Issue Two: Twenty Twenty Three

OPPORTUNITIES | PATIENCE | GROUNDWORK

Covisory Connect

MAGAZINE

About us

[but really all about how we can assist you with your issues and concerns]

Are you looking to understand what is important to you from your perspective?

We partner with you to help you understand what is truly important to you. We help individuals, families, and their businesses to exceed their expectations for what matters most to them.

Have a problem?

We work with you to transform how you conduct your businesses and trusts. We help you to build enduring, resilient frameworks and capabilities across all that you do.

Our team defines us

Covisory is a team that are united by a strong set of values, with a deep commitment to making a positive impact through our work and how we connect with you, our client.

With an expert team with significant technical and commercial experience based New Zealand and Internationally, we combine local insight and global expertise and contacts to help you turn your goals into reality.

Our consultants include accountants, lawyers, designers, business managers, entrepreneurs, strategists, researchers, and writers. We can provide you with the right team, with the right expertise and experience when you need it.

All our people have been drawn to Covisory for the opportunity to apply their expertise to important complex challenges that you face.

Our reputation is defined by our interactions with our clients

- We help clients build strong systems to achieve better performance through data.
- We work with you to build positive outcomes for your future, and for future succession.
- We create solutions that are always in partnership with you, that uniquely combine our expertise and the particular resources of your business and family circumstances. We deliver innovative solutions that create immediate results and a strong framework to sustain your progress into the future.

OUR PURPOSE

To be innovative customer centric advisers exceeding your expectations for your business, trust, wealth & tax needs

Covisory Website

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Interactive - Click to Navigate

NIGEL SMITH
Founder -
Covisory Group

Welcome to New Zealand's meteorological and economic winter.

Welcome to our latest Covisory Connect. Thank you for your continued feedback around how much you enjoy reading our eMagazine. We try to provide content for you that we believe is relevant, stimulating and will cause discussion that is pertinent to the current point in time that we find ourselves in.

I am writing this on one of the shortest days of the year. It is New Zealand's meteorological winter, but you could also say that we are in our economic winter as well. Economies move in cycles and currently we are in that cold bleak period of a recession. Anyone that tells you they are doing alright, is either very fortunate or lying. Everyone is finding it tough out there and we consider that it is not likely to improve for a while yet.

Election years are always slow, particularly as the election grows closer, and this year will be no exception. Anyone that thinks that centre right has already won the election, think again as there is a real danger of the wasted vote if New Zealand First cannot get either a seat or 5%. In October 2020 they polled at 4% and failed to get a seat, then that's 4% the centre right missed at the end of the day relative to the centre left. In my mind this election is anything but a foregone conclusion.

The spectre of a Greens wealth tax has weighed heavily on the minds of many of our clients. We have had a lot of interesting discussions and already seen several wealthy Kiwis leave New Zealand never to return. Their money has gone with them overseas and won't be coming back. While we may replace them with wealthy migrants, those are people who are only just buying a passport and the opportunity to come here if they want. They will only move enough money to New Zealand to fulfil their immigration requirements and not the balance of their wealth. It is a false economy to believe that what has left can be replaced.

As part of this, we have also seen families looking at succession around their trusts and where beneficiaries are based. From the start of 2023 we have seen a significant increase in work in this area and continue to see a lot of difficulty around getting capital out of trusts to beneficiaries who reside in foreign countries that have unsympathetic tax regimes, often with the spectre of up to 70% of the distribution going in foreign taxes. This is an area where we continue to work with clients closely.

The one thing we do know about both meteorological and economic winters is that they do pass with time. While we can go and get on a plane and leave New Zealand as many are to enjoy the sunshine, it will take longer for us to see the economic winter pass. Higher interest rates will be with us for a period of time but that does not mean that opportunities don't exist. 2023 is certainly going to prove to be a difficult year, but there are opportunities on the horizon. With the property market looking like it has potentially reached the bottom or close to it, hopefully we will see the economy starting to improve gradually over time. If only the Reserve Bank and the Government could get inflation under control to permit more sensible and realistic interest rates for the future.

Like you, we look forward to sunnier times.

