge all or part of the assets of the Fund with repayment and payment of interest on the moneys so borrowed;*

- 23) Pursuant to the ruling, the Fund can only borrow in the following circumstances:

- To temporarily fund the redemption of units when the cash pool has insufficient funds; this borrowing must be repaid at the earliest practicable time, and in any event and such borrowing will be repaid within three business days;
- Where a security is sold and another purchased and a settlement mismatch occurs resulting in the Fund's bank account becoming inadvertently overdrawn, and in this event for no longer than strictly necessary;
- To temporarily fund the purchase of securities in order to rebalance following a merger, where pursuant to the merger payment due to the Fund for securities that have been disposed of has been delayed (such delay being beyond the control of the Fund), and in this event for no longer than strictly necessary; or
- For advances (not to exceed total borrowings for \$5,000) by the Administration Manager to the Fund to meet expenses of the Fund, where the Administration Manager's expense account is insufficient to enable the Administration Manager to meet such expenses.

*Cash investments held by the Fund*

- 24) Although it is not an objective of the Fund to hold cash, the Trustee and the Investment Manager may hold cash to facilitate the easier administration of the Fund. The cash held by the Trustee and the Investment Manager is on "call".

Wherever possible, futures contracts will be entered into by the Investment Manager to cover cash held by the Investment Manager. This is **known** as "equitised cash".

- 25) The Investment Manager **or** the Trustee will hold cash in the following circumstances:

- Following the sale of securities in the course of tracking the Modified World Index or in the course of a compulsory acquisition, merger, takeover, share buy-back or distribution of capital pending the reinvestment of that cash;
- Following a contribution to the Fund, pending the investment of that contribution;
- Following the sale of securities to meet a request for withdrawal by a member;
- When a dividend is paid to the Fund in respect of an investment in a security;
- To accumulate the minimum amount of cash required to allow for minimum trade sizes and to obtain a reasonable representation of the number of securities on the Modified World Index ("the minimum investment level"). The Investment Manager has advised that this amount is presently approximately \$US 3 million. The minimum investment level may increase (or reduce) in the future to the extent that a different amount is required to purchase the equivalent representation of securities on the Modified World Index.

- 26) The Investment Manager may hold up to an amount equivalent to the minimum investment level in cash (including both free and equitised cash). This threshold may be exceeded in the following circumstances:

- for up to ten business days preceding a MSCI Structural Change or for up to three business days following a significant new investment;
- for up to three business days after a MSCI Structural Change;
- for up to ten business days prior to a pending withdrawal in respect of which it has received a withdrawal request.

- 27) In addition to any funds held by the Investment Manager, the Trustee may hold up to NZ\$2 million in cash. This threshold may be exceeded in the following circumstances:

- for up to ten business days if there are withdrawals pending in respect of which it has received a withdrawal request; or
- for up to three business days if the excess results from a significant new investment.



- 28) At all times, there is a limit on the total cash (including cash held by the Trustee and free and equitised cash held by the Investment Manager) of 5% of the total Fund (except if there is a significant withdrawal or investment).
- 29) The Investment Manager will use best endeavours to equitise all cash, subject to futures contract size constraints.
- 30) The following futures contracts are used:

Country	Contract
Australia	SPI200
Canada	S&P/TSE60
Japan	Topix
Germany	DAX
United Kingdom	FTSE100
United States	S&P500
Spain	IBEX35

- 31) In the event that alternative futures contracts in one or more markets enable improved tracking of the Modified World Index, or that one or more of the above contracts ceases to exist, the Investment Manager will use such alternative contract or contracts.

*Dividends*

- 32) The Investment Manager will receive the dividend (and other income) distributions from the securities in which funds are invested and will hold these as part of the cash pool, subject to the terms of paragraph 25 above.
- 33) The Investment Manager will not elect to participate in any dividend reinvestment plan.

*Foreign Currencies*

- 34) The Investment Manager may enter into spot foreign exchange contracts where these are necessary in order to purchase or sell the foreign currencies necessary to invest in Modified World Index securities. These contracts are not speculative and are settled within two business days.

*Suspension of subscriptions and withdrawals*

- 35) Clause 18.7 of the Trust Deed enables the Fund to suspend the payment of benefits relating to withdrawal requests. The Fund has not previously suspended withdrawals. The Fund also has the power under clause 3.2 of the Trust Deed to refuse any application for membership without giving reasons. The Fund has never exercised this power.

