Leaving Australia - Key Steps for Individuals & SMEs

Carlo Di Loreto

Tuesday, 10 June 2025

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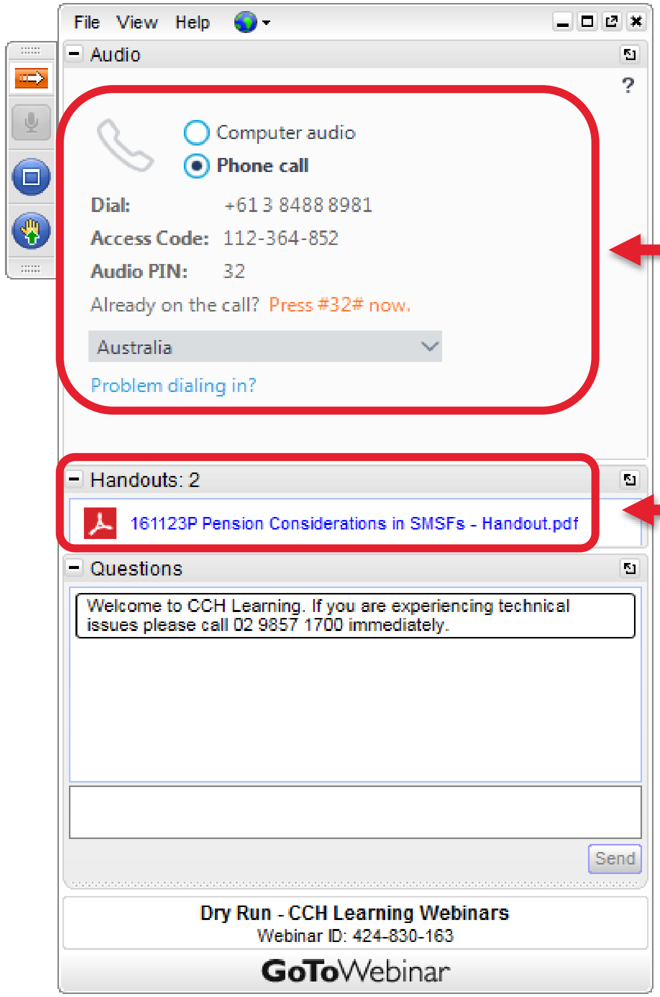

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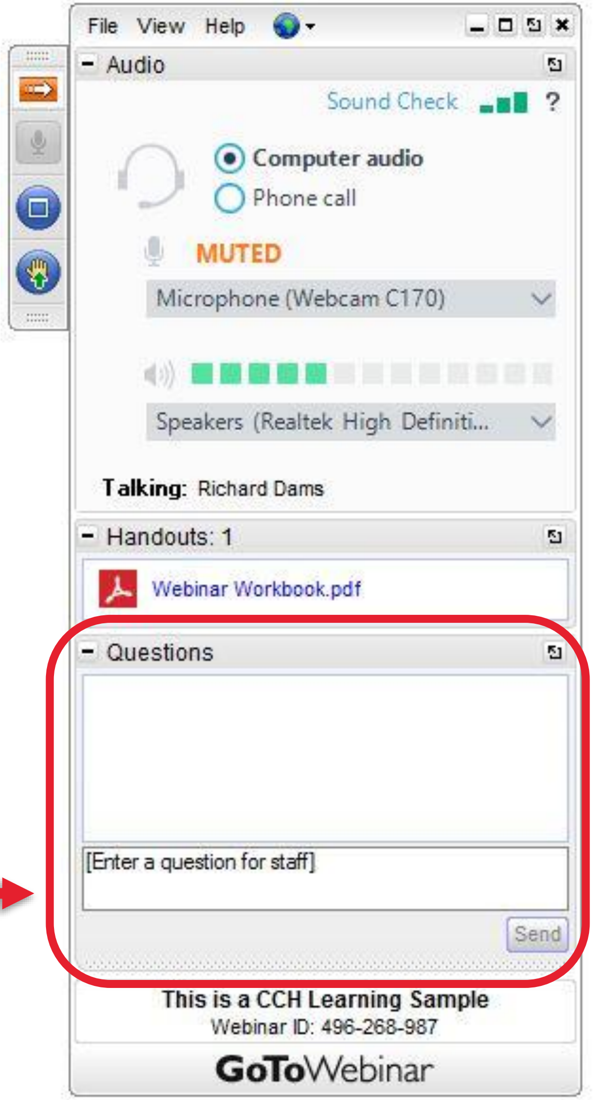

