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Income Tax in Australia

Issues for New Zealand residents

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Australia's Tax System – The Basics

Australian residents are required to declare assessable income from all sources.

Non-residents of Australia are required to declare their assessable income from Australian sources only.

From assessable income deduct all allowable deductions to arrive at the taxpayer’s taxable income.

Tax residence – Individuals

An individual is a tax 'resident' if any of the following four tests are satisfied:

- Ordinary concepts;
- Domiciled in Australia unless permanent place of abode outside Australia;
- Presence in Australia > 183 days; or
- Member of a Commonwealth superannuation scheme.

Temporary residents

A person is a "temporary resident" if:

- he or she is the holder of a temporary visa granted under the Migration Act 1958;
- he or she is not an Australian resident within the meaning of the Social Security Act 1991; and
- his or her spouse (if he or she has one) is not an Australian resident within the meaning of the Social Security Act 1991.

Note: See Taxation Determination TD 2012/18 in regards to New Zealand individuals.

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Australian tax rates

Company tax rate: 30%

Resident individual tax rates:

Taxable Income			Tax Payable			
$0	-	$6,000			0%	
$6,001	-	$37,000	$0	+	15% of excess over	$6,000
$37,001	-	$80,000	$4,650	+	30% of excess over	$37,000
$80,001	-	$180,000	$17,550	+	37% of excess over	$80,000
$180,001	+		$54,550	+	45% of excess over	$180,000

Non-resident individual tax rates:

Taxable Income			Tax Payable			
$0	-	$80,000			32.5%	
$80,001	-	$180,000	$26,000	+	37% of excess over	$80,000
$180,001	+		$63,000	+	45% of excess over	$180,000

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Tax residence – Companies

A company will be a resident of Australia if:

- it is incorporated in Australia; or
- it both carries on business and has its central control and management in Australia; or
- it both carries on business in Australia and has its voting power controlled by Australian resident shareholders.

Tax residence – Trusts

A trust estate is taken to be a resident trust estate if, at any time during the income year, a trustee of the trust estate was a resident or the central management and control of the trust estate was in Australia.

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Tax residence – DTA

Australia's various Double Tax Agreements (DTAs) may also provide rules for determining residency. This sometimes includes 'tie-breaker' rules where a taxpayer is a resident of more than one country (see International Tax Agreements Act 1953).

Source of income

Income	General Rule of Source
Employment or personal exertion income	Where services are performed (*FCT v French* (1957) 98 CLR 398; *FCT v Efstathakis* 79 ATC 4256). Note: Place of making contract <u>may</u> be relevant where particular skills are required (*FCT v Mitchum* (1965) 113 CLR 401).
Trading or business income	Relevant factors include: ▪ where contract is negotiated and made; ▪ where contract is performed (e.g. goods or services provided); ▪ where payment is made, <u>and</u> the residence of the payer.
Dividend income	The place where the profits from which the dividends are paid are made (*Esquire Nominees v FCT* 73 ATC 4114).
Interest income	Where the contract is made <u>or</u> where the funds are advanced (*FCT v Spotless Services Ltd & Anor* 95 ATC 4775). Note: Other relevant factors may include: ▪ the location from which the principal and interest are repaid; or ▪ the place where the borrower carries on business.

Source of income

Income	General Rule of Source
Rent from real property	Where the real property is located (*Rhodesia Metals Ltd (in liq.) v Commissioner of Taxes* [1940] AC 714).
Rent from other property	▪ Where hiring agreement is executed; or ▪ Where property is used (i.e. location of economic activity that generates the rental income). Note: The appropriate test depends on the nature of the property (e.g. income tangible property is more likely to be sourced from place of use).
Royalties	▪ From the use of property - the place where the property is located; or ▪ From the use of know-how and technical knowledge - the place where the contract is made and the know-how provided.

Common types of business entities

In Australia the major forms of business structure are as follows:

- sole trader - an individual trading in their own right;
- partnership - an association of people or entities carrying on a business together, but not as a company;
- company - a legal entity separate from its shareholders; and
- trust – a relationship which involves an entity (trustee) holding a trust property or income for the benefit of others (beneficiaries).

Partnership

A partnership is not a separate legal entity.

It is an association of two or more individuals or entities that go into business together for the purpose of carrying on a business activity with a view to profit or who are in receipt of income jointly.

Partnerships – who pays the tax

Each partner pays tax on their share of net partnership income.

