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# International Tax: Taxation of Individuals in Australia

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# Overview

1. The significance of tax residency
2. The legislation - how does Australian law determine who is a tax resident of Australia?
3. The *Harding* Full Federal Court decision
4. The impact of a Double Tax Agreement
5. Current reform – Board of Tax
6. Pros and Cons of being an Australian tax resident
7. Useful tools and ATO guidance material





# The significance of tax residency

1. “Residency” and “Source” are the key themes which determine a country’s right to tax a certain item of income.
  - If you are a tax resident of Australia, you are taxable on income derived from **all** sources, whether in or outside of Australia.
  - If you **are not** a tax resident of Australia (i.e. a foreign resident), you are **only** taxable on income sourced in Australia.
2. Residency for tax purposes is different from residency for immigration purposes. That is, nationality ≠ tax residency
3. Don’t forget any relevant Double Tax Agreements.
4. Temporary Residents and “working holiday makers” (i.e. backpackers).
5. Tests are different for companies – here the focus is on individuals.



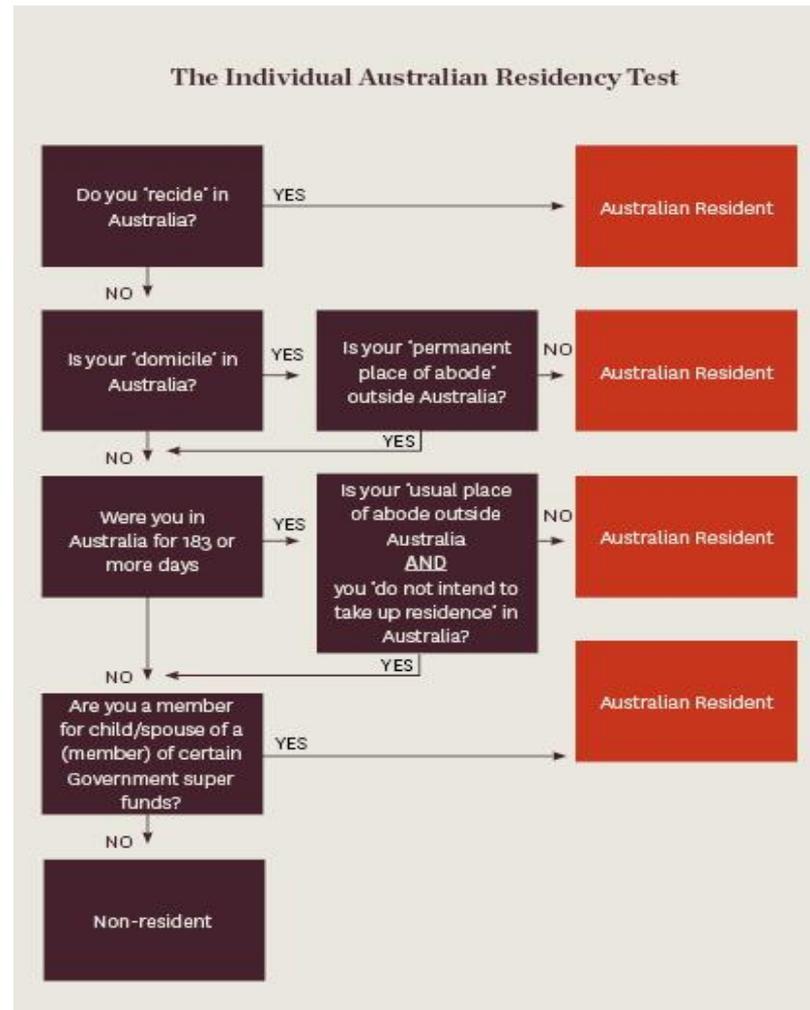
# The legislation – Section 6 ITAA 36

**"resident or resident of Australia"** means:

- (a) a person, other than a company, who resides in Australia and includes a person:
  - (i) whose domicile is in Australia, unless the Commissioner is satisfied that the person's permanent place of abode is outside Australia;
  - (ii) who has actually been in Australia, continuously or intermittently, during more than one-half of the year of income, unless the Commissioner is satisfied that the person's usual place of abode is outside Australia and that the person does not intend to take up residence in Australia; or
  - (iii) who is:
    - (A) a member of the superannuation scheme established by deed under the Superannuation Act 1990 ; or
    - (B) an eligible employee for the purposes of the Superannuation Act 1976; or
    - (C) the spouse, or a child under 16, of a person covered by sub subparagraph (A) or (B); and



# Individual tax residency tests





# Test 1: Ordinary concepts - do you reside in Australia?

1. A question of fact and degree.
2. “Resides” is not defined and takes its ordinary meaning - “to dwell permanently or for a considerable time, to have one’s settled or usual abode, to live, in, or at a particular place.”
3. Tax Ruling TR 98/17:

