

GMS Flash Alert

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Australia - Individual Tax Residency Rules: Change Is Coming

An independent review of the Australian tax residency rules by the Board of Taxation was recently made public.¹ The review called for changes to the residency rules to bring them more in-line with modern work and lifestyle practices, by simplification of the current "uncertain and complex" residency tests.

At the same time a recent decision of the Federal Court of Australia, *Harding v Commissioner of Taxation*, highlights the timeliness of this initiative and the unpredictability that taxpayers departing Australia have faced when interpreting and applying the current "qualitative" individual tax residency rules.

WHY THIS MATTERS

Whether a taxpayer is an Australian tax resident will determine if he or she continues to be liable to pay Australian taxes on income earned while overseas.

The stakes are particularly high when taxpayers are heading to jurisdictions with low or no income tax which may not have tax treaties with Australia. A finding of continued Australian tax residency in these situations can often mean the difference between a taxpayer paying full Australian tax on foreign wages or no tax at all.

There is also a "flow-on" effect to an employer who may be faced with complying with Australian PAYG withholding and other employer tax obligations for residents depending upon the employer's connections to Australia.

Background

Australia's individual income tax residency rules have been in place, largely unaltered, since the 1930s. Much has rested on case law interpretations of the ordinary meaning of "resides" and "permanent place of abode." For

Australians who live and work overseas, the 2009 removal of the foreign earnings exemption has caused much more to ride on these definitions. For foreign nationals coming to work in Australia, the lack of a precise rule has also caused uncertainty.

Board of Taxation Report

The Board of Taxation ("BoT") is a non-statutory body appointed by the federal government to advise it on tax policy matters. On 9 July the BoT made public its August 2017 report to the federal government on Australia's individual tax residency rules, including a recommendation that new rules be legislated. In parallel, the Minister for Revenue requested that the BoT undertake further public consultation with regard to this recommendation.

The BoT has not made a concrete recommendation on what the new residency rule should be. However at this stage it broadly envisages that there would be a pair of two-stage tests, one each for individuals becoming resident and ceasing to be resident. The first stage would be based on a days count. The second stage would assess certain lifestyle factors in determining the status of an individual who was not a resident under the first stage. The consultation process may bring other more effective possibilities to light.

Harding v Commissioner of Taxation

In *Harding*, the taxpayer accepted that he was an Australian-domiciled person. On that basis, he could only cease Australian tax residence if he had ceased to reside in Australia under ordinary concepts, and had also established a permanent place of abode outside Australia.

The taxpayer was an Australian citizen living and working in the Middle East for more than six years. During this period, Mr. Harding lived in a number of fully furnished apartments within the one apartment complex in Bahrain.

The case concerned only one of the years of income during which Mr. Harding lived in Bahrain. The court found that for this year, the taxpayer did not reside in Australia under ordinary concepts. In considering whether the taxpayer had also established a permanent place of abode in Bahrain, there was a focus on the use of the apartments in Bahrain and Mr. Harding's intention to bring his family to Bahrain and move out of the furnished apartment complex. Unfortunately the latter never eventuated due to Mr. Harding and his wife divorcing. Factors in the analysis of "permanence" included Mr. Harding having purchased his own television and linen, but not having to pay for utilities.

Ultimately the decision was that the taxpayer continued to be a tax resident of Australia because he did not have a permanent place of abode outside of Australia.

KPMG NOTE

If the BoT's work can lead to a situation where an individual taxpayer's residence status is much less likely to require clarification by the Federal Court, then great progress will have been made.

FOOTNOTE:

- 1 For the "Self-initiated Review of the Income Tax Residency Rules for Individuals," click [here](#).

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