# Tax Residency: A Practical Guide
# 25/10/2023

Alison Wood:

Hi, everyone. I'm Alison Wood from CCH Learning Wolters Kluwer and I'll be your moderator for today. Welcome to this webinar, which is Tax Residency: A Practical Guide. Just a few quick pointers before we get started. In the handout section, you'll find the PowerPoint for today's webinar. And if you're having any sound problems, you can toggle between audio and phone. And shortly after the session today, you'll receive an email letting you know your recording is ready to be viewed. You can ask questions at any point during the session today, simply type in the questions box. I'll collate those questions and ask them at the Q&A towards the end of today's presentation. CCH Learning also offers a subscription service, which many people have termed Netflix for professionals. It provides members with access to our entire library of recordings as well as live webinars for a very competitive flat fee.

That's for over 500 hours of content. And for CPD purposes, your viewing is logged automatically. Your presenter today is Mark Chapman, who is the Director of Tax Communications for H&R Block Australia. Mark has over 25 years experience as a tax professional in both the UK and Australia specialising in tax for small businesses and individuals. He is a member of the Institute of Chartered Accountants in England and Wales, the Chartered Institute of Taxation, and is a fellow of CPA Australia. He also holds a master's of taxation law with the University of New South Wales. So without any further ado, I'll now pass you over to Mark to commence today's presentation.

Mark Chapman:

Thanks, Alison, and good afternoon, everybody. Thanks for taking the time to come along to today's session. So basically, as Alison said, if you've got any questions surrounding this topic, do please feel free to put them in the chat box. I'll deal with them at the end. Well, hopefully, I'll deal with them at the end. If I don't get the chance to deal with your question or if you've got any questions which come to you afterwards, my email details are also on the final slide and you can contact me out of the session and I'll deal with your queries then. So basically today I'm going to be dealing with all aspects of tax residency, residents, non-residents, temporary residents, working holiday makers, et cetera. We're going to try to cover basically all of it in the course of one hour. So the question arises, why does it actually matter what your residency status actually is?

Well, it matters because the law treats residents and non-residents very differently. Residents, for example, are taxed on all of their worldwide income. If you're a resident, you're taxed on overseas income as well as Australian income, whereas non-residents are only taxed on their Australian sourced income. The tax rates are different for residents and non-residents. So for example, non-residents don't get the tax-free threshold, that's the $18,200, and non-residents do pay tax at 32.5% from the first dollar of income right the way up to $120,000. So it is considerably more expensive if you like to be a non-resident. On the other hand, residents pay the Medicare levy. Non-residents typically don't. Non-residents pay withholding tax on their bank interest at a flat rate of only 10%. And non-residents are generally not liable to Australian CGT except in relation to taxable Australian property, which is basically often real properties, so land, buildings, et cetera. So shares and other investments aren't going to be subject to CGT if you're a non-resident.

So you can see that it is important to get this judgement right. How do we determine if somebody is resident or not? Well, we determine it, first of all, by looking at the resides test. That's in Section 6(1) of the 1936 Act. Unfortunately, there isn't definition of resides within the legislation, so therefore we've got to look at the sort of standard dictionary definition if you like, which is to dwell permanently or for a considerable period of time to have unsettled or usual bode to live in or at a particular place. That's the definition from the shorter Oxford Dictionary. So therefore, we've got to try to establish whether our taxpayer actually meets that definition in terms of their instance in Australia.

The tax office does give us a certain amount of guidance as to how the resides test will actually be implemented. A new ruling came out last year, Taxation Ruling TR 2023/1. There isn't really anything particularly earth-shattering in that ruling. It's simply a restatement of an earlier ruling, and nevertheless, that is the place to look for all things at residency. So for example, we've got to take into account the period of physical presence in Australia, the intention or the purpose of that presence, we've got to look at the taxpayer's behaviour whilst in Australia. We've got to look at their family, their business, their employment ties. Are those ties actually with Australia or are they with another country? We look at the maintenance and location of their assets, their social and living arrangements. No one factor is determinative, but looking at the overall picture, we can come to a conclusion as to whether somebody is actually resident in Australia or alternatively somewhere else.

Now, if a taxpayer passes the reside test, then they're resident and we don't need to go on and consider the other tests. If a taxpayer fails the resides test, we then need to consider the other three tests, which are on the next slide, which I'll talk about in a moment. And basically if any one of those tests is passed, then the taxpayer is resident. Now, the three tests are on the set out on the slide here. I won't spend too long talking about the superannuation test, which is typically only going to be relevant to current public servants. However, the other two tests could well be relevant. First of all, we've got the domicile test which says that the person is resident in Australia if his or her domicile is in Australia, unless the commissioner is satisfied that the person's permanent place of abode is outside Australia. So we've got to look for example at the place which is considered to be your permanent home. So it's quite a slippery concept, domicile, it's something more than the place where you actually reside and it's a place where you consider yourself to belong.