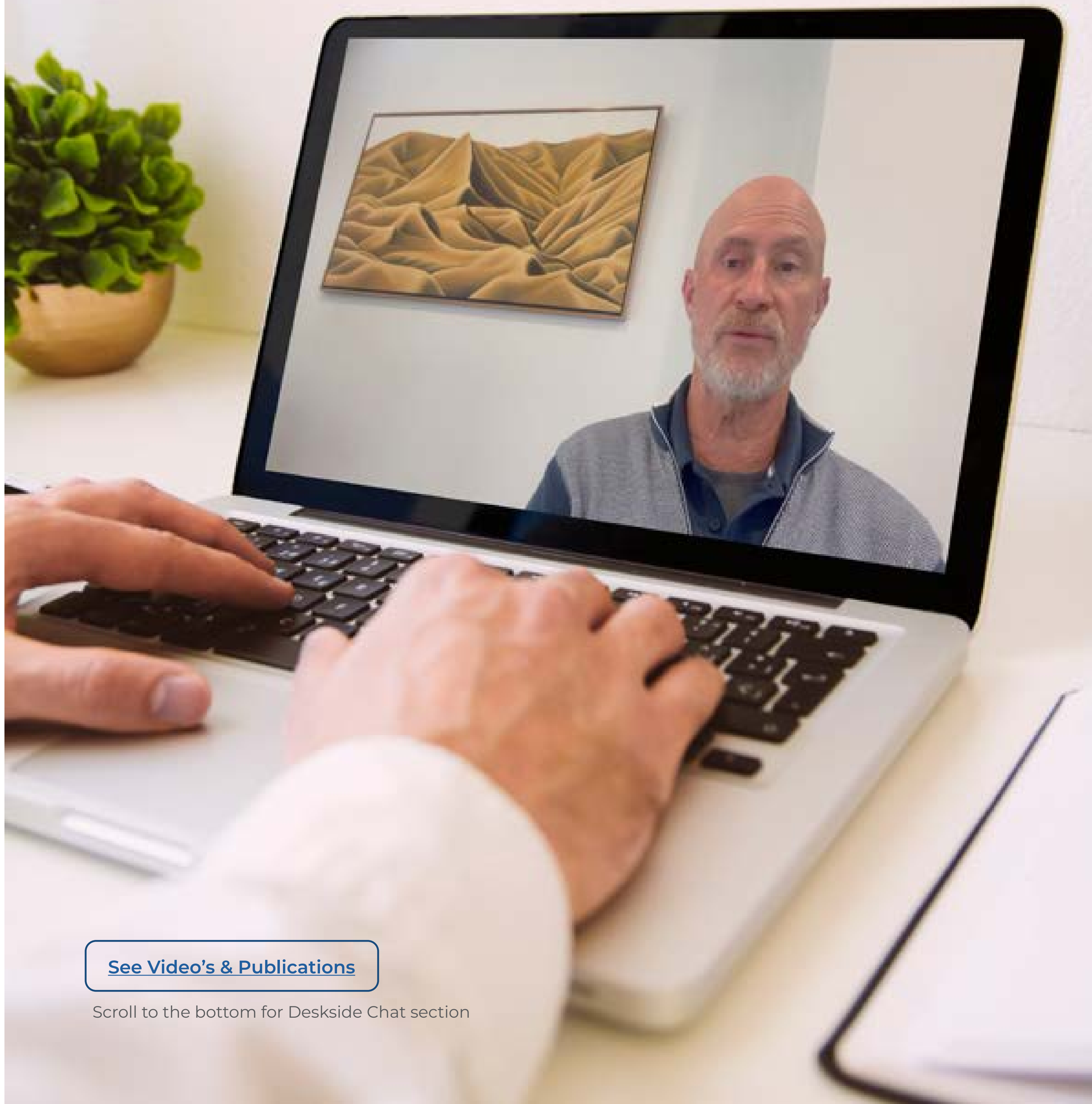
Nigel

Covisory Deskside Chats

Two new topical short information videos have been added to our on-line vblog collection.

1: Taxing the rich

2: For beneficiaries of a Trust, place of residence matters



See Video's & Publications

Scroll to the bottom for Deskside Chat section

The recession is coming.

– Europe, North America, Australasia, and global perspectives.

ECONOMIC OUTLOOK:

The wolf is coming; the wolf is coming! Most people know the Greek fable about the boy, who frightens the whole village with his cries of a threatening wolf; there is no wolf, but the boy gets the attention he wants.

Aesop's Fables, The Boy Who Cried Wolf. Illustration: Francis Barlow, 1687

History is often – somewhat dismissively – mentioned when the current economic situation is discussed, and I can understand it, if you feel like resigning somewhat towards the many financial reports we're currently receiving; but that's hardly a good idea.

Because if the recession becomes a reality on an international scale, across the board – company earnings will suffer and this will mean lower share prices, just as the bond market will experience falling yields and rising prices.

Admittedly – I've also howled a bit as part of the chorus. Because, together with several of my local and international colleagues, I've also been proclaiming for a long time that 'the recession is indeed coming'. But even if it hasn't happened so far in many parts of the world, recession is still Covisory's main scenario ('live reality') for the world economy over the coming period.

The latest signs became evident only a few weeks ago (at the end of May), when the German economy officially entered a 'technical recession' with two consecutive quarters of negative growth. In fact, as we all now know, this was also recently reported closer to home with New Zealand now too in a recession as official data shows that the economy has contracted over two consecutive quarters.

At Covisory, we follow the developments closely, and unfortunately, our expectation is that it may turn out to be a slow winter season (summer season of course in the Northern Hemisphere) for the world economy, or perhaps a decidedly hard out springtime (autumn period in the North). It is difficult to answer exactly when a recession will start in individual economies and how long it will be upon us, but we have no doubt that it will come to most.

In the battle that is currently being fought in the 'economic arena', there are three major points of contention, the outcome of which may provide an answer to whether the recession will take hold – broadly or not.

Point of contention number one: When does monetary policy actually work?

Historically, monetary policy interest rates have risen rapidly in the world economy since 2022.

It has largely happened because of the focal point since the corona pandemic: Inflation. Put at the forefront worldwide it's the job of central banks to ensure low and stable inflation.

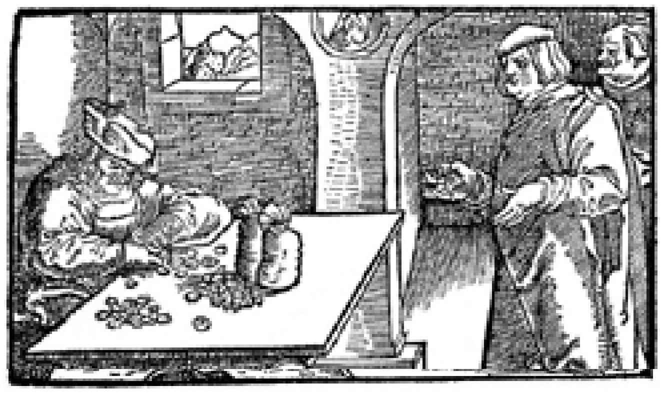
In the world of central banking, this translates into inflation that will be around two (2) percent within two (2) to four (4) years. Inflation has not been close to that for almost two (2) years, and it hurts deep inside the central banks.

Therefore, interest rates have been raised and tight monetary policy has taken over from the global pandemic as the most powerful headwind for the world economy right now.

But when do interest rate increases affect the economy? Immediately? In a few months or in a year? If you want to get into a fight with an economist then that's potent the question, which must be asked – and undeniably it's extremely difficult to clarify!

The theory goes that higher interest rates usually lead to lower economic activity, but the textbooks aren't clear on when – and the data isn't much help either.

To take an example, Scandinavian homeowners (and Kiwis alike, for that matter) with variable interest rate mortgages have already felt the effects of rising interest rates, while homeowners with fixed interest loans only feel indirect rate increases through lower house prices.



Interest rate payments on the rise. Photo: Alamy Stock Photo

But nevertheless, 'when?' is an extremely important question here and now. If the effects of the past year's monetary policy tightening have already hit the economy, then central bank governors Jerome Powell in the US and Christine Lagarde in Europe may have to hit even harder with the 'interest hammer', because the world economy is not yet in balance.