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Your Presenter

Carlo Di Loreto

Partner - Tax Advisory

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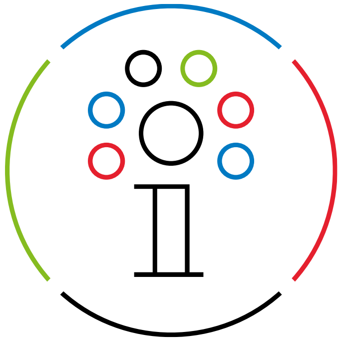
Today's session will cover

Overview



- tax residence rules for individuals, companies, trusts and self managed superannuation funds
- dual residence provisions
- double tax agreement implications on taxation rights in Australia
- CGT events on becoming a foreign resident
- other obligations for foreign residents in Australia

Overview

- Australia has complex tax residence rules and where you have individuals or groups “leaving” Australia, there are a series of key issues to consider
- most small or medium sized client groups will have companies, trusts and self managed superannuation funds
- typically, the residence status of the “controlling” individual will have a direct impact on SME structures and this has to be carefully managed to avoid pitfalls
- it is imperative that clients receive advice prior to any moves overseas to ensure their tax obligations are managed effectively in Australia
- many clients may only bring this to their adviser’s attention after the fact and on many occasions, this may already be too late

Overview

- practically, the key issues impacting on an individual leaving Australia (for them and their family entities), can be summarised, as follows:
  - the change in their tax residence status when they leave Australia
  - the CGT implications on ceasing to be a resident
  - DTA issues
  - taxation of income earned by foreign residents
  - impact on SMSF's
  - taxation of foreign sourced income
  - international tax avoidance

Overview

- for ‘outbound’ clients, need to consider:
  - whether Australian or foreign resident
  - source of income
  - CGT issues on departing Australia
  - relief from double taxation and availability of foreign tax credits
  - impact of their residency on their group structure
  - ongoing foreign resident issues (e.g. distributions from Australian trusts, dividends, foreign resident CGT withholding etc.)

Tax Residence of Individuals

Tax residence - individuals

- residence status is central to determining if liable to Australian tax on income (or otherwise)
- Australian residents assessed on their gross income derived from all sources - whether derived in or out of Australia
- resident individuals taxed at resident rates, plus Medicare levy – obtain benefit of tax-free threshold
- foreign residents are assessed on Australian sourced income only & taxed at foreign resident rates

Tax residence - individuals

- there are four components of the definition of a resident individual (s 6 ITAA 1936):
  1. whether the person is 'residing' in Australia, according to ordinary concepts
  2. the domicile and permanent place of abode of the person
  3. the 183 day test & usual place of abode
  4. eligible employee for the purposes of the Superannuation Act 1976
- The most relevant time to determine residency is the time when the income is derived
- However, must consider circumstances before and after the year of income

Tax residence – resides according to ordinary concepts

- the word ‘resides’ is not defined in Australian tax legislation and therefore, we are required to consider the ordinary meaning of the word ‘reside’
- the Macquarie Dictionary defines 'reside' as *'to dwell permanently or for a considerable time; have one's abode for a time*’
- the Shorter Oxford English Dictionary defines it as *'to dwell permanently or for a considerable time, to have one's settled or usual abode, to live, in or at a particular place*’
- if an individual resides in Australia according to ordinary concepts, the other tests do not need to be considered

Tax residence – resides according to ordinary concepts

- TR 2023/1 considers the following factors:
  - period of physical presence in Australia
  - intention or purpose of presence
  - behaviour while in Australia
  - family, and business or employment ties
  - maintenance and location of assets, and
  - social and living arrangements.