There are three types of domicile. There's the domicile of origin, domicile of choice, and domicile by law. Now, I won't talk too much about domicile by law because it very rarely is invoked. However, your domicile of origin is basically the place where you are born. However, it is possible to replace that with a domicile of choice. So I'm from the UK originally, so my domicile of origin, which is the UK. However, I came to Australia in 2007. I settled here permanently. I regarded as my home and therefore my domicile by choice is actually Australia. The other test which we need to consider is the 183-day test. So to be resident, you need to be physically present in Australia for more than 183 days in a year. Now, they don't need to be continuous. That doesn't need to be 183 continuous days, you can come and go, but nevertheless, you do need to be here for more than a 183 days in a year. Again, that test does not apply if your usual place of abode is outside Australia.

Now, the ATO has produced a bit of a table which highlights some common situations and they've given us their view as to whether that taxpayer is actually resident or foreign resident that's reproduced here. So we've got an overseas student enrolled in a course of more than six months duration at an Australian institution. Well, in that instance, you're generally speaking Australian resident. What if you're visiting Australia and you're working and living in one place and have taken steps to make Australia your home? Again, you're typically Australian resident. If you're visiting Australia and you're travelling and working in various places, the ATO says that you'll typically be regarded as foreign resident, possibly indeed as a working holiday maker.

If you're holidaying in Australia or you're here for less than six months, you're typically foreign resident. And if you are migrating to Australia, intend to live here permanently, then you're generally speaking Australian resident. Now, let's apply these principles to an example. So we've got Adam who was born in Australia, works as an airline

pilot, owns a house in Sydney with an Australian bank account, private health cover under the Australian dividends. Now, he works in Dubai from the 1st of November 2021 to the 1st of April 2022 and he lives in a lease apartment for that time. However, his salary is actually paid into his Australian bank account and he spends December in Australia visiting family who remained in Australia. Now, later on, he accepts an offer to relocate to Dubai and flies there on the 1st of July 2022 for an indefinite period.

He opens a joint bank account in Dubai. He purchases an apartment there. His wife joins him in Dubai. However, his kids actually do stay in Australia and he retains his Australian house, which he rents out. He retains his private health cover and his local bank account and he takes six weeks leave in Australia over the Christmas period to visit his children. So there are two questions, in relation to 2021, '22, is Adam going to be resident or non-resident? And in relation to the following year, 2022, '23, we've got the same question, is he resident or non-resident? Well, in relation to 2021, '22, we can probably say that Adam is actually still Australian resident.

We say that because he passes the resides in Australia test, which is the common law test, the primary test we talked about a few minutes ago. So for example, he maintains his family here, his home and his financial ties are here. He visits Australia to stay with his family who are here and he doesn't have a permanent place for abode outside Australia. Now, on that basis, he's resident in Australia. However, I've also considered the other two tests purely as a sort of academic exercise. And indeed he also is domiciled in Australia because he hasn't established a domicile of choice in Dubai. And in addition, he passes the 183-day test because he's physically present in Australia for seven months and away for five months.

Now, roll forward on tax year, and looking at the facts, we suddenly come to a slightly different conclusion. So in 2022, '23, Adam is no longer Australian resident. He doesn't pass the resides in Australia, the common law, the primary test, he's overseas employment is for indefinite period. He's purchased an apartment in Dubai, he's established a bank account in Dubai. His wife has relocated with him and therefore his permanent place of abode is in Dubai. Now, there are still factors which indicate residency in Australia. So he still owns his family home, his children are still here, et cetera, but they're now outweighed by other factors and those other factors tell us that he's no longer Australian resident.

So in terms of new migrants, do we have an action plan? Well, yes, we do. New migrants basically need to undertake a number of steps. First of all, they need to get a tax file number. You can only apply for that once you've arrived in Australia, but that's pretty much the first thing that you need to do to get into the Australian tax system. They need to get a market valuation of any assets that could be subject to CGT such as property shares or business interests which the taxpayer actually owns on the date of entry to Australia. We'll talk about that in more detail in a few slides time. They need to get an ABN if there's an intention to start a business, they need to choose and sign up with a superannuation fund. They need to lodge their first tax return for the period from the date of arrival through to the following 30th of June.

And just bear in mind that if they're coming to Australia permanently, the taxpayer will be resident from the date of arrival and they'll therefore be entitled to a partial tax-free threshold depending on when in the year that date of arrival actually is. Now, the $18,200 tax-free threshold consists of two elements. So there's a flat element of 13,464 and that is paid in full irrespective of when you actually arrive, but there's then an additional 4,736, $4,736, which is apportioned for the number of months that the taxpayer was in Australia during the income year including the month of arrival.

So our migrants must disclose all of their worldwide income earned from the date of arrival. So that is interest on overseas bank accounts, foreign pensions, rent from investment properties, disposals of foreign assets, shares or proceeds from employee share schemes or wages and salaries. That includes all of those and they do need to disclose them provided that they're actually resident from the date of arrival. Now, there might well be some tax

which is payable in their home country as well. However, to avoid double taxation, they can potentially claim a foreign tax offset in Australia in relation to that foreign tax which they have already paid.