This will mean falling prices for fixed-income securities (bonds) as well as shares. If the effects of the 'interest hammer' only come now or over the coming months, then the central banks may just have hit hard enough or even too hard – and not much more should come from monetary policy.

Whether international central banks raise interest rates further depends both on what individual central banks think about, when the interest rate hammer will hit the economy, but also on their own assessment of whether inflation has fallen or not.

Point of contention number two: Is inflation falling?

Without prejudice, it should immediately be easy to conclude from the data, whether inflation is falling or rising; but this isn't always the case – because more often than not, the devil is in the detail. If you look at the entire index and calculate inflation as the change from May 2022 to May 2023, inflation in the US, for instance, is five (5) percent as measured by the consumer price index – and this has been falling for a long time.

Now, if you look at core inflation, which is cleaned/stripped of the price of food and energy – and consider the development over the past three (3) months, then inflation is also five (5) percent, but it has fundamentally been increasing or flat since December 2022.

The crisis and depression spawned by the five-year hyperinflation (1618-1623), AKA in German – the "kipper-und-wipperzeit.Photo: Kipper, Wipper and Kings Who Were Clippers

Both parts are strictly correct, but the conclusions and implications are VERY different. If inflation has peaked, then the monetary policy has worked – and then that hammer can go back into the toolbox!

If the inflationary curve hasn't really been broken, then more monetary policy tightening will be needed. For example, there are parts of local pocket economies, which haven't yet (markedly) been affected – namely insular labour markets. Here, in some cases – wages rise unabated and continue to push up prices and thus inflation.

Point of contention number three: U or V?

If the demand for labour increases and the supply does not keep up to the same extent, then the price of labour – that is, wages – must rise. It sounds very good with higher wages, but here again we run into the central bank hammer ...

Because if wages rise too sharply, it will be extremely difficult to keep inflation at bay. Think, for example, of the hospitality industry, where a large part of expenses goes towards staff salaries. And when a restaurant's expenses increase, the restaurant must increase its prices.

The labour markets in both North America and across Europe are currently growing; for example, there are around six (6) million unfilled positions in the US alone! In the short term, there's only one option to bring the labour market back into balance: Reduce the demand for labour. This is essentially, why the final point of contention (point 3) is basically how it will most likely play out ...

Unemployment can increase – this is the U (unemployment), or the number of open unfilled positions can decrease – this is the V (vacancies). It is hugely important to the question of recession or not, whether the labour market can be brought into balance through decreases in open vacancies or through increases in unemployment.

The Great Depression was the worst economic crisis in US history when unemployment reached 25%. When the pandemic hit in 2020, the world hadn't felt that level of economic tragedy in nearly a century. Photo: AP Photo

If wage growth can be moderated without unemployment rising, then the economy can be brought back into balance and inflation can return to a tolerable level for the world's central banks without requiring a definite decline in economic activity

Conversely, rising unemployment almost certainly means a recession with a decline in growth. Whether it'll be unemployment – i.e. U – or open positions – i.e. V – which will get us out of the current situation, it is difficult to say. Theoretically, it's entirely possible that companies will cut positions without dismissing the existing staff to a large extent; but let it be said, this has never happened before.

Possible landings

When we put everything together, here at Covisory we have come to the conclusion that the world economy, almost by necessity, has to fall into a decline in growth. It will not be the GFC 2.0, but it'll be a real recession with increasing unemployment and loss of financial security and welfare for households – as well as an anticipated loss of production for most companies.

From personal experience – and as well as an important lesson learned from global economics and the theory thereof – I know that if something isn't sustainable, it must stop; and the longer you wait, the harder the fall. In other words: The recession will spread, internationally – sooner or later, because growth must slow, and the rate of wage increases need to fall somewhat.

Otherwise, the world's central banks will never reach their inflationary targets.

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Investors are made aware that investments may be associated with a risk of loss that cannot be determined in advance, just as past returns and price developments cannot be used as a reliable indicator of future returns and price developments. For further information, please contact us.

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Looking for Staff?

Don't forget Kiwis who want to come home.

If you are recruiting staff, don't forget to consider the multitude of Kiwis who have been living offshore and looking for the right role to come home to. As everyone ages, so does the pull of family and familiarity to return home to increase. It is often a matter of seeing the right role.

Working in a larger, more competitive environment can be helpful in building your business's technical capability but also the bench strength of your management team. While there is no doubt that re-integrating back into NZ has its challenges for returnees, a well-structured onboarding process can reduce this risk.

Advertising for staff is as simple as a social media campaign. On Facebook alone, there are groups such as "Kiwis returning to NZ from Australia" (8,400 members), "Hoki Mai" (17,000 members) and "Kiwis in Aussie" (83,000 members).

There is a myriad of groups in cities e.g., London, Hong Kong etc who can be reached easily and cost-effectively through social media. Many groups are simply social, but it is a low-cost way of getting your name in front of talent and networking back into NZ. They may know someone who could be interested in your job or company. Consider Seek or similar platforms in the country in which you are looking to recruit e.g., Australia.

Crossing the Tasman to interview is now approaching a cost-effective level as competition increases with an improved number of flights.

Tip: In your job post always include that only NZ or Australian Citizens or NZ permanent residents will be considered (unless you are planning to support a visa process).

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Relationship Property

With all the media around trusts being about increasing tax rates and potential wealth taxes, the New Zealand Supreme Court recently ruled on a relationship property case which should give everyone who has a trust in a relationship pause for concern.

For a while now courts have been viewing trusts as an impediment to sorting out relationship property claims and this case is no different.

On the face of it, it appears the party in the relationship who set the trust up did a lot right but missed one crucial step which left all the trust property available to a relationship property claim.

As this case is from the Supreme Court, it is the last word on how similar relationship property claims will be viewed in the future.