Tax residence – resides according to ordinary concepts

- the courts generally consider the following eight factors (which have been established through history of case law) in determining this:
  - physical presence
  - nationality
  - history of residence and movements
  - habits & “mode of life”
  - frequency, regularity and duration of visits
  - purpose of visits to or absences from a country
  - family and business ties with a country
  - maintenance of a place of abode

Tax residence – domicile & permanent place of abode

- domicile test mainly applies to individuals leaving Australia
- a person is a resident of Australia if their domicile is in Australia unless the Commissioner is satisfied that their permanent place of abode outside Australia
- need to consider:
  - what is a person's domicile
  - where is their permanent place of abode
- a person will not be a resident under this test where Commissioner satisfied:
  - has definitely abandoned their residency in Australia, and
  - commenced living permanently overseas

Tax residence – domicile & permanent place of abode

- domicile is a person's place of residence, abode, house, home
- three types of domicile:
  - domicile of origin: acquired at birth, being the domicile of father, generally
  - domicile of choice: acquired if person, being over 18, abandon's domicile of origin by changing country of residence
  - domicile by operation of dependence: acquired where person lacks capacity to acquire their own domicile, dependent on domicile of another person, such as minor and parent
- person domiciled in Australia treated as resident unless they have a permanent place of abode outside Australia

Tax residence – domicile & permanent place of abode

- significant body of case law developed over time, to assist in determining the tax residence status of individuals
- ATO rulings have also been released in the context of determining the tax residence status of individuals leaving and coming to Australia
- *FCT v Applegate 79 ATC 4307* - permanent means indefinitely continuing, but does not have to be everlasting - must be more than temporary
- can have a permanent place of abode outside of Australia, even if he/she has intention to return to Australia some day

Tax residence – domicile & permanent place of abode

- TR 2023/1 has replaced IT 2650 (withdrawn)
- states that a person's domicile continues until they acquire a different domicile, either by choice or by operation of law
- to show that a new domicile of choice in a country outside Australia has been adopted - must be able to prove an intention to make their home indefinitely in that country
- a working visa would not usually be sufficient evidence of an intention to acquire a new domicile
- if a person has in mind only a vague possibility of returning to Australia – may support the intention required by law to acquire a domicile of choice in the foreign country

NOTE

- ATO accepts two years abroad is a substantial period – anything less than this is unlikely to establish that permanent place of abode outside Australia [para 77 TR 2023/1]

Tax residence – domicile & permanent place of abode

- TR 2023/1 states the relevant factors as to whether permanent place of abode is overseas include:
  - length of overseas stay
  - nature of accommodation, and
  - durability of association.
- the longer the duration in one particular place – the more permanent likely to be
- staying in temporary accommodation indicates presence overseas is not permanent
- strength of connections in Australia and overseas
- location and maintenance of bank accounts
- location of other assets
- maintenance of professional memberships
- recreational activities

Permanent place of abode - Harding v FCT [2019] FCAFC 29

- Commissioner will consider facts and circumstances surrounding person's departure from Australia, their arrangements in relation to overseas country and nature of presence there
- accepts definition of 'place of abode' is inclusive - nature of dwelling, or dwellings, and particular use made of them will form part of relevant facts and circumstances taken into account as to:
  - whether a person has definitely abandoned residence in Australia; and
  - commenced living permanently overseas
- type of accommodation and conditions upon which it is occupied will be relevant in ascertaining whether any place of abode overseas is a permanent place of abode
- not necessary to live in a particular dwelling in a permanent way
- the accommodation provides a relevant indication of whether your presence overseas is permanent

Tax residence – 183-day test and superannuation test

- the 183-day test states that a person is a resident of Australia if:
  - he or she has actually been in Australia, continuously or intermittently, during more than one-half of the year of income, unless
  - the Commissioner is satisfied that person's usual place of abode is outside Australia and that he or she does not intend to take up residence in Australia.
- 'superannuation test', states that a person who meets any of the following conditions will be a resident of Australia:
  - 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 by (a) or (b).