Just bear in mind that money or cash, which is actually brought into Australia with the taxpayer when they first arrive isn't taxable. That includes physical cash that actually bring with them, but also oversee savings, profits, massive disposals, et cetera, which they may not have brought across, that is not taxable. I'll just talk at this point about taxable Australian property, which is a concept we're going to talk about in quite a bit of detail as we get into the CGT side of residency because foreign residents are only subject to capital gains tax in relation to taxable Australian property. Now, there are five categories of taxable Australian property. First of all, there's what's called taxable Australian real property and that basically means real property, which is situated in Australia, for example, land, buildings. It also covers mining, quarrying, prospecting rights to minerals, petroleum or quarry materials situated in Australia.

The second category of TAP is an indirect interest in Australian real property. We'll talk about that in more detail on the next slide. The third category is a business asset of permanent establishment in Australia. So if for example, our foreign resident disposes of a business or an asset of a business, that will be subject to Australian CGT provided that business had a permanent establishment here. The fourth category is an option or a right to acquire any of the CGT assets, which I've just talked about. And the fifth category of TAP is a CGT asset where a taxpayer makes an election on the Section 104-165. That election is only made on ceasing to be an Australian resident and we'll talk again about that in more detail in a few slides time.

Now, I mentioned that the second category of taxable Australian property is an indirect Australian real property interest. So what's that? Well, an indirect Australian real property interest is where a foreign resident has a membership interest in an entity and that interest passes both of the following tests. First of all, there's a non-portfolio interest test and secondly there's a principal asset test. Now, the non-portfolio interest test refers to the direct interests held by the foreign resident, its associates are 10% or more of the entity and the principal assets test is basically whereby the entity has an interest based on market value, which is more TARP assets than not TARP assets. Now, how will that actually apply in practise? Well, a typical example would be a company or a unit trust in which a foreign resident and his or her associates where they own more than 10% and whose assets consist of at least 50% Australian land and buildings.

And it's worth pointing out incidentally that the definition of taxable Australian property does not include Australian listed company shares. So they're not TAP. So Australian private company shares typically are TAP, but listed company shares are not. So arriving residents do need to be aware of capital gains tax. So CGT assets are deemed to actually be acquired on the date that the taxpayer becomes resident in Australia, which could well be but isn't necessarily depending on what kind of visa they actually come in on the date of arrival. Therefore, the taxpayer will need to get a market valuation of any assets that could be subject to CGT such as property, shares, business interests, personal items like jewellery which were owned on the date of entry to Australia.

However, if the asset is already TAP such as real estate located in Australia, obviously it's already within the Australian tax system, an evaluation is required. So therefore, we're typically talking about overseas property, overseas business interests, et cetera. Now, from that point on, normal CGT rules apply, if they later on dispose of the asset, obviously the capital gain is equal to the difference between sale proceeds and base cost, which is typically going to be that market valuation which they had done when they first arrived. Just bear in mind that in order to get the 50% discount, they do need to hold on to assets for 12 months from the date of becoming resident.

Now, here's an example which illustrates that the client purchased a family home in England in 2010 for around £500,000. So they immediately moved into the house and lived there until they left for Australia. Now, they left England to live permanently over here in 2013, and they were on initially a temporary resident visa. So they

renovated the house and during the period of renovations, the house actually sat vacant. So the renovations cost around £100,000. In July 2014, they rented the house out for about six months and then their in-laws moved into the house and are still in the house now. They became Australian residents for tax purposes in April 2016, which was the date that they moved onto a permanent residency visa and they purchased a main residence here in Australia on the 12th of March 2014. So they wish to sell the UK house for around £750,000.

So the question is, what are the tax implications of the sale of the UK house? Well, the UK house would be deemed acquired for Australian tax purposes at the date on which they became permanent resident in April 2016, not the date on which they first arrived because they came on a temporary visa and it would be deemed acquired in April 2016 for its market value at that date, and therefore, they'll need to get a market valuation of the property at that date in order to find out what the base cost actually is. Now, everything prior to April 2016 is basically irrelevant because the asset wasn't inside the Australian tax net until that date. So the capital gain with a difference between sale proceeds and market value at April 2016, there won't be any main residence exception because they'd already acquired another main residence actually in Australia in 2014 before becoming full tax residents.

However, it is worth noting it's not relevant to this particular example, but it could well be relevant in other examples that both the six-year abstinence rule and the main residence exemption can in theory apply to an overseas property sold after you become resident. So you need to take a look at TD 95/7 and ATO ID 2010/101 to see more detail about that. So we've basically covered the situation of becoming a resident. So let's flip the coin, let's look at the other side of the equation and look at the tax implications of becoming non-resident. And it's worthwhile taking a look at a particular quote which is very relevant in this context. It's easier to convince the ATO that you've been dead for a year and then miraculous to come back to life than to convince them that you've ceased to be tax resident for that period.