The facts of the case are straightforward. Mr Sutton and Ms Bell had been in a de facto relationship for over seven years and had two children together. Just before the commencement of the relationship Mr Sutton – with Ms Bell's encouragement – transferred his residential property to the trustees of a trust that had been set up to hold the property. When the relationship ended Ms Bell made a claim under the Property (Relationships) Act 1976 (PRA) that Mr Sutton had transferred his property to the Trust to defeat her claim or rights under the PRA. Using section 44 of the PRA Ms Bell argued the transfer to the trust should be set aside and a half interest in the property should vest in her. Unsurprisingly, Mr Sutton argued section 44 did not apply as the property was transferred before the couple's de facto relationship commenced.

The dispute made its way through the lower courts with all of them being consistent that section 44 applied in these circumstances. The Supreme Court allowed the appeal from the Court of Appeal by Mr Sutton and the trustees of the Trust to be heard.

It found: Section 44 can apply to dispositions made prior to the commencement of a de facto relationship.

The Supreme Court interpreted that section 44 is wide in its construction and applies to all property, not just relationship property. Also important was the fact that Mr Sutton and Ms Bell had a clear intention to commence a de facto relationship when Mt Sutton transferred his property to the Trust.

The transfer of the property does not require a definitive purpose to defeat rights or cause loss under the PRA. It was enough that Mr Sutton had knowledge the transfer of the property would defeat Ms Bell's future PRA claims. Also, the fact Ms Bell knew of, and supported, Mr Sutton's transfer did not matter as there was no valid contracting out agreement under the PRA.

The result of this had the Supreme Court conclude that Mr Sutton's transfer of the property was done with the intent to defeat Ms Bell's PRA claim. It ordered that half of the property would vest in Ms Bell.

The conclusion here is although there was no intent from either Mr Sutton or the trustees of the Trust to defeat any RPA claim, their actions still lead to this. This situation could have been solved if Mr Sutton and Ms Bell had put in place a section 21 contracting out agreement at the same time the transfer of the property was made to the Trust. The section 21 agreement would have made it clear that the property owned by Mr Sutton was personal property and not relationship property. It is a bit surprising in the circumstances that Mr Sutton's advisers did not raise this as an option.

The lesson is that if you are entering into a relationship and want to protect your assets then a section 21 agreement is compulsory. Without it, you are opening yourself up to RPA claims.

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TAXATION:

Taxing the Rich

Recently the Green Party released its tax policy manifesto. Normally this isn't something that grabs our attention but given recent events in the New Zealand tax world and there is a real chance of Labour and the Greens retaining power, we think it is worthwhile considering the implications of what they proposed.

The rich list review provides an argument for the fact that rich people don't pay enough tax at least on economic income. This is simply because we don't tax capital gains in New Zealand. People that make real money in New Zealand also make it from capital gains due to the sale of property, shares or businesses. All those things are legitimately tax-free in most cases in New Zealand.

So, the problem with this is that the Labour government through their Revenue Minister David Parker has done the rich list review. Their analysis of the review indicates a need to get more tax from the rich. More importantly, we know there is a big hole in the budget and the government needs more money. Taxing the rich more will not hurt their own voter base ~ the majority of the "rich" are not going to vote for Labour and most likely the same with the Greens.

So, what was the Green Party's manifesto? Well, it is quite frightening if you haven't caught up with it. Firstly, they would increase the corporate tax rate to 33c, this is not bad, but it makes New Zealand somewhat internationally uncompetitive. More importantly, they would increase the top marginal personal tax rate and likely therefore the trust tax rate to 45%. For individuals that would apply to incomes over $180,000 the current threshold for the 39% rate.

More problematic is the proposal to bring in a wealth tax, an annual tax on an unrealised basis. To clarify a capital gains tax is when you sell an asset when you realise it and you have got the cash. In comparison a wealth tax is an annual charge whether you have sold the asset or not so, i.e., it is on unrealised gains.

There are two parts to it, for individuals it would be a 2.5% per annum charge on assets with a value over $2m with the exemption available to each of a husband and wife. Now it is not clear what happens if a husband or wife dies, does the exemption then drop back to $2m, we don't know as there is no detail.

For trusts, it is a flat 1.5% from the start. Now obviously the question is how do you value assets? For the land you could use CV for anything listed which is pretty straightforward. It is for unlisted things like shares in companies and businesses that you would need to value and that could be problematic. Maybe you use a particular figure and for 5 years you are aligned and then you must reset it. We don't know the details yet but there may be some further work done around this area.

TAXATION:

There would be few exemptions in what the Greens have talked about. So what does that all mean practically and why am I worried about this for my clients? Firstly, the Green's mathematics says that in year 1 they will raise $12b in additional tax from the 0.7% of New Zealanders that would be affected by these changes. Now I don't think that includes the companies when they say the 0.7% but from the individuals and the wealthy. So that is a lot of money coming from very few New Zealanders.

So, what are we likely to see? The first thing is we haven't seen the Labour Party manifesto yet but with the Green Party manifesto kicking the ball down the road that far, it means that Labour can come in again with some reasonably aggressive tax policy that will probably seem a lot more neutral or acceptable than what the Greens are proposing. Obviously, if the Greens and Labour end up in a coalition together it will be interesting to see how hard the Greens push for this. They have become more of a social conscience party than a "green" party, which is an interesting change in their political landscape.

What I am seeing in my client base, which has a lot of wealthy New Zealanders, is that people are either leaving New Zealand or looking to leave New Zealand. We have had significant enquiries from rich New Zealanders asking how do I break my New Zealand tax residence and how do I get out of here.

Obviously, there are a couple of parts to leaving New Zealand. Firstly, you must break that tax residence and I will come back to that in a moment. The second is the extent that you still have assets here. It is likely that non-residents would be subject to wealth tax in New Zealand on their assets here as well as residents. So simply leaving New Zealand as a tax resident isn't going to solve the problem if you leave all your assets behind which means ultimately that you are going to end up selling your assets here over time.

Returning to breaking your tax residency, there are two parts to this. First, you must be out for 325 days in any 365-day period and then you are deemed out from the first day. The days don't have to be consecutive, and any part day counts as a whole day. Mechanically simple and not that difficult to do. Secondly is the permanent place of abode. This is the one that is going to be more difficult. You are going to need to sell your home and you are probably going to need to sell your Bach or Baches. For many this is going to be the one that is difficult, that is the emotional break to New Zealand. We really are leaving. We are not coming back, and we haven't got a bolt-hole here. Some people say you can have them owned by a trust but if they are still available it will still count as a place of abode and that view is incorrect.