Becoming a foreign resident

Foreign resident taxation in general

- foreign residents of Australia do not receive the tax-free threshold and are taxed at foreign resident tax rates
- foreign residents of Australia are taxable in Australia in relation to Australian sourced income only
- withholding tax rules apply for certain types of income e.g. interest, dividends and royalties
- foreign residents are assessable on capital gains in relation to ‘taxable Australian property’ (TAP)
- no longer have access to the 50% CGT discount and have also lost access to the main residence exemption

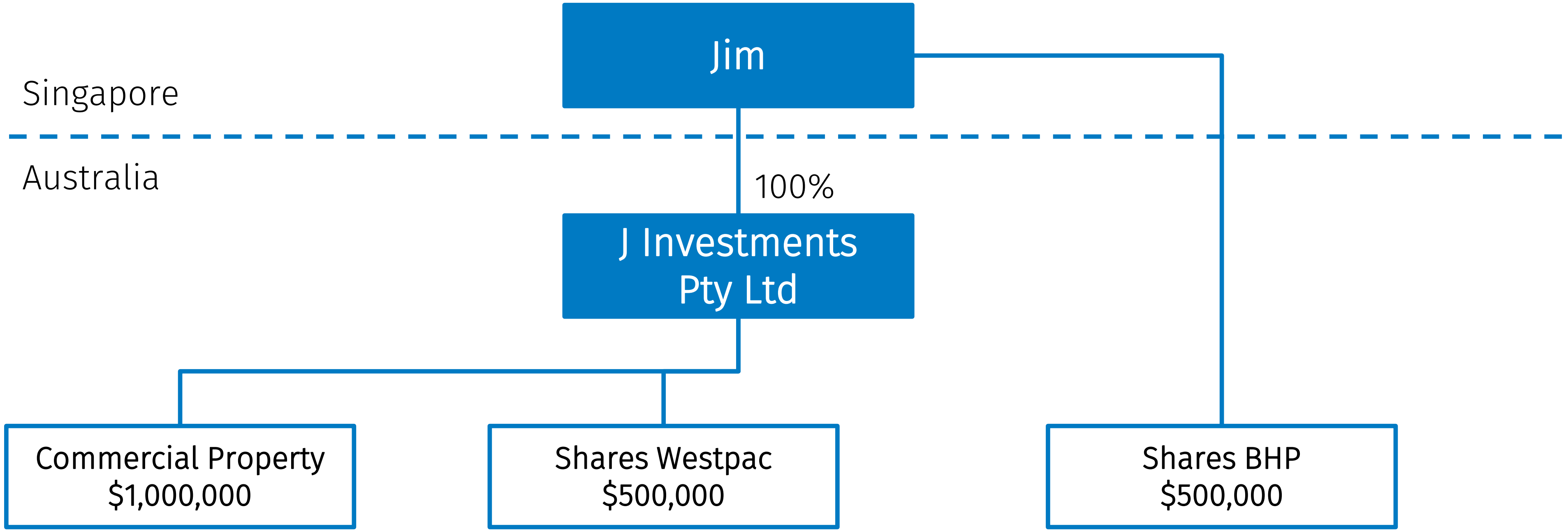
Foreign residents and CGT

- a person who is a foreign resident just before a CGT event happens, can disregard a capital gain or capital loss if it relates to a CGT asset that is not 'taxable Australian property' (TAP)
- TAP is defined to include:
  - Category 1 = taxable Australian real property (directly held);
  - Category 2 = indirect Australian real property interests (other than interests in category 5);
  - Category 3 = business assets used in an Australian PE a foreign resident (other than assets in category 1, 2 or 5);
  - Category 4 = options or rights over category 1-3 assets; and
  - Category 5 = assets where a CGT gain or loss is deferred when an entity ceases to be an Australian resident