And that simply highlights the difficulty of actually persuading the ATO. You have actually become non-resident, particularly for a short period of time, because obviously the ATO prefers it if you're a resident because they can tax your entire worldwide income. With non-residents, they're only taxed on their Australian source income, which means that the ATO typically will lose out. Having said that, there are different tax rates as we talked about at the very beginning of this presentation. So in a common situation whereby you leave Australia and don't set up a permanent home in another country, you'll still probably be Australian resident. However, if you leave Australia permanently, then you'll be foreign resident from the date of departure.

Now, in order to determine whether you are, whether the client is non-resident or not, we need to consider basically the same list of factors that we took into account to determine whether you are a resident. So we need to look at TR 2023/1 and we need to consider factors such as whether the taxpayer intends to return permanently to Australia. We need to look at the roots that they put down in the new country such as buying a house or marrying, the duration of frequency of their visits to Australia, the continuing family connections to Australia. So for example, is their spouse still here? Are their children still here? And the continuing financial, social and emotional ties to Australia, is the family home still here? The car, the salary, is it paid into an Australian bank account? All of these factors need to be considered in determining whether a taxpayer is non-resident or indeed resident.

Now, a recent tax case has shed some light on what a taxpayer has to do in order to be regarded as non-resident. So the case is the Harding case, which dealt with an Australian who moved to Bahrain. He then stayed there for several years, albeit that he actually moved between several different rented apartments. Now, the commissioner argued that the taxpayer hadn't established a permanent place of abode in Bahrain because he hadn't actually settled in one particular apartment, and on that basis, the taxpayer was still domiciled in Australia and therefore he was still tax resident here. Mr. Harding obviously disagreed with that interpretation. Ultimately the case was appealed all the way to the full federal court which held that Mr. Harding was not a tax resident as

he was no longer domiciled in Australia. What the court found was that the reference to place, in the permanent place of abode test wasn't a reference to a person's specific dwelling, but could instead be the town or country in which a person is permanently residing.

So the full court found that if a person has abandoned their residence in Australia, there should be no distinction between someone who, for example, buys an apartment overseas and someone who simply lives in a series of temporary flats in the same country as indeed to Mr. Harding. Therefore, even though Mr. Harding's specific type of accommodation in Bahrain was temporary or transitory, the full court concluded that his place of abode was indeed in Bahrain. Now, the implications of that where really there are several that we need to flag. So first of all, most Australian expats who move overseas will be deemed as residing in Australia and hence will remain fully taxable in Australia unless they can show that they've established a permanent place of abode overseas.

However, temporary accommodation does not prevent a taxpayer from having a permanent place of abode overseas. So basically the place of abode can be a town or a country rather than a specific dwelling. So if an Australian who's living or working overseas can establish that particular town or country outside of Australia is their permanent place of abode, it can therefore be easier for them to establish that they're not a resident of Australia for tax purposes. So we've looked at CGT for arriving residents, CGT for departing residents is what I'll consider next, and basically departing residents CGT event I1 happens. So all their CGT assets except taxable Australian properties such as Australian London buildings are basically deemed to be disposed of at market value at the date on which they leave Australia and therefore capital gain happens which they can actually elect to disregard.

And so that's the election, it's Section 104-165, that's the fifth category of TAP, which I talked about on the TAP slide a few minutes ago. So if they elect to disregard that deemed disposal, then obviously no deemed disposal happens and the assets remain within the Australian tax net. The assets are all regarded as TAP and it's fully subject to Australian tax. Now, the election is an all or nothing event, so either all your CGT assets must be included or none of them, and the way that the tax return for the period of departure is completed is actually then evidence of whether or not the election is made. Now, whether or not you choose to make that election depends on a number of factors. So there can be obviously advantages in choosing that deemed disposal if the value of assets is expected to increase in the future because the increase will be outside the Australian tax net.

But obviously there's a serious disadvantage in terms of cashflow because you trigger a capital gain without actually having physically disposed of the asset and therefore you may not have any cash in which to pay the capital gain. You'd also need to think about the impact of non-residents on the CGT discount. So if you elect to disregard that deemed disposal, then when you ultimately dispose of the assets, all of the gain will be subject to Australian taxation, but you won't actually get the capital gains tax discount in relation to your period of non-residents, that can make it quite an expensive exercise. So you've got to really weigh up those factors in working out whether to actually disregard that deemed disposal.

If we roll the story forward and then the taxpayer ultimately comes back to Australia, well, what happens then? Well, if no election was made to defer the disposal, then assets will be deemed to have been acquired at the date of becoming resident. Just the normal rule for somebody who's coming into Australia and therefore any increase in value whilst the taxpayer was overseas will escape Australian tax when the asset is ultimately disposed of. Just bear in mind that the family home is obviously TAP and therefore it isn't subject to the deemed disposal rules. So all of this is not really relevant to the family home, for example. If an election was made to defer disposal, then the assets never ceased to be TAP and so returning to Australia has no impact.