*The period of physical presence or length of time in Australia is not, by itself, decisive when determining whether an individual resides here. However, an individual's behaviour over the time spent in Australia may reflect a degree of continuity, routine or habit that is consistent with residing here.*

5. Relevant factors:
  - Intention or purpose of presence
  - Family and business/employment ties
  - Maintenance and location of assets; and
  - Social and living arrangements





# Test 2: Domicile and Permanent Place of Abode

***...whose domicile is in Australia, unless the Commissioner is satisfied that the person's permanent place of abode is outside Australia***

1. “Domicile” –the country in which the taxpayer intends to make his or her home indefinitely.
2. Tax Ruling IT 2650 (*under review*)- whether individuals who leave Australia temporarily to live overseas cease to be Australian residents for income tax purposes during their overseas stay.
3. Relevant factors for “permanent place of abode” (paragraph 23):
  - the intended and actual length of the taxpayer's stay in the overseas country;
  - whether the taxpayer intended to stay in the overseas country only temporarily and then to move on to another country or to return to Australia at some definite point in time;
  - whether the taxpayer has established a home (in the sense of dwelling place; a house or other shelter that is the fixed residence of a person, a family, or a household), outside Australia;
  - whether any residence or place of abode exists in Australia or has been abandoned because of the overseas absence;
  - the durability of association that the person has with a particular place in Australia, i.e. maintaining bank accounts in Australia, informing government departments such as the Department of Social Security that he or she is leaving permanently, place of education of the taxpayer's children, family ties and so on...
4. 2 year “rule of thumb” - a period of about 2 years or more is generally regarded as a substantial period for the purposes of a taxpayer's stay in another country. However....the duration of the taxpayer's actual or intended stay out of Australia is not,of itself, conclusive...



# Test 3: 183 days test

***Who has actually been in Australia, continuously or intermittently, during more than one-half of the year of income, unless the Commissioner is satisfied that the person's usual place of abode is outside Australia and that the person does not intend to take up residence in Australia;***

1. Constructive residence

*This test is necessary in order to obviate the great difficulties which occasionally arise in establishing to the satisfaction of a Court that a person is resident in any particular country.*

2. Refers to income year, not calendar year.

3. Does not need to be a continuous period.

4. Just because you are Australian tax resident for at least 183 days doesn't automatically mean you are an Australian tax resident for the full income year.

5. Full Federal Court - *Addy* [2020] FCAFC 135 (could be appealed!)

6. AAT - *Subrahmanyam* 2002 ATC 4001





# Test 4: Commonwealth Super test

***...a member of the superannuation scheme established by deed under the Superannuation Act 1990, or an eligible employee for the purposes of the Superannuation Act 1976, or the spouse, or a child under 16, of a person covered above,***

1. Applies to Commonwealth public servants and their spouses/children under 16.



# *Harding v Commissioner of Taxation* [2019] FCFCA 29

## Facts

- Mr and Mrs Harding were Australian citizens. In 2006, Mr Harding worked in Australia but took up an offer to work in Saudi Arabia in February 2009.
- The Hardings' agreed that that Mr Harding would live in Bahrain and commute each day to Saudi Arabia and that Mrs Harding would join Mr Harding with their youngest son toward the end of 2011.
- When Mr Harding left Australia in March 2009 he took his personal possessions, and those he did not take he sold or left for his sons.
- Upon his return to the Middle East, Mr Harding started making plans to relocate his wife and youngest son to Bahrain. Mrs Harding and the children visited Mr Harding and they looked for appropriate accommodation.
- Mr Harding returned to Australia regularly each year to visit his family. In the 2011 income year he spent 91 days in Australia and stayed in the family home.
- From 2011, Mrs Harding indicated her reluctance to return to the Middle East. Mr Harding was not prepared to alter his plans and the pursuit of his employment opportunities in the Middle East. The first instance judge accepted that the purposes of Mr Harding's extended visits in the 2011 income year were to see his family and to encourage Mrs Harding to come to Bahrain.
- Mr and Mrs Harding separated around October 2011 and ultimately divorced.
- In Bahrain, Mr Harding leased and lived in an apartment building and moved between fully furnished apartments within that same building. He initially took a two bedroom apartment and then moved to a one bedroom apartment in June 2011 when he knew his family would not be joining him.
- In 2014, Mr Harding committed to moving to Oman for work. His relationship at the time ended as his then partner was reluctant to move to Oman.
- Mr Harding subsequently met and married another person and they commenced living together in Oman.



# *Harding v Commissioner of Taxation [2019] FCFCA 29*

## Issues

- Was Mr Harding a tax resident of Australia for the 2011 income year under the ordinary concepts test OR the domicile test?

## History

- The Court at first instance found that Mr Harding was not a resident under the ordinary concepts test **but** was a resident under the domicile test;
  - He did not have a permanent place of abode outside Australia in the sense required under the domicile test.
  - The apartment complex was a type of premises used for temporary accommodation.
- Mr Harding appealed.