Foreign residents – taxable Australian real property

- the term 'taxable Australian real property' (TARP) is defined in the legislation as:
  - real property situated in Australia; and
  - mining, quarrying or prospecting rights where minerals, petroleum or quarry materials are situated in Australia
- the term 'indirect Australian real property interests' means an interest that meets the following two tests:
  - the non-portfolio interest test
  - the principal asset test

Example – indirect taxable Australian real property



- Jim’s shares in J Investments Pty Ltd are indirect taxable Australian real property
- If Jim sells these shares, the capital gain is NOT excluded under Division 855
- Jim’s shares in BHP are NOT indirect taxable Australian real property – he passes the non-portfolio interest test

2024 Budget proposal – taxable Australian real property

- Consultation completed on the 2024-25 Budget measure to strengthen the foreign resident CGT regime
- Aims to broaden types of assets that foreign resident subject to CGT on
- Will include any asset with a close economic connection with Australian land
- Principle asset test to become a 365-day testing period
- Foreign residents to notify ATO before sale of assets exceeding $20 million
- Proposed to start from 1 July 2025 – will now start beginning of quarter after assent

Individual becoming non-resident – CGT Event I1

- CGT event I1 happens when a person stops being an Australian resident
- they are deemed to have disposed all non-TAP assets at market value at that time
- TAP assets for the purposes of CGT Event I1 include:
  - taxable Australian real property
  - a capital gains tax (CGT) asset used at any time in carrying on a business through a permanent establishment in Australia
  - option or right over one of the above
  - an asset covered by CGT event I1 (where a person ceases chooses to defer the CGT liability)

Individual becoming non-resident – CGT Event I1

- CGT event I1 triggered when individual stops being an Australian resident & subject to certain exceptions, the following consequences arise:
  - for any asset which is 'taxable Australian property' there are no CGT consequences, subject to certain exceptions
  - for an asset which is not taxable Australian property - but was acquired before 20 September 1985 - there are no CGT consequences
  - for any asset not covered above - a capital gain or loss may be made, calculated by reference to the cost base & its MV at time of the event

Becoming non-resident – CGT Event I1

- CGT event I1 includes a deferral mechanism that allows you to disregard making gain or loss until the earlier of:
  - a CGT event happening in relation to the asset; or
  - when you become Australian resident again
- the choice is not on an asset-by-asset basis and all non-TAP assets would be covered if the deferral is chosen
- important to consider DTA's which may limit Australia's taxing rights e.g. the Alienation of Property Article in the Australia: New Zealand DTA limits Australia's taxing rights to six- years in relation to assets affected by CGT Event I1 [Article 13 (7)]

Board of Taxation Review – Residence of individuals

- Board of Taxation has submitted its report to the Treasury in relation to its self-initiated review of the individual tax residency provisions
- Treasury conducted consultation process in July to September 2023
- recommend wholesale changes which include (but are not limited to):
  - removal of the resides and permanent place of abode tests
  - make the 183 day test the primary test
  - introduce “new” commencing and ceasing residence provisions which will make it more difficult for a person to become non-resident
  - deem tax treaty residents of other countries to be non-residents of Australia to ensure they are not eligible for concessions intended to tax residents of Australia (tax free threshold, 50% CGT discount etc.)