Now, there are a number of special rules which apply to non-residents, particularly with regard to CGT. With CGT over the last 10 years or so, there have been a series of moves to stop non-residents from applying the various exemptions and concessions which are typically available to Australian residents. So really the first move in this

long story was the removal of the CGT discount back in 2012. So the 50% CGT discount allows for gains made by individuals is reduced for any periods in which the taxpayer has been a foreign resident during the period of ownership. Therefore, if the taxpayer becomes non-resident, in effect the CGT discount ceases to be available. In 2017, there was another change, foreign resident CGT withholding. So from the 1st of July 2017, the CGT withholding rate for foreign tax residents of 12.5% payable on disposal of Australian property with a market value of $750,000 or more.

$750,000 in real estate terms these days is nothing and therefore most disposals will be caught by the foreign resident CGT withholding rules. It applies in relation to contracts entered into on or after the 1st of July 2017. And most recently, the government has basically blocked access to the CGT main residence exemption. So for the 9th of May 2017, foreign tax residents can't access the CGT main residence exemption but there are some exceptions to that which are on the next slide. Now, this new legislation applies to all foreign residents, and therefore it will also apply to Australian citizens or permanent residents who dispose of their Australian main residence whilst a foreign resident. So for example, somebody who goes overseas on secondment is overseas for potentially many years, they lose their Australian tax residence and they dispose of their property whilst they're overseas. They won't be entitled to claim the main residence exemption even though most or all of the gain might actually have arisen while they were actually resident.

So there aren't any partial exemptions. So the determining factor is the residency status of the taxpayer at the time of the CGT event i.e. when the contract for sale is signed. So if you are not resident at the time the contract for sale is signed, then you simply don't qualify for the main residence exemption at all. If on the other hand you are resident, then you do qualify for the main residence exemption as usual. So if you're an Australian citizen and a permanent resident who could be a foreign resident for a period of time, they actually can still claim the CGT main residence exemption if they come back to Australia and dispose of their main residence after they've reestablished Australian tax residency. Now, the exceptions to this rule is where a life event occurs and basically the taxpayer satisfies the life events test if they've been a foreign resident for six years or less and they meet one of these three criteria.

So the first criteria is that the taxpayer or the taxpayer spouse or child under 18 years has had a terminal medical condition during that period of foreign residency. The second criteria is that the death of either the taxpayer spouse or child under 18 years during that period of foreign residency. And the third criteria is where the CGT event happens because of the taxpayer's divorce or separation. So pulling all of that together, basically the effect of these rules is that for Australians going overseas who sell their main residence exemption at a time at which they're a foreign resident, the main residence exemption will not be available at all. So there's no partial exemption, as I said, it won't be available at all either where a life event does not occur or after six continuous years as a non-resident, even where a life event occurs.

And obviously that means that foreign residents won't benefit from the absence rule because that's part of the main residence exemption if the property is sold when they're a foreign resident. So a quick example, Vicki acquired a dwelling on the 10th of September 2010, moving into it and establishing it as a main residence. On the 1st of July 2018, Vicki vacated the dwelling and moved to New York. On the 15th of October 2020, Vicki signs a contract to sell the dwelling. As Vicki is a foreign resident on the 15th of October 2020, she's not entitled to the main residence exemption at all. So the period from 10th of September 2010 to the 1st of July 2018 is quite simply overlooked, but because the fact that she's a foreign resident on the date of sale means that she won't be entitled to the main residence exemption at all.

In relation to deceased estate, there's a similar rule which applies to the trustee or the beneficiary of a deceased estate who will be denied the main residence exemption in two circumstances. The first one applies to the deceased ownership period. So if the deceased had been a foreign tax resident for a continuous period of six years or more immediately before that death and therefore they were excluded foreign resident and the second

one applies to the trustee or the beneficiary's ownership period, if the relevant beneficiary had been a foreign tax resident for a continuous period of six years or more immediately before the CGT event. In either case, the main residence exemption won't be available.

Now, there are also special income tax rules which are going to be applicable to non-residents. For example, if the taxpayer has a HELP or a TSL loan, so a student loan of some type. From the 1st of July 2017, Australians who are now non-resident and who are living overseas who are earning above the minimum repayment threshold must make a loan repayments based on their worldwide income. In terms of investment income, there's a withholding tax regime which applies to non-residents whereby the payer must deduct withholding tax in relation to bank interest unfranked dividends and royalties, the rate is currently 10% for bank interest. It's between 15 and 30% for unfranked dividends, depending on whether there's a DTA and it's up to 30% for royalties. Again, depending on whether there's a DTA, that withholding tax is a final tax. After that, the income is exempt and doesn't need to be included in the tax return of the non-resident.

If the payee, the recipient hasn't given an overseas address, the payer must actually withhold tax at 47%. So that's quite a punitive outcome. And just bear in mind that the withholding tax only applies to unfranked dividends. Franked dividends on the other hand are not accessible at all and therefore they don't need to be included in the recipient's tax return. However, the imputation credits are also not available. The franked dividends basically already have tax deducted by the company which is paying them and therefore nothing else needs to be included in the recipient's tax return. So I've given you an overview of the situation regarding residents and non-residents. There's a third category that we do need to consider, however, which is a temporary resident. Now, you're a temporary resident if you hold a temporary visa under the Migration Act 1958 for example, a 457 working visa and if you and your spouse are not an Australian resident within the meaning of the Social Security Act 1991.

