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BREAKING AUSTRALIAN RESIDENCY FOR TAX PURPOSES

We live in a more integrated world than ever before. As a result, the workforce is more globalised and increasingly more mobile. It is increasingly common for people to work overseas on a short stint or on a more permanent role. The residency of that individual for tax purposes then becomes an issue.

In essence, an individual who is domiciled in Australia is generally considered to be a tax resident of Australia, unless the Commissioner is satisfied that their permanent place of abode is outside Australia. Generally, an individual's place of abode is considered to be a dwelling where one lives with their family and sleeps at night. A permanent place of abode need not necessarily indicate an intention of the individual to remain in the foreign country indefinitely without any foreseeable return date to Australia.

In contrast, the individual should be able to support that they have an enduring relationship with the foreign country which is more than temporary or transitory in nature. The courts have ruled that an intention to return to Australia in the foreseeable future does not prevent the establishment of a permanent place of abode in a foreign country.

As a general rule of thumb, an assignment ***greater*** than two years is likely to indicate that an individual is breaking residence, unless they are unable to establish a permanent place of abode outside of Australia. The following factors are relevant when determining if an individual has established a permanent place of abode outside of Australia:

- 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 residency 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 duration and continuity of the taxpayer's presence in the overseas country; and
- the durability of association that the person has with a particular place in Australia, (i.e. maintaining bank accounts in Australia, informing government departments that he or she is leaving permanently i.e. Centrelink or AEC, place of education of the taxpayer's children, family ties and so on).

The weight given to each factor will vary depending on the individual's circumstances. There is no single factor that is considered exclusively and not all factors need to be present to establish a conclusive argument for the individual having a permanent place of abode outside of Australia.

There are certain actions that an individual can take to support the existence of a permanent place of abode outside of Australia by severing certain habitual ties with Australia. Getting tax advice and proper planning in advance can therefore give a little bit more certainty and maximise the tax outcome.

Please contact Peter Hong or Sean Pearce if you have any queries.

Passive Investment Companies and the Lower Tax Rate – Take 3!

In our July and October 2017 PAN Member Tax Flashes, we noted that the Australian Taxation Office (**ATO**) in a footnote to the draft ruling TR 2017/D2 stated that the activities of passive investment companies may also constitute carrying on a business. As a consequence of this there was a view that this meant passive investment companies could not only qualify for the reduced corporate rate, but also possibly other small business entity concessions , such as the CGT concessions, Small Business Rollover Restructure, immediate depreciating assets write-off and many others.

At the time the Revenue Minister, Kelly O'Dwyer, issued a media release stating that reports that the ATO had broadened the interpretation of company tax cuts were premature. The Minister further stated that the policy decision made by the Government to cut the tax rate for small companies was not meant to apply to passive investment companies.

On 18 September 2017, the Government in turn released exposure draft legislation proposing to ensure that corporate tax entities with predominantly passive income (such as rent, dividends, interest and capital gains) cannot access the lower corporate tax rate of 27.5%.

Having received numerous comments on the draft legislation the Government then introduced new legislation on 18 October 2017 to apply from 1 July 2017 enabling a company to access the 27.5% tax rate if:

- no more than 80% of the corporate tax entity's assessable income for that income year is "base rate entity passive income"; and

- the aggregated turnover of the corporate tax entity for the income year is less than the aggregated turnover threshold for that income year ($25 million for 2018).

The final legislation was different to the exposure draft legislation in that it removed the requirement for the company itself to be carrying on a business.

In broad terms, "base rate passive income" will comprise dividends, interest, rent, royalties and net capital gains. Furthermore a company's entitlement to assessable income consisting of partnership or trust income will also be considered passive income to the extent it is referable to amounts of passive income derived by the partnership or trust.

So essentially where a company derives at least 20% of its income from non-passive sources, either directly or indirectly through a partnership or trust it will be able to access the 27.5% tax rate for the 2018 year. The only proviso is that its aggregated turnover is less than $25 million. This clearly enables corporate beneficiaries of trusts that derive at least 20% of their income from non-passive sources to access the lower 27.5% tax rate.

If you have any queries on the subject, please contact Sean Pearce or Peter Hong.

PAYROLL TAX – THE OFTEN FORGOTTEN BUT PAINFUL TAX

We have noticed in recent times the Office of State Revenue ("OSR"), have ramped up their presence and are conducting a significant number of reviews. The major area they are focusing on are contractor payments. We also note that they are now focusing on specific industries such as the building industry.

Contractor payments are often over looked by many accountants and can result in significant payroll tax liabilities, as they often push a client above the threshold or alternatively add significantly to existing liabilities. Worse still, the reviews generally go back 5 years with the penalty in the 5th year often being 50% of the resulting liability.

Revenue Ruling PT6.1 helps establish the process of determining whether an employment relationship exists and is focussed on gathering detailed information about the relationship, as well as identifying the indicia that either support or do not support the existence of an employment relationship.

The factors the Commissioner considers are outlined in paragraph 52 of the Ruling. These include whether the worker:

1. undertakes to produce a "given result" for a fixed fee rather than to simply do work i.e. the worker is paid for the result of the labour and not for the labour itself;
2. provides the material and/or equipment necessary to undertake the task. The equipment should be more than "incidental" to the person's services;
3. has an unfettered discretion to delegate the work;
4. bears the risk of making a loss in running a business through incurring significant expenses related to the income earned; and
5. provides services to the general public.

The Commissioner notes at paragraph 51 of the Ruling that where all these factors exist in a relationship between a worker and the person for whom the services are provided, it is likely that the Commissioner will accept that the relationship is one of independent contractor/principal.

Further, the Commissioner provides at Schedule 1 of the Ruling a list of questions which when answered, will give an indication as to whether an employer/employee relationship exists. If the answer to most of the questions is "yes", it is a strong indication that the person providing the services is an employee and payments made to that person would be subject to pay-roll tax.

These questions being:

- Is the person providing the services paid on a time basis (e.g. hourly rate) rather than on a per job basis?
- Is the contract wholly or principally for labour?
- Does the person requiring the services have the authority to control or direct the manner in which the work is to be performed?
- Is the person providing the services prevented from delegating or subcontracting his/her work to another person without approval?
- Is the person providing the services engaged for a lengthy period or on a continuing basis?
- Are the services provided by the worker ordinarily required by the person requiring the services in the normal course of their business?
- Is the person providing the services performing work similar to work carried out by an employee in the organisation?
- Are the work hours defined?

Further, it must be remembered that even if a contractor operates through an entity such as a trust or company this is basically irrelevant in determining whether the relationship between the contractors and the entities in question are one of independent contractor/principal for Payroll Tax purposes.

Specifically, section 11(E) of the Payroll Tax Act provides that:

"Where any person enters into any agreement, transaction, or arrangement ....., whereby a natural person performs or renders, for or on behalf of another person, services in respect of which any payment is made to some other person related or connected to the natural person performing or rendering the services and the effect of such agreement, transaction, or arrangement is to reduce or avoid the liability of any person to the assessment, imposition, or payment of pay-roll tax, the Commissioner may:

a) disregard such agreement, transaction or arrangement;
b) determine that any party to such agreement, transaction, or arrangement shall be deemed to be an employer for the purposes of this Act; and
c) determine that any payment made in respect of such agreement, transaction, or arrangement shall be deemed to be wages for the purposes of this Act."

As such, the Commissioner may disregard any agreement between an employer and third party and deem any payments to the third party to be wages for the purposes of the Act.

Should you have any concerns with respect to contractors and payroll tax liabilities, please call Nigel Kingston.

KEEP OFF THE COMMISSIONER'S CHRISTMAS WISHLIST

With the festive season and the 2018 new year approaching, here are a few target areas which can get you or your client onto the Commissioner's Christmas (and New Year) audit list.

1. **Property developers** – the main audit areas for this group of businesses centres on the following:

a) Have ITCs been over-claimed?
b) What is the basis that developer is claiming full ITCs (ie. Selling straight after completion of construction) and have their intentions changed.
c) Has the appropriate amount of GST been paid on the sale of developed property?
d) For once off developments the issues extend from GST the question of whether the developed property is a revenue generating activity from an isolated transaction.
e) Was the developer entitled to apply the margin scheme or sale of a going concern concession?

2. **Capital gains tax (CGT) non-disclosure and under-reporting** – The Commissioner continues to see businesses engaged in complex restructuring that attempt to disguise asset sales or manipulate asset valuations to artificially reduce their capital gains tax (CGT) liabilities. Some businesses attempt to reclassify revenue and capital items so they can inappropriately access concessional tax treatments. Failure to disclose CGT events or claiming small business concessions when ineligible will also bring the Commissioner's attention to your door.

   The ATO will conduct a number of audits and reviews to identify incorrectly reported (or non-reported) capital gains and losses. Their continued focus is on ensuring that foreign residents disposing of Australian property disclose their transactions and pay capital gains tax where liable. The ATO will continue to data match information from the office of state revenue with information recorded in the tax returns.

3. **Companies raising capital through an IPO or the issue of shares and or options** – have they claimed input tax credits (ITCs) on input taxed financials supplies and has the "financial acquisitions test" (FAT) been breached? - as capital raising information is readily available through the ASX and the costs of such activities is high, this is an easy target area for the ATO to devote their audit teams towards.

4. The ATO will also be targeting **Uber and Airbnb operators** with the focus on under reported income. For Airbnb operators – any Capital Gains Tax arising from disposing of their property and the property was generally available for rent. For Uber drivers – GST

and income tax is subjected on the gross fare and that they are complying with all legislative requirements.

5. **Small Business** – in particular;

a) Internet businesses – whether internet businesses are disclosing the correct amount of income and paying the appropriate amount of GST on their transactions;
b) Have all criteria been met in order for the Taxpayer to apply the small business tax concessions;
c) where some individuals continue to split their Personal Services Income (PSI) with an associate to lower their tax debt, the ATO are particularly getting more vigilant in enforcing the PSI rules;

If you find that you or your client falls within one or more of the Commissioner's Christmas wishlist above, we encourage you to seek advice to ensure you do not become the ATO's audit target for the new year.

If you have already been notified of an impending audit or review and need assistance in this regard, please contact Ms Mimi Ngo of MKT.

MKT Webinars – Tax Residency for Individuals, Companies and Trusts

Our latest webinar, Tax residency for Individuals, Companies and Trusts is now available to download from our website.

In this session, Sean Pearce discusses the current tax issues, tips and traps in determining the tax residency of individuals, companies and trusts.

Sean also discusses recent developments in areas, such as:

- Recent AAT cases dealing with individual residency;
- The recent High Court decision in Bywater Investments Ltd v FCT;
- The draft Taxation Ruling TR 2017/D2; and
- The tie-breaker rules in Double Tax Agreements.

A reminder that PAN Member PD vouchers can be used to download our webinars. Please contact Nicola for the voucher codes or log in to the PAN Secure Zone on our website.