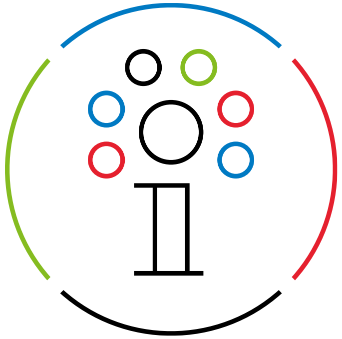
Checklist of issues for individuals

- residency matters to consider for a departing individual:
  - If resident,
    - ascertain tax residence status in foreign country (under its domestic tax law) and consider DTA implications if dual residence (if DTA exists)
    - consider the taxation of their income and gains (source-by-source) under relevant article of DTA, to determine planning opportunities
  - If non-resident,
    - consider CGT implications of their CGT assets (TAP and non-TAP)
    - generally, assessable on Australian sourced income only
    - consider the impact on their group structure e.g. SMSF, companies and trusts

Poll Question 1.

Bob, a tax resident of Australia, acquired a property in Melbourne on 1 February 2009. He became non-resident on 1 June 2019. CGT Event I1 would happen to this property on that date.

a) True
b) False



Dual Residence

Dual residence

- an individual or company can be resident in two or more places simultaneously, depending on the residence rules in each country:
  - an individual resides in one country and has a permanent abode or domicile in another
  - a company is incorporated in Australia, but has its central management in another country
- foreign income tax offset (FITO) rules may be sufficient to prevent double taxation
- double taxation agreements (DTA's) contain 'tiebreaker' rules to allocate a single place of residence to dual residents

Dual residence & DTA's

- most DTA's provide for tie breaker rules as follows:
  - resident only in the State where a permanent home is available
  - if a permanent home is available in both states or no permanent home in either state:
- resident only where centre of vital interests are located (i.e. where personal and economic relations are closer)
- if residence cannot be determined by centre of vital interests test, then need to consider habitual abode & then nationality

Note:

- Where no DTA exists and an individual is a resident of both countries - will be subject to tax laws of Australia & foreign country
- Must rely only on domestic exemptions
- If not exempt – FITO system.

DTA’s & source of income

- Australian residents are taxed on income from all sources - rules on the question of source are a mixture of statutory rules & common law principles
- different rules apply to different types of income - DTA’s may also apply to determine the source of certain income
- all DTA’s contain source rules for various types of income covered by the DTA:
  - business profits articles allocate taxing rights between countries for business profits
  - profits taxed only in the country where the business is a resident, unless the business has a PE in the other country

DTA’s & source of income – example of DTA on source

Type of income	Source	Tax treaty resident of Australia	Tax treaty resident of other treaty country
Interest	Australia	Taxable in Australia	Taxable in Australia but subject to lower rate of tax
Interest	Other treaty country	Taxable in other country but subject to lower rate of tax	Not taxable in Australia
Dividends	Australia	Taxable in Australia	Taxable in Australia but subject to lower rate of tax
Dividends	Other treaty country	Taxable in other treaty country but subject to lower rate of tax	Not taxable in Australia
Royalties	Australia	Taxable in Australia	Taxable in Australia but subject to lower rate of tax
Royalties	Other treaty country	Taxable in other treaty country but subject to lower rate of tax	Not taxable in Australia
Employment Income	Australia	Taxable in Australia	Taxable in Australia - may be exempt in certain DTAs if in other country for less than 183 days
Employment Income	Other treaty country	Taxable in other country but may be exempt in certain DTAs if in other country for less than 183 days	Taxable in other country

Checklist of issues on dual residence

- if a person is dual resident and there is a tax treaty with the relevant country:
    - consider the relevant DTA and ascertain the tax treaty tiebreaker rules
    - based on the result of the tie breaker, consider the sources of income and check whether Australia has primary (or secondary taxing rights)
    - consider withholding taxes on certain types of income (dividends, interest etc.)
    - consider the capital gains tax implications (if any)
- if a person is dual resident and there is no tax treaty with the relevant country, Australia will retain taxing rights and the individual will be subject to ordinary taxation rules - domestic FITO rules to consider