In other words, that applies to individuals who reside in Australia and are an Australian citizen, holder for permanent visa, or a protected special category visa holder. So in other words, if you are not any of those things, you are included. Just bear in mind that even if you've got a temporary visa, if your spouse is an Australian resident within the meaning of the Social Security Act 1991, you're not a temporary resident for tax purposes. So that is just something to be aware of that taxpayers are not automatically regarded as temporary tax residents. It depends pretty much on the status of their spouse. If the spouse is also a temporary resident, then they will qualify. If they're not, then they won't. How are temporary residents actually taxed? Well, temporary residents are taxed only on their Australian sourced income. So employment income, bank interest, dividends, et cetera, and certain short term foreign employment income.

So basically temporary residents are taxed as non-residents if you like. They're not taxed on most foreign income. So overseas bank interests, dividends, rental income and capital gains are not taxed. Basically, temporary residents are completely exempt from Australian CGT except to the extent to which the asset is taxable Australian property. Now, if a temporary resident applies for permanent residency, then the worldwide assets come into the Australian tax net at market value at the date of application and that obviously defers the tax entry point compared to similar permanent migrants. So if you've got two people, they come to Australia on the same day, one of them on a permanent residency visa, one of them on a temporary resident visa. The one on the permanent residency visa is taxed as a permanent resident from the date of arrival. The other one is actually going to be taxed as a full tax resident from the date of which they get permanent residency. So that could well be considerably later.

This is particularly interesting for New Zealand citizens. So when New Zealand citizens enter Australia, they receive what's called a special category visa, which allows them to remain and work in Australia or not reenter if they leave, basically if they do leave, they lose that visa, and if they come back, they can then get another one. Now, the ATO has accepted that this is actually a temporary visa. They did that in TD 2012/18. So temporary visa obviously means that they are taxed in accordance with the rules, which I just outlined on the previous couple of

slides. So when New Zealand citizens entered Australia after the 26th of February 2001, which was the date on which the special category visa was introduced, and they haven't applied for permanent residency or taken Australian citizenship and be treated as temporary residents for tax purposes no matter how long they stay in Australia.

So basically if you're a New Zealand citizen, you can live here for years or potentially even decades and always be regarded as a temporary resident for tax purposes. Now, obviously this means that New Zealanders who qualify for this status aren't taxed on most of their foreign income, including their New Zealand income and are excluded from Australian CGT except to the extent that the asset is TAP. Obviously, this doesn't apply where the New Zealand citizen is married to or in a defacto relationship with an Australian resident. In terms of superannuation, temporary residents who are departing Australia permanently do get a refund of superannuation contributions, which should be paid by their ex employers. That refund is payable after the temporary resident has left the country and it isn't accessible income. The taxpayer does need to apply for it online and the tax rates that apply are basically between zero and 47%.

And finally, the fourth category of residents or non-residents that I want to talk about briefly, working holiday makers. So basically from the 1st of January 2017, if you're a working holiday maker, which is somebody on visa type 417 or 462, you'll be taxed at a rate of 15% on all income from the first dollar up to $45,000. And then for income from $45,000 onwards and normal tax rates apply, so 32% for income up to $120,000. Now, these rates do actually apply regardless of whether the taxpayer satisfies the normal rules for residency. So you can work your way through the tests and you can determine whether the individual is actually resident or not. But in this context, it simply doesn't matter if the employee or if the taxpayer is on a 417 or 462 visa, they're simply treated as working holiday makers automatically.

So if a taxpayer starts a job after the 1st of January 2017, obviously they must advise the employer of their particular visa type so that the employer can then deduct tax at that special 15% rate. So if the employer doesn't register with the ATO in order to do that, the employer must deduct tax at foreign resident rates starting at 32.5% from the first dollar. And working holiday makers basically cease to be taxed at the special rates if they transition to a different visa type. So from the date at which they transition to the different visa type, you apply the residency tests as normal from that point. Now, one particular aspect of the working holiday makers legislation has recently been considered by the courts and that's resulted in a certain carve out of some taxpayers from the working holiday makers tax rate.

The tax case was the Addy case, which was finally decided about two years ago. It concerned a British working holiday maker who argued that although she was a working holiday maker, she was actually resident for tax purposes applying the ordinary resides or abode test and the 15% working holiday maker rate was discriminatory and shouldn't be applied. And she quoted Article 25 of the Australia UK DTA, which she said should apply to British nationals at the same rates that apply to Australian citizens who are tax residents. Now, Article 25 of the DTA of the Australia UK DTA at least is a non-discrimination clause which provides that nationals of, in this case the UK shouldn't be subject to tax in Australia. That's more burdensome than the tax to which Australian nationals in the same circumstances are or may be subjected.