It is going to be interesting to see what it does and whether we get new rich migrants coming in to replace the Kiwis that are leaving. In my opinion, for what it is worth, is that those coming in won't bring that amount of money back into New Zealand. People who have come here from overseas will tend to maintain investments outside of New Zealand. They will do the minimum they need to meet our investment criteria but not a lot more.

So watch this space, it is going to be an interesting few months leading up to the general election on the 14th of October 2023. Firstly, the Labour Party tax manifesto and to see what it says and then the actual election results itself. Remember if Labour and the Greens get in, the Greens want this policy to apply from 1 April 2024, so people are only going to have a window of 4 or 5 months to start getting their affairs in order.

We are already seeing it with our clients reviewing their structures, looking at their estimated wealth and coming up with a plan for them to leave if they want to in the future. At least by having the options identified up front and if, heaven forbid, the Greens and Labour were to get into power then they have got a lifeboat planned already in place. Yes, they will still have assets here that will take some time to sell down but the steps to break their tax residency are under way or can easily be put underway.

Something to think about.

If you would like updates for this and other areas relating to New Zealand Tax, Business and Trusts please join our Mailing List.

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TAXATION:

International wealth – the NZ IRD and taxation:

Perspectives from Europe, in local context – Wealth Tax; To be, or not to be, that's the question ...

HIGH-NET-WORTH-INDIVIDUALS (HNWI): Since 2021, the New Zealand Inland Revenue (IRD) has carried out research to find out more about how much tax is paid by New Zealand's high-wealth individuals relative to their economic income, a concept of income that's broader than taxable income.

To undertake this research, the IR has used tax administration data, data from public sources and collected information from the individuals involved in the research. The data has been analysed and recently published; but before we look at this in a bit more detail, let's put it into context; and let's consider other jurisdictions of comparative interest.

The richest one (1) percent has hijacked two-thirds (⅔) of all newly created wealth during the corona crisis. At the same time, we are experiencing the largest increase in global inequality since the Second World War. Graphic: Financial Times

Swedish wealth tax under pressure

Back in 2005, the Swedish Finance Minister at the time, Paer Nuder was considering removing the wealth tax in Sweden, which is in clear contrast to what he was championing less than one year earlier. At the time, Mr Nuder said, referring to wealth tax, "it is not on the agenda;" – but then, Mr Nuder suddenly came up with other ideas ...

When the EU introduced a law that could make certain types of investments tax-free, Mr Nuder feared a flight of capital outwards from Sweden. The wealth tax in Sweden back then meant that families with a fortune of over SEK 3 million (equivalent to ca. NZD 450,000) had to pay 1.5% wealth tax. However, major changes to the tax system of that time would not be discussed until after the general elections in 2006.

The wealth must remain in Sweden

Fast forward to 2007, it was confirmed that the abolition of the wealth tax would cause the richest Swedes to leave their millions in Sweden, which in turn would lead to increased investment in Swedish businesses. According to the plan, this furthermore gave employment a tailwind boost.

To this day, right across Europe and amongst select Scandinavian countries there's a general consensus that an often referred to term of "envy tax" is unnecessary and will lead to wealth and business flight – whereby large fortunes will move out of the country, if a permanent wealth tax is introduced.

In fact, Denmark's wealth tax was abolished way back in 1996! This was a result of a European Central Bank research piece, which found that higher capital taxes lead to less revenue in Denmark. This is because higher capital taxes in Denmark lead to fewer investments, prosperity and thus the tax base.

In contrast, Norway to this day still tax their wealthy; more about that later on in this article ...

TAXATION:

Actually, there aren't very many countries left with a wealth tax. Currently, out of the OECD's 38 member countries, only four (4) countries still continue to implement the wealth tax on individuals. The five countries are Colombia, Norway, Spain and Switzerland.

Crunch time – and in times of economic hardship

Taxes on net wealth have been declining in Europe over the last twenty (20) years. But the topic has regained momentum in times of fiscal consolidation and strong macroeconomic adjustment needs, particularly in vulnerable countries. Iceland and Spain reintroduced the tax during the crisis, and from time to time we see this popping up on political agendas in other European countries; we're currently experiencing stark debate including here in New Zealand (as we speak). At the same time, the academic discussion around the possibility of levying taxes on assets has increased.

Covisory has prepared this Connect article/briefing note aiming at giving an overview of the type of wealth taxes that are implemented in Europe. The topic of taxation of wealth is highly controversial, but also very complex. The lack of a common definition and the large interpretation of what is a wealth tax explain the diverging information that can be found when mapping the European countries, which today have a wealth tax in place.

If wealth taxation is such a good idea, why did Europe kill theirs? – Euro flop?

Normally progressives like to point to Europe for policy success. Not this time. Ongoing experimentation with the wealth tax in Europe was a failure in many countries. France's wealth tax contributed to the exodus of an estimated 42,000 millionaires between 2000 and 2012, among other problems. Consequently, over the years 2018/2019, French president Emmanuel Macron ultimately killed it off.

In 1990, twelve (12) countries in Europe had a wealth tax. Today, there are only three European countries that levy a net wealth tax are Norway, Spain and Switzerland. Countries with wealth taxes only on selected assets, such as real estate, include France and Belgium. Examples of countries with no wealth tax are Portugal, Monaco and Liechtenstein.

You can obtain residency and earn a foreign income tax-free as well as access reduced national tax rates to avoid paying higher taxes on local income, making Portugal one of the lowest tax countries in Europe.

Outside Europe

Several countries around the world don't charge a wealth tax. Gulf states in the Middle East with oil wealth, like Bahrain, Kuwait, Oman, and the United Arab Emirates, don't charge taxes on wealth. A number of Caribbean countries don't impose wealth taxes or taxes on other assets offshore, such as the Bahamas, the Cayman Islands, Antigua and Barbuda, and St. Kitts and Nevis.

You can also steer clear of wealth taxes in Pacific islands like Vanuatu and the Solomon Islands – and a disputed territory like Western Sahara.