Tax Residence of Companies

Tax Residence – Companies

Australian Domestic Tax Rules

- incorporated in Australia
  - a company is a resident of Australia if it is incorporated in Australia, regardless of where the company is controlled from
- NOT incorporated in Australia
  - a company that is NOT incorporated in Australia is resident if:
    - it carries on business in Australia & has its central management & control in Australia; or
    - it carries on business in Australia and its voting power is controlled by shareholders who are Australian residents

Tax Residence – Companies

TR 2018/5: Central Management & Control

- TR 2018/5 applies from 15 March 2017 [accompanying draft PCG 2018/9 on identifying where a company's central management and control (CMC) also issued]
- finalised view on applying CMC test for company residence following decision in Bywater Investments Limited & Ors v FCT; Hua Wang Bank Berhad v FCT [2016] HCA 45
- ruling does not deal with:
  - the voting power test of company residency for foreign incorporated companies; or
  - when a company carries on a business

Tax Residence – Companies

TR 2018/5: Central Management & Control

- In Bywater Investments Limited & Ors v FCT , High Court looked to where real business of relevant company was carried on:
  - while board meetings held overseas (where directors lived)
  - each company was Australian resident because one individual (an Australian accountant) was ‘pulling all of the strings from Sydney’

Tax Residence – Companies

TR 2018/5: Central Management & Control

- Whether a company is an Australian resident under the CMC test is determined by asking 4 questions:
  1. Does the company carry on business in Australia?
  2. What does CMC mean?
  3. Who exercises CMC?
  4. Where is CMC?

Tax Residence – Companies

What does CMC mean?

- refers to control & direction of a company's operations - key element is the making of high-level decisions that:
  - set the company's general policies
  - determine the direction of its operations
  - the type of transactions it will enter

Tax Residence – Companies

What does CMC mean?

- the matters most likely to influence a court's decision, as to where those who control and direct the operations of a company do so from, are:
  - where those who exercise central management control do so, rather than where they live
  - where the governing body of the company meets
  - where the company declares and pays dividends
  - the nature of the business and whether it dictates where control and management decisions are made in practice·
  - minutes or other documents recording where high-level decisions are made

Tax Residence – Companies

- practically, for most ‘outbound’ clients, they will have companies incorporated in Australia and therefore, the companies will be considered Australian tax residents
- but, other countries may have similar rules to capture companies within their own ‘tax net’
- this means that its possible for company may be considered a tax resident of both countries (‘dual resident’)

Tax Residence – Companies

- DTA’s generally contain ‘tie breaker’ provisions to deem a company solely resident in one country
- most DTA’s use a “place of effective management” (PoEM) test which is similar to CMC
- previously, with most tax treaty countries, you could self assess PoEM but now you may be required to request a Competent Authority Determination to establish where PoEM is located

Competent Authority Determinations

- Multilateral Instrument has modified Australia's bilateral tax treaties with various countries (generally, with effect from 1 January 2019)
- multilateral instruments are a '*multilateral treaty that enables jurisdictions to swiftly modify their bilateral tax treaties to implement measures designed to better address multinational tax avoidance*'
- in light of changes, dual resident taxpayers (who are not individuals) may need to apply for a determination on their tax residence status for the purposes of the treaty
- the ATO have has issued administrative concessions for dual tax residents of Australia & New Zealand

Competent Authority Determinations

- to make determination, taxpayer’s application must be lodged in prescribed form and include relevant information / documentation supporting their proposed position
- the taxpayer can provide a ‘minimum level of supporting information and documentation’
- all information received by a Competent Authority will be provided to the other Competent Authority
- if this is not agreed upon, the taxpayer may not be entitled to any relief or exemption offered by the DTA

Competent Authority Determinations

Administrative Approach: New Zealand

- allows continued self-assessment of PoEM to reduce compliance burden on 'smaller' taxpayers and allows the ATO to focus on other arrangement which may have more material consequence
- to be eligible for the