Now, this case was another very complicated type case and it was ultimately appealed through various different levels of the courts all the way to the high court which ultimately found for Miss Addy and therefore what are the indications of that case? Well, your clients are going to be affected by this if they meet certain criteria. So first of all, the client has spent time on a working holiday maker visa, so that's 417 or 462 visa since the 1st of January 2017. And the taxpayer is also tax resident on the normal tests and this is the crucial one. The taxpayer is from a country with which Australia has a DTA containing a non-discrimination article like Article 25. So that is actually a very limited group of countries. It only includes Chile, Finland, Germany, Japan, Norway, Israel, Turkey, and of course United Kingdom.

If the taxpayers from anywhere else forget it, the Addy case is not relevant to them. Now, for clients who do meet these three criteria, the working holiday maker 15% tax rate is discriminatory and can't be applied and therefore the client will be taxed at normal resident rates, meaning that they're also entitled to the $18,200 tax-free threshold. On the other hand and less advantageously, the next $26,800 of their income could well be taxed at 19% rather than the 15% working holiday maker rate. They're also potentially liable to the Medicare levy and they could also be obliged to include their foreign sourced income in the tax return.

Now, clients who don't satisfy the resides test, the abode test under the normal rules are simply not affected by the Addy case. And in addition, any client who comes from any country other than the ones which I just mentioned, the Addy case is not relevant. How does the ATO identify whether the taxpayer is potentially going to be affected by this? Well, they introduced a new box in the working holiday maker label, it's box A4 whereby the taxpayer gives their home country and they also need to tick the residency status at the resident label on the front of the tax return. So those two in conjunction identify possible cases who are going to be affected by Addy. In relation to working holiday makers and superannuation, Addy working holiday maker who is leaving Australia, again, like temporary residents, is entitled to a refund of their superannuation contributions. Same rules apply except that the rate of tax that's deducted is a absolutely [inaudible 00:58:33] 65%. That's an eye watering figure.

And finally, it is worth pointing out that the Medicare levy does not apply to foreign residents. It also doesn't apply to temporary residents who have a Medicare entitlement statement from the DHS showing they're not entitled to Medicare benefits. Do bear in mind however, that some temporary residents do have to pay the Medicare levy if they're from a country such as the UK, New Zealand, Ireland, the Netherlands, Norway, Sweden, Finland and others because of the reciprocal agreements between those countries and Australia. Now, at that point, I've pretty much used up my hour, but nevertheless, if you've got any questions which I can't deal with now, do please feel free to contact me. My details are on the slide, however, I'll just hand you back to Alison and then we've got a few minutes to take some questions after that.

Alison Wood:

Thank you very much, Mark. All right, we have had quite a few questions come in today, so we will run through them, but feel free to let me know when that's the end of the Q&A, and then yeah, everyone can direct them through via email. In the interim, I'll quickly run through our upcoming webinars. So tomorrow, we're looking at insolvency and restructuring, then family law property settlements, also accessing super benefits. Then our tax technical update for the month, also looking at staff onboarding, cybersecurity and tax considerations of Christmas parties. So let's jump into this Q&A, Mark. So first one was from David. So do bridging visas overwrite the domicile test?

Mark Chapman:

In what sense?

Alison Wood:

David, if you can... Yep.

Mark Chapman:

So the actual visa type is not really relevant to determining whether you're resident or not. So you simply apply, first of all, you apply the resides test, and if they fail that, you then need to consider the other two tests, possibly the superannuation test, but let's forget that, the other two tests and determine whether they're resident

according to the domicile test or the 183-day test. So that is entirely disconnected to your visa type. You're either domiciled here or you're not. The visa type won't be relevant to that discussion.

Alison Wood:

Thank you, Mark. Steven's asked, "How about an Australian living overseas for the past six years, but they're using an Australian bank account for their foreign business trading and the Australian is also using their ABN for the foreign business, does this affect residency?"

Mark Chapman:

It would be a factor to take into account, but I would think that in this instance, your physical presence abroad indicates that, which is six years, you're out of the country for six years, presumably living in pretty well settled overseas, wherever they are, that would be taken as a sort of dominant factor if you like. So the fact that they're trading through an Australian ABN and their income might be paid into an Australian bank account would be outweighed by the fact that they've been overseas for six years. Presumably, it sounds like they're settled and not planning to come back and therefore they are actually nonresident in that situation.

Alison Wood:

Thank you, Mark. Chris has asked, "Can you please explain the concept of the foreign resident CGT withholding at 12.5%?"

Mark Chapman:

Yes. So basically the proceeds, so you don't actually work out the capital gain, you actually apply that to 12.5% to the proceeds and that is deducted and paid across to the ATO by the purchaser. And when the seller actually comes to report, their capital gain further down the track in the tax return, the amount of tax which has been withheld is actually available as credit to reduce their tax liability. It was introduced to prevent basically tax avoidance whereby people go overseas, sell their Australian property and then don't pay any capital gains tax on it.