The truth about wealth taxes in Europe

There are many myths about wealth tax in Europe, so let's seek to set the record straight. Although collaboration across many legal policies exists, Europe does not have a uniform wealth tax system, and there is no continent-wide wealth tax. Individual countries' tax authorities make their own decisions about whether or not to implement a wealth tax, and they set their own rates.

European wealth taxes vary considerably from country to country. Some countries impose very high rates (up towards 5%), while others have none at all. The vast majority of countries in Europe that impose a wealth taxation fall somewhere in between rates of 0.1% to 0.5%.

The wealth tax definition explained

A wealth tax is a tax imposed as a percentage of everything an individual owns (assets), less any liabilities. Liabilities include any debts or financial obligations, such as a mortgage or personal loans.

There are two (2) specific types of wealth tax; 1.) Net wealth tax: A tax is levied on a person's global net worth; and 2.) Wealth taxes on selected assets, whereby a tax is levied on selected assets of what a person owns.

According to recent reports by the OECD and others, there were some clear themes with the policy, which could be of real value for New Zealand policy makers to ponder, not to mention of real insight to the New Zealand general public, broadly speaking:

1.) It was expensive to administer;
2.) It was hard on people with lots of assets but little cash;
3.) It distorted saving and investment decisions;
4.) It pushed the rich and their money out of the taxing countries—and, perhaps worst of all
5.) It didn't raise much revenue (after all).

TAXATION:

NZ IRD project scope

Let's get back to the high-wealth individuals research project recently published here in Aotearoa New Zealand; it looks at how much tax is paid by high-net-worth families in New Zealand. The Revenue calculated their effective tax rates – that is the tax they pay relative to their income – using an economic measure of income; 300+ families were covered by the analysis.

Similar to research undertaken using the Household Economic Survey, the IR's analysis is based on the family unit, which includes partners and dependent children. The project also incorporates the income, and tax paid, of companies and trusts associated with the family units.

IRD's aim is for the findings of the research to help assess the progressivity and efficiency of the New Zealand tax system and will allow for the provision of more robust advice on future tax policy. The project does not seek to make policy recommendations but may feed into future policy advice.

External input

A Methodology Advisory Group of external experts from economics, statistics and tax disciplines were consulted as the project methodology was developed. Report findings were subject to peer review by two academic peer reviewers.

Privacy

Results presented in the report have been aggregated to ensure the identity of individuals is protected. The privacy and security measures implemented during the project are outlined in the Privacy Impact Assessment.

The New Zealand Treasury report

The NZ Treasury has conducted a similar study on the effective tax rates paid across the full income and wealth distribution. NZT found that the country's wealthiest 1% own more than a quarter of the country's wealth.

Furthermore, a recent report from Oxfam Aotearoa found New Zealand's tax system contributed to the gap between the rich and poor. It found that the tax system was effective at collecting revenue, but this had a direct impact on unequal income distribution.

Wealth tax and taxation, generally, have been hot topics of discussion in recent weeks following the Inland Revenue's research, which concluded that the wealthiest New Zealanders paid 8.9% tax on their incomes, on average.

As always, there's no silver bullet

In a survey of 135 economists across 40 countries – incl. Denmark – 87% believe that the rising cost of living is helping to increase inequality in their country, while 71% of the economists believe that the rising inequality is partly due to the falling taxation of the richest.

The fact remains that, over the past 40 years, governments across countries have lowered taxes for the richest, whether it applies to income tax, inheritance tax or the tax on share income.

This is happening while in many countries there is a lack of money for education and health. With more money, you will be able to help the most vulnerable people globally, who are currently struggling with hunger and drought – and at the same time invest in climate adaptation and education. It will also be possible to abolish the poverty-creating schemes that we see across so many of the world's nations.

A fairer taxation of wealth cannot solve all the world's problems, but it may just be one of the viable tools at hand for curbing rising inequality and finding resources for the crises we face. We need to ensure that the world's wealth is distributed for the benefit of the majority and not just the few. The extreme increase in wealth has prompted over 200 millionaires, worldwide to write a letter, in which they write that "the politicians of the world need to tax us – the super-rich – and you need to start now"!

Millionaires unite

The ongoing tax debate very much stepped up in earnest post-COVID, when in July 2020, Kiwi rich listers Sir Stephen Tindall, Peter Torr Smith called for taxes on the wealthy to be raised. And even back then, the Greens kicked off their 2020 election campaign with plans for a wealth tax and higher income tax brackets (a rare instance of history repeating).

The Warehouse Group founder Sir Stephen Tindall and Hire Things founder Peter Torr Smith were two (2) of 174 millionaires to have signed the missive at the time. The letter, which was also signed by the Disney Company's Abigail Disney and Ben and Jerry's ice cream co-founder Jerry Greenfield, asks countries to recognise the function the world's richest can play in relieving the economic impacts of coronavirus.

"As COVID-19 struck the world, millionaires like us have a critical role to play in healing our world. No, we are not the ones caring for the sick in intensive care wards … but we do have money, lots of it," the letter reads. "Money that is desperately needed now

TAXATION:

and will continue to be needed in the years ahead, as our world recovers from this crisis. "Today, we, the undersigned millionaires, ask our governments to raise taxes on people like us. Immediately. Substantially. Permanently."

Close to 100 wealthy Kiwis speak out: "We'd like to contribute more to society"

On our very own home turf, some of the wealthiest Kiwis in Aotearoa know they pay lower tax rates than most – and have signed a letter explicitly asking to pay more. In an open letter, titled "Sharing wealth through paying more tax", more than ninety (90) of the country's richest addressed "the public and the politicians of Aotearoa New Zealand," and asked that they be made to pay higher tax rates.

The letter bluntly asked politicians to "back a tax system that asks more from those who can most afford it". "We write as people who are frustrated with how much tax we pay. We want to pay more," the letter opens. "As people leading financially comfortable lives, we might be expected to be anti-tax. But we recognise tax as a shared contribution to our collective success. It funds everything from the teachers who give our children a great start, to the DOC rangers who look after our environment, through to the health care professionals on whom we all rely."