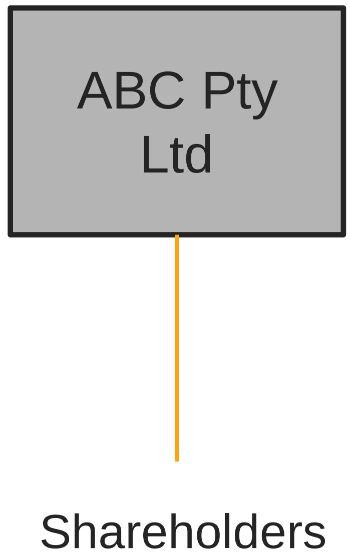
Partnership has to lodge an income tax return.

Each partner pays tax according to their identity and own personal circumstances.

Company

A company is an independent legal entity able to do business in its own right. It is separate from its directors and shareholders. The shareholders own the company and directors run the company. The directors of a company, as well as company employees, can be shareholders.

Company



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Company

- Assessable at company level – 30% tax rate
- There is no flow-through taxation. Income distributed by the company to its shareholders is dividends in the hands of shareholders and subject to the dividend imputation rules
- Distributions to shareholders must be in accordance with rights attaching to shares
- No capital gains tax discount available

Imputation system

Under the simplified imputation system contained in Part 3-6 of the ITAA 1997, corporate tax entities are able to pass on credits for income tax paid to their members. Australian members are able to claim a tax offset for the credit and in some circumstances claim a refund if they are unable to fully utilise the tax offset.

Company

Illustration - imputation taxation system		
Company level		
Income earned	$100.00	
Company tax (30%)	**$30.00**	
Net Profit after tax	$70.00	
Shareholder level		A credit for tax paid by the
Franked dividend received	$70.00	company is allowed to the shareholder
Imputation credit	$30.00	
Taxable income	$100.00	
Tax Payable (46.5%)	($46.50)	
Credit for company tax	$30.00	
Net tax on Dividend	**$16.50**	
Total tax on company earnings	**$46.50**	

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Trusts

What is a trust?

A trust is not a separate legal entity. It is a relationship which involves an entity (trustee) holding property or income (the trust property) on certain terms for the benefit of others (beneficiaries).

There are four essential elements of a trust:

- a trustee;
- an object (a beneficiary);
- a subject (a trust property); and
- an equitable obligation attaching to the trust property.

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Who pays the tax

General rules

Although a trust is not a separate legal entity, the trustee is required to lodge an income tax return showing the income derived and expenses incurred by the trust as if it were a separate taxable entity.

The trustee is not assessed on that income provided beneficiaries have been made presently entitled to the income in which case the beneficiaries will be subject to tax except where a beneficiary is under a 'legal disability‘ or a non-resident in which case the trustee will be assessed.

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Discretionary trust

In a discretionary trust the beneficiaries do not have any fixed interest in the trust income or its property but the trustee has a discretion to decide whether any of them is to be entitled to income or capital of the trust.

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Unit Trusts

These are generally fixed trusts where the beneficiary's fixed entitlements to the income and capital of the trust are divided into 'units'. The amount of the beneficiary's entitlement to the income or capital of the trust is dependent on the number of units held. The beneficiaries are usually called unitholders.

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Other – Limited Partnerships

A "limited partnership" is effectively defined as an association of persons (other than a company) carrying on business as partners or in receipt of ordinary income or statutory income jointly, where the liability of at least one of those persons is limited.

Limited partnerships may be established under specific legislation in Australia and overseas.

Limited partnerships are generally taxed as companies.

Other – Foreign Hybrids

A "foreign hybrid" regime operates in Australia.

A foreign hybrid is a foreign hybrid limited partnership or a foreign hybrid company

Foreign hybrids are treated for taxation purposes as partnerships. Therefore, the normal partnership "flow-through" taxation treatment applies.

Other – Foreign Hybrids

To qualify as a foreign hybrid limited partnership or a foreign hybrid company, the entity must have the following essential features:

- it must be formed in a foreign country and must not be an Australian resident at any time;
- it must be taxed in the relevant foreign jurisdiction as a partnership;
- it must not be taxed in another foreign country (apart from the country of formation) as a resident of that country; and,
- there must be a least one Australian taxpayer who has a direct or indirect interest of at least 10% in the limited partnership or company (note that where this requirement is not met there is the ability for an election to be made so as to satisfy the requirement).

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Branch Operation

Two main options for business operations

- branch operation of NZ resident entity
- establish an Australian company/subsidiary

Branch Operation

A New Zealand resident entity deriving business profits sourced in Australia is subject to income tax in Australia on those profits unless a specific exemption applies.