# *Harding v Commissioner of Taxation* [2019] FCFCA 29

Did Mr Harding reside in Australia under ordinary concepts?

- No.
- Mr Harding held a strong and fixed intent to resume his previous lifestyle in the Middle East irrespective of whether his family ultimately joined him there.
- The objective circumstances surrounding Mr Harding's departure were consistent with this intent and that his conduct prior to and after the 2011 income year were also consistent with that intent.
- The maintenance of a house in Australia where a spouse and children lived and the maintenance of a house as a family home would usually be important indicators of residency. However, in the 'unusual' circumstances of this case, those factors assumed less significance and concluded that the nature and quality of Mr Harding's continued presence in Australia was not consistent with residing in Australia.
- Mr Harding's connections with Australia either supported the finding that Mr Harding was not a resident, or were insufficient to overcome the significance of Mr Harding's intention to leave indefinitely.



# *Harding v Commissioner of Taxation* [2019] FCFCA 29

Was Mr Harding's permanent place of abode outside of Australia?

- Yes.
- His permanent place of abode in the 2011 income year was Bahrain. That was the “place” where he was living. The fact that he was living in 2011 in a serviced apartment as distinct from permanent lodging was not determinative of his liability to pay tax in Australia.
- Although his family remained in Australia and he visited them, the quality and nature of those visits supported the conclusion that Mr Harding had abandoned his residence in Australia.
- The phrase “place of abode” was not a reference only to a person’s specific house or flat or other dwelling. The word “place” in the context of the phrase “outside Australia” invited a consideration of the town or country in which a person was physically residing “permanently”.
- So long as the taxpayer had “definitely abandoned” his or her residence in Australia, it did not...require that the taxpayer be permanently located at a particular house or flat in a particular town within a foreign country.



# Tax Treaties and Dual Residence

1. Double Tax Agreements: Bilateral agreements that define taxing rights.
2. Applies to people who are “residents” according to the treaty (which in turn is generally linked to the domestic law definition).
3. What happens if a person resident of both countries? Tie Breaker rules kick in.
4. Article 4 “tie breaker” in Australia/UK DTA determines residence solely based on:
  - the state where the individual has a permanent home (if permanent home in both states, or neither, the state with which the personal and economic relations (PER) are closer)
  - if PER cannot be determined, the state in which the individual is a national;
  - if a national of both (or neither), the Competent Authorities decide
5. Foreign Income Tax Credits – Double tax relief under Division 770 ITAA 97.



# Summary of the Tests

- Facts Facts Facts!
- Start with the tax treaty (if there is one!)
- Then move to the ordinary concepts test, and work your way down.
- Possible to be a resident for only part of the year, not the whole year.
- Intention and behavior are the key factors . Generally objectively determined.
- See ATO Decision Impact Statement of *Harding*. - [https://www.ato.gov.au/law/view/pdf/dis/dis\\_harding.pdf](https://www.ato.gov.au/law/view/pdf/dis/dis_harding.pdf)



# Board of Tax review

1. Self initiated review in 2016 by the Board of Taxation (a non-statutory body, comprised of industry experts, who provide advice to Government) – see [link](#)
2. Final report in March 2019 – “Reforming Individual Tax Residency Rules – A Model for Modernisation - Final Report” – see [link](#)
3. Proposal:
  - a primary ‘days count’ bright line test that automatically determines the residency status of most individuals; and
  - a secondary test taking into account individual circumstances, which leverages some existing case law, as well as international practices.
4. Work in progress but watch this space! Further consultation is occurring but the government yet to make a final decision.



# Do I want to be an Australian tax resident?

## Benefits of being an Australian tax resident

- Tax free threshold. First \$18,200 tax free.
- Availability of franking credit offset on franked dividends.
- CGT main residence exemption.
- CGT 50% discount on assets held for more than 12 months.

## Benefits of being a foreign resident

- Lower tax rate (5 – 30%) applies to interest, royalties, and unfranked dividends (withholding taxes)
- For CGT, only taxed on “Taxable Australian Property.” (e.g. Australian land)
- No Medicare Levy.



# How to assist clients to determine their tax residency status

1. Refer to the legislation and ATO public guidance – TR 98/17 and IT 2650 (although being reviewed following *Harding*).
2. Consider using the ATO website tool - <https://www.ato.gov.au/Calculators-and-tools/Work-out-your-tax-residency/>
3. Look at the ATO Private Ruling database for similar fact scenarios (but only binding on the applicant!)
4. Consider early engagement and discussion with the ATO – see [link](#).
5. Make a complex issue resolution enquiry (need a tax agent/lawyer) or a private ruling with the ATO (need evidence) – can take 3 months.
6. If going through the objection or litigation process, the burden of proof is on taxpayers. Have evidence to substantiate your contentions!