"As Cyclone Gabrielle has made horribly clear, the cost of responding to the climate crisis, repairing the public realm and future-proofing our infrastructure will only increase. And that will require a bigger tax contribution from those who can afford it."

Signatories include Sir Ian Taylor, Phillip Mills, of gym chain Les Mills, company director Rob Campbell, actress Robyn Malcolm and Dame Susan Devoy.

The group want to call on everyone, who lives and works in Aotearoa New Zealand to back a tax system that asks more from those who can most afford it – and urge politicians to make that a reality.

The group says tax is one way to build a better world and are proud to pay it, and ready to pay their fair share.

Les Mills executive director Phillips Mills says higher taxes for the wealthy would lift the poorest Kiwis out of poverty. Source: Stuff

Mills said wealthy people should be paying more than they were. He would be in favour of both a capital gains tax and wealth tax. "Those who can afford it should be paying significantly more taxes." He says it's "bad for the economy to be tax-advantaging asset classes like residential property".

Fellow signatory, Sir Ian Taylor said there was so much talk about tax being a burden and not enough people thought about the benefits it could deliver for better access to healthcare, education and infrastructure. He said New Zealanders' attitudes towards tax needed to change – to start thinking about it as a "social contract" of sorts as people did in the Nordics and other European countries.

"The only words we put with tax are burden, relief; everything is a negative about tax, but actually I believe it is part of a social contract that we all have to each other."

In conclusion

As with most things, only time will tell where all of this will land, around the world, across Europe, North America, closer to home in OZ – and here at home in clean, green Aotearoa New Zealand.

One thing's for sure, opinions remain mixed!

Further reading - Web links of interest:

1. Briefing requested by the BUDG committee – EU Parliament 2022 relating to this subject can be found here: **Read More**

2. The Cost of Extreme Wealth is a campaign powered by the Patriotic Millionaires, Patriotic Millionaires UK, Millionaires For Humanity, and taxmenow. Their Letter for the Attention of our Political Leaders attending Davos can be found here: **Read More**

3. High-wealth individuals research project document – prepared by Policy and Regulatory Stewardship, NZ Inland Revenue can be found here: **Read More** and further research background information about tax and the economic income of the wealthy (in New Zealand) can be accessed here: **Read More**

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BUSINESS:

Reference Checking

In this article about the recruitment process I will comment based on my experience in the recruitment industry, with a focus on what I believe is a critical part of the process and, something that will provide valuable information on the best way to manage a new employee for optimum results.

Reference checks are not a tool to help you decide if you should employ a candidate or not, although, as you will see from an example I will provide later, they can have that impact! The decision to hire a particular candidate should be made before taking reference checks.

In the US companies are very resistant to providing any information other than the role and dates employed by a former employee. Occasionally, you may be successful in obtaining personal comment from a co-worker, but in the litigious environment, unsuccessful candidates have taken legal action against the person and the former employer providing the reference checks.

This leads us to the New Zealand situation and requirements for reference checking. Privacy legislation requires that a candidate must give permission before reference checks are undertaken. In my view, having this permission in writing removes any possible misunderstanding. I think that can be appropriate to do this at the time of the interview, as part of the decision to shortlist a candidate, using a standard form and advising the candidate that they may be asked to provide the names and details of referees at a later date.

It is imperative to provide some structure to the reference check that you will make, remembering that you should try and undertake two or more in my view. You should formulate questions that confirm the referee's role in the organization and if the candidate was a direct report. Ensure you have open-ended questions about areas where you may have minor concerns. Ask about the breadth of the role the candidate filled, and their achievements, confirm dates and ensure they match.

Always ask the candidate to contact the referees nominated, to advise you will be calling. Remember New Zealand is a village; there is a possibility that you may know someone in one of the companies the candidate has worked for. You can suggest and encourage the candidate to use that person as a referee if the working relationship validates this. You should not contact the person you know without permission.

Moving on to the reference check phone call: Most reference checks are done over the phone, although several times during my career I have done them face to face. On most occasions, this isn't an option. Always confirm who the person you are talking to is, their role in the company, and their relationship with the candidate. Make sure that they are willing and have time to participate in the process. You may need to call back at a better time.

Ask open-ended questions and encourage the referee to speak freely. That's when the gems of information will come out. Talk about the candidate's achievements, performance, and specific skills, ask why the candidate left (or is leaving) the role.

My final question is always 'Would you re-employ (or employ)?'

Challenge any response that signals doubt or is not YES. Why? What would you change? Was there a problem?

If the answer is NO, ask why.

A client of mine asked me to help on one occasion when they had a candidate, who, on paper and in the interview looked a star. I had not been involved earlier in the recruitment process, but came in for the second round of interviews because something just didn't feel right ... and it wasn't. I offered to do some reference checking and the candidate willingly provided referees from his last three roles.

The references were good to glowing. Then I asked "Would you re-employ?"

There was a resounding NO. and many senior executives said no one had asked that before. It turned out this candidate had an issue with using company credit cards for his own use, taking from the company and general dishonesty. When I asked

why they were providing good reference checks on the former employee, they all said that as part of the termination process, they agreed to provide positive references for that person. Apart from the morality and integrity of that agreement, each of the subsequent employers had suffered because of poor process, and a desire to take the easy way out of an employment contract.

My process saved my client embarrassment and the cost associated with exiting a habitually bad employee. One of the few times a reference check has resulted in a decision not to employ.

The information gained from a reference check can be invaluable for managing a candidate, Previous experience can show where development is required, where additional skills and knowledge can be used for your company's benefit, and even help with retention.

One final point; a reference check is the result of communication between you and a nominated party. The candidate is a third party to this conversation and is not privy to the information gathered from the process. Many companies make the error of putting written details of reference checks from their recruitment consultants or notes from their own checks in the candidate's HR files. To me, this is an error. It potentially breaches the confidence of the referee, if and when the candidate chooses to review their file and can have a negative impact in the event of an employment dispute!

As a recruiter, a reference check is a good barometer of my search and selection process. If aspects confirm my recommendations and views, then my judgement is confirmed, and if not then I need to ask, "What did I miss?" For an employer in the market to hire, it also supports the integrity of the company's process.

Do your reference checks; they are valuable tools in your recruitment toolbox.