- 36) The Fund will only suspend withdrawals or subscriptions in the following exceptional circumstances:
- if the volume of withdrawals is too large to be processed; or
  - if the volume of withdrawals exceeds the immediately available funds; or
  - trading on the relevant equity markets has been suspended.
- 37) Any suspension will only be for three business days unless the exceptional circumstance giving rise to the need to suspend is beyond the control of the Trustee and Investment Manager, in which case the suspension will only be for such period as is strictly necessary for the Trustees and/or the Investment Manager to recover from that event.

**Conditions stipulated by the Commissioner**

This Ruling is made subject to the following conditions:

- a) The Fund will not be resettled in order to enhance the performance of the Fund or to minimise losses of the Fund in any way.
- b) Subject to condition (a), if the Fund is resettled this Ruling will continue to apply until resettlement. If the Fund is resettled this Ruling shall not apply from the date of resettlement.
- c) The Fund is an investment vehicle primarily for investment into by superannuation funds which are themselves either: (i) widely-held investment vehicles for direct investment by natural persons or, (ii) vehicles for investment (directly or indirectly) by other superannuation funds that are widely-held vehicles for direct investment by natural persons.
- d) The Fund is registered under the Superannuation Schemes Act 1989.
- e) All investors in the Fund who are not natural persons are registered under the Superannuation Schemes Act 1989.
- f) The existing binding private ruling for the Fund (BR Prv 04/10) remains in force and continues to apply in all respects to the Arrangement.

**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 that term is defined in section OB 1.

- The Fund is a “qualifying trust” as that term is defined in section OB 1.
- Investors are not assessable to income tax on withdrawals from the Fund, by virtue of section HH 3(5).

## The period or income year for which this Ruling applies

This ruling will apply for the period 1 July 2007 to 30 September 2007.

This Ruling is signed by me on the 23<sup>rd</sup> day of March 2007.

**Maryanne Hansen**  
Sector Manager, Investigations

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## NEW LEGISLATION

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### ORDER IN COUNCIL

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#### Deemed rate of return set

The deemed rate of return for taxing foreign investment fund interests has been set at 10.27% for the 2006–07 income year, up from 9.82% last year.

The deemed rate of return is set annually and is based on an average of five-year government stock, to which a 4 percent margin is added. It is one of the methods that can be used to calculate income from foreign investment fund interests.

The new rate was set by Order in Council on 23 July 2007.

*Income Tax (Deemed Rate of Return, 2006–07 Income Year) Regulations 2007 (2007/210)*

## REGULAR FEATURES

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### DUE DATES REMINDER

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#### September 2007

**20 Employer deductions**

Small employers (less than \$100,000 PAYE and SSCWT deductions per annum)

- *Employer deductions (IR 345) or (IR 346) form and payment due*
- *Employer monthly schedule (IR 348) due*

**28 GST return and payment due**

#### October 2007

**23 Employer deductions**

Small employers (less than \$100,000 PAYE and SSCWT deductions per annum)

- *Employer deductions (IR 345) or (IR 346) form and payment due*
- *Employer monthly schedule (IR 348) due*

**29 GST return and payment due**

These dates are taken from Inland Revenue's *Smart business tax due date calendar 2007–2008*. This calendar reflects the due dates for small employers only—less than \$100,000 PAYE and SSCWT deductions per annum.



## YOUR CHANCE TO COMMENT ON DRAFT TAXATION ITEMS BEFORE THEY ARE FINALISED

This page shows the draft binding rulings, interpretation statements, standard practice statements and other items that we now have available for your review. You can get a copy and give us your comments in these ways.

**By internet:** Visit [www.ird.govt.nz](http://www.ird.govt.nz)

On the homepage, click on "Public consultation" in the right-hand navigation bar. Here you will find links to drafts presently available for comment. You can send in your comments by the internet.

**By post:** Tick the drafts you want below, fill in your name and address, and return this page to the address below. We'll send you the drafts by return post. Please send any comments in writing, to the address below. We don't have facilities to deal with your comments by phone or at our other offices.

Name \_\_\_\_\_

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***Draft interpretation statement***

IS0097: GST – Apportioning supplies under section 5(14)

***Comment deadline***

30 September 2007

*No envelope needed—simply fold, tape shut, stamp and post.*

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stamp  
here

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