It makes sure that the ATO does actually receive the capital gain or at least something approaching the capital gain from the purchaser before the actual sale happens. And it makes sure that the ATO does actually get their tax. It is possible to withhold that rate to value that rate downwards potentially to zero. So you simply need to give reasons. For example, if it was your main residence, whatever you might potentially end up reducing the gain and therefore you cannot advise the ATO that the rate of withholding should be lower than 12.5%. But there is a sort of standard rate which starts at 12.5%.

Alison Wood:

Thank you, Mark. Simone has said, "It would be really helpful to know what all the different residency status are reported as in single touch payroll."

Mark Chapman:

Well, I am not quite sure how it applies to single touch payroll, but basically, I can't cover every possible situation because every taxpayer is different, but ultimately the taxpayers are either going to be resident, they're going to be non-resident or they're going to be temporary residents or working holiday makers. So really, you just need to, those are the four categories to focus on and whichever one applies to your clients is their status.

Alison Wood:

Thank you, Mark. Arthur asked, "Does the tax-free threshold get apportioned if one ceases tax residency?"

Mark Chapman:

Yes, it does. So again, you get the full whatever it was, 14,000 and something dollars and the remaining 4,000 and something dollars is simply apportioned for a period of time that you are actually resident here, but you don't get it for the period that you are non-resident.

Alison Wood:

Thank you. Chris has asked, "There's a temporary resident of New Zealand, are they treated as a foreign resident or a tax resident?

Mark Chapman:

Well, basically both. I mean, they're treated as a temporary resident, so they get the best of both worlds. So they're not taxed on their overseas income, they're only taxed on their Australian source income, which is basically the same as a foreign tax resident. However, they are subject to tax at Australian resident tax rates. So they're basically taxed for what they are taxed on. They pay tax at Australian resident tax rates, which means they get the Australian tax-free threshold and they pay Australian resident rates. So, potentially they have less to pay because they're taxed as residents.

Alison Wood:

Thank you, Mark. Simone has said, "WHM residents, so does this apply to the tax return only and not in payroll?"

Mark Chapman:

Well, look, the payroll will be relevant because ultimately the income tax which is deducted by the employer will be determined by their status, and if they are actually not working holiday makers, that their employers should not be deducting tax at the working holiday maker rate and so therefore it will impact their payroll potentially.

Alison Wood:

Thank you. Arthur said, "What's happening to tax reform in this space? This area is highly subjective."

Mark Chapman:

Well, it is, and there are proposals floating around to completely reform the residency system. However, they are pretty much at the drawing board at the moment. I think it was about two or three years ago that the Board of Tax put forward some recommendations to reform the residency rules. Well, there's no indication whether the current government will adopt those recommendations or not. So either way, we've got several years, I suspect of the current rules still to run. Those revised rules are much more of a bright line test. So I didn't cover them in this presentation because they're not really relevant because they're just a proposal at the moment. However, if they do get adopted, then ultimately the residency rules will be far less subjective. They'll be far more basically fact driven basically, depending on how long you are actually in Australia will determine whether you're a resident or not.

Alison Wood:

Thank you, Mark. We've got three questions left. Hopefully, we can squeeze these in. So Tamara has asked, "A client returned from overseas to Australia and bought a property here in Australia. Unfortunately, due to a health issue, they left the country and returned three years later. They are an Australian resident. They only have one real estate property, which is in Australia." And I'm not sure of the question.

Mark Chapman:

I'm not quite sure of the question.

Alison Wood:

Oh, are they an Australian resident? Thanks, Tamara.

Mark Chapman:

Oh, well, if they've gone back overseas and they are basically living overseas and they've got a permanent place of abode overseas, then they'll be foreign resident now. But they may well have been resident for the period that they were actually here. So the three years that they were here, they would've been resident, but presumably now, they're not resident.

Alison Wood:

Perfect. Thank you, Mark. Chris has asked, "I have a client who lives in New Zealand, and held property in Australia. When he sells his property, will he get a CGT discount?"

Mark Chapman:

No, because he's not resident here, so unfortunately not.

Alison Wood:

Thank you. Lucky last Diane. So after moving from a working holiday visa to another temporary visa, do they become a temporary resident and then determine residency from that date based on what happens in the future after inferred tax year?

Mark Chapman:

If they cease to be on a working holiday maker visa, they'll cease to be taxed as working holiday makers from the date on which they become, say a temporary resident. However, they won't actually become full tax residents until they ultimately choose to become permanent residents or citizens, and therefore they'll go on a bit of a journey if you like, a residency journey, starting off as working holiday makers, then becoming temporary residents and then ultimately possibly becoming full tax residents.

Alison Wood:

Perfect. Thank you. Really appreciate you getting through all those questions, Mark. We've also had some comments. Hats off to you. Everyone appreciates the Q&A there, so we will look at wrapping up the session here. In terms of next steps, I will ask everyone to please take a moment to complete the feedback survey. It's important that we hear your opinions, and shortly after the session today, you'll receive an email letting you know the e-learning recording is ready and you can also access the PowerPoint, transcript, and CPD certificate as well. So thanks again to Mark for the session today, and thank you to everyone for joining us. We hope to see you back online for another CCH Learning webinar very soon.