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Meet David Ealson
Director Cornerstone Search NZ Ltd

David has 37 years in the recruitment industry, the past 23 in executive search. He uses search techniques at all levels when clients struggle to find and hire performers in their industry. David works across Australasia and has a global network of partners he works with.

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Tax in Brief

Tidy Up for the Bright-Line Test

The Bright-Line test was introduced to our income tax legislation to tax gains on the sale of residential property disposed of within a certain time period from the acquisition. Initially, it was a two-year period and it has now moved to a ten-year period.

The test has been subjected to numerous legislative changes over this time. However recent changes have been introduced to prevent taxpayers from being subject to the test (and a tax bill) for transfers of residential property where there has been no effective change of economic ownership of the property.

The changes mostly apply from 27 April 2021 (where the bright-line test period moved to ten years) although there are some changes that only apply from 1 April 2022.

"Rollover relief" from the bright-line test can now be obtained from transfers of property to the following (subject to meeting the relevant criteria in the legislation):

- Family Trusts (from 1 April 2022);
- Look through companies;
- Partnerships;
- Transfers within wholly owned groups of companies;
- Settlements under te Tiriti o Waitangi.

"Rollover relief" does not provide an exemption from the bright-line test but means the original state date for the test is retained by the recipient of the residential property.

Importantly "rollover relief" can be applied where the property is transferred by a family trust back to the settlor of the trust or transferred to another family trust under a resettlement (subject to meeting the legislative criteria).

These changes are taxpayer-friendly and the general principle is that transfers that do not change the economic ownership of property should maintain the original acquisition date for bright-line purposes.

However, the legislative provisions are complex and require substantial analysis to ensure that the transfer being considered can obtain "rollover relief". Advice should be obtained prior to transferring any residential property that might be subject to the bright-line test.

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Where are my trust beneficiaries living?

In New Zealand for a long time, we have exported our young talent, either permanently or temporarily overseas, on trips called “the Big OE” and similar. We often don’t think much about this when our kids leave, and the impact that that may have on trusts where they are beneficiaries.

Over the years Mum and Dad may get older, and eventually they may die. The kids may or may not have come back from overseas by that time. The problem is if they haven’t returned and the trust has built up significant wealth, then before anyone realises it, distributing wealth to those children who are overseas from the trust in New Zealand, is suddenly not very tax effective in the overseas jurisdiction.

This is because many overseas countries tax distributions from foreign trusts of income and/or capital gains as if that income is either income or capital gain in that country, whether or not tax has already been paid on it in New Zealand. In some countries, as discussed in other past Covisory Connect articles, there may even be wealth taxes or transfer taxes on that wealth that passes to the beneficiaries in those foreign countries. In some cases, we have seen potential tax imposts of up to 70% of amounts being distributed.

Where should you start?

Let’s use the starting point that you have a trust in New Zealand, as a trustee, as a settlor, as a parent, you need to know where your beneficiaries are and whether it is possible to get income to them in the future.

Taking a simple example, Johnny or Mary leave New Zealand and decide to go on their big OE to the UK. While there, they meet someone and decide to stay on a bit longer. Typically, they ring up Mum and Dad in New Zealand and ask for some money to help them buy a house in the UK, particularly given how expensive the houses are, and the fact that the Kiwi dollar doesn’t buy a lot of pounds.

Even though they may be Res Non-Dom (Resident Non-Domiciled) in the UK, if a distribution is made to them from a trust in New Zealand and those funds are taken into the UK, then those amounts will be taxable to them in the UK at their marginal income tax rates. This effectively means that the distributions are taxed again.

This makes getting funds to Johnny and/or Mary very difficult in the UK. In some cases, the thought is to have the trust distribute to Mum and Dad in New Zealand, and then them gift the funds on to Johnny and/or Mary in the UK. The problem with this is that the UK is a bit smarter than that and their revenue authorities have developed an avoidance rule which sees the amounts gifted to Johnny and/or Mary in the UK being taxable, if they can be traced back to funds that came from the trust. It is actually more complicated than that because it also looks at the income of the trust going forward after the gifts have been made.

What if the Trust loans the funds?

A similar problem arises with loans. Unless interest is charged on these, often the foreign country will impute a taxable gain or advantage to a beneficiary in that country equal to the interest not charged in the base currency.

The moral of the story is to understand the country that beneficiaries are moving to before they go there. Is it appropriate to make a capital distribution to a beneficiary while they are still tax resident in New Zealand in case they don’t come back from overseas or want funds while they are in the foreign country. Children who are beneficiaries may also move from one country to another and that is also something that needs to be considered.

What about Australia?

A similar example exists when beneficiaries move to Australia. If they enter Australia on a New Zealand passport, and both them and any spouse or partner do not take out permanent residence or citizenship for immigration purposes in Australia, then they are referred to as a foreign temporary migrant or a special category visa holder (the more derogatory term these days is a 501 visa holder for those that get deported back to New Zealand). In these circumstances, as an SCV holder, these Kiwis are not taxed on their foreign sourced income other than foreign employment income, even if the funds are taken into Australia. Thus, they can receive distributions from a New Zealand trust, and they won’t be taxable as long as they remain an SCV holder.

With the recent discussions between Australia and New Zealand about making it easier for Kiwis to get Australian citizenship, trustees will need to be talking to beneficiaries who are in Australia to make sure that they don’t go and obtain their Australian citizenship, as it may detrimentally affect the ability to get the money in the future.

We have been recently working on several jobs for clients around these circumstances, with children based in a wide range of foreign countries. Each one took some planning and each one could have been handled better had advice been taken earlier. In only one case were we contacted before the settlor of a trust was about to die. In every other case, we were usually dealing with trusts where the settlors had died or the ability to get income to beneficiaries in foreign countries was severely compromised because advice was not taken before the beneficiary had gone to that country.

What Should You Do?

We recommend that you consider where the beneficiaries of your trust are residing? If they are in New Zealand today great, but are they looking to move overseas in the future? You should consider where the beneficiaries are likely to end up against the likely timetable to want to distribute funds to assist them in the future. Naturally we are able to assist with this, but it is something that takes careful planning and management as time goes forward.

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