Branch Operation

General rule is modified by any relevant Double Tax Agreement (DTA).

Australia/New Zealand DTA allows Australia to tax the business income of a non-resident entity only to the extent the business operations are attributable to a ‘permanent establishment’ in Australia – refer Article 7.

Permanent Establishment

Article 5 of the DTA defines a permanent establishment generally as follows:

For the purposes of this Agreement, the term “permanent establishment” means a fixed place of business through which the business of an enterprise is wholly or partly carried on.

Permanent Establishment

Does “permanent” mean everlasting?

A presence in Australia of 6 months or more will generally constitute a “permanent” presence for the purposes of the permanent establishment definition.

Refer Taxation Ruling TR 2002/5.

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Permanent Establishment

The term “permanent establishment” includes especially:

(a) a place of management;
(b) a branch;
(c) an office;
(d) a factory;
(e) a workshop;
(f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources; and
(g) an agricultural, pastoral or forestry property.

A building site, or a construction, installation or assembly project constitutes a permanent establishment if it lasts for more than 6 months.

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Permanent Establishment

An enterprise has a permanent establishment in a contracting state if:

(a) it performs services in the other contracting state either:

(i) through an individual who is present for more than 183 days in any 12 month period and more than 50% of the gross revenue attributable the active business activities of the enterprise during the relevant period are derived from that individual's services;

(ii) for more than 183 in any 12 month period and the services are performed for the same or connected projects through one or more individuals who are present in that state;

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Permanent Establishment

An enterprise has a permanent establishment in a contracting state if:

(b) it carries on activities (including the operation of substantial equipment) in the exploration for or exploitation of natural resources or standing timber situated in the state for a period or periods of more than 90 days in any 12 month period; or

(c) it operates substantial equipment in the contracting state (including as provided in (b) (above)) for a period of more than 183 days in any 12 month period.

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Permanent Establishment

Exclusions:

- a person who is a broker, a general commission agent or an independent agent and who is acting in the ordinary course of that person's business as such a broker or agent and at arm's length

- activities including:
    - the maintenance of stock solely for the purpose of storage, display or delivery; and
    - the maintenance of a fixed place of business solely for the purpose of purchasing goods

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Permanent Establishment

Exception to the exclusions:

A person, other than an independent agent, is deemed to have a permanent establishment in a Contracting State if the person:

- has, and habitually exercises, in that Contracting State an authority to substantially negotiate or conclude contracts on behalf of the enterprise; or
- manufactures or processes in a Contracting State for the enterprise goods or merchandise belonging to that enterprise;

unless the person's activities are only limited to the specifically excluded activities (e.g. solely for storage, display or delivery etc.)

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Tax Registration

Income Tax File number (TFN)

- Required for Australian entities and New Zealand entities with a permanent establishment/branch operation in Australia

Australian Business Number

- Required for entities carrying on an ‘enterprise’ in Australia. Will include non-resident entities carrying on an enterprise in Australia. (Note, this is the number used for GST registration purposes.)

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Tax Registration

PAY AS You Go Withholding (PAYGW)

- Required for Australian resident entities paying interest, royalties and unfranked dividends to non-resident entities
- Required for Australian resident and non-resident entities employing individuals in their business enterprise and paying salary or wages

Tax Registration

Fringe Benefits Tax (FBT)

- Required for Australian resident and non-resident entities employing individuals in their business enterprise and paying salary or wages and providing fringe benefits

Compliance

Annual income tax return required to be lodged.

Business Activity Statements (BAS) – required on a quarterly or monthly basis depending on size of entity. Includes remittances for:

- FBT
- PAYGW
- Income tax instalment amounts, etc

Compliance

For Australian incorporated private companies at least one of the directors of the company and the company secretary (if one exists), must reside in Australia.

If a foreign company chooses to establish a branch office in Australia, it must be registered as a foreign company with the Australian Securities & Investments Commission.

Upon registration, an Australian Registered Body Number (ARBN) will be allocated to the foreign company.

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Compliance

Once registered, the branch must file the foreign company's annual accounts and comply with other reporting requirements.

Must also:

- Appoint a local agent (either a person or company) for service of notices.
- Maintain a registered office in Australia.
- Provide a list of the Australian resident directors.

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Compliance

New Zealand companies that are registered as foreign companies in Australia are exempt from the requirements to lodge certain basic company information and financial statements with ASIC.

Further ASIC information:

http://www.asic.gov.au/asic/asic.nsf/byheadline/Foreign+Companies?opendocument

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Issues for non-residents

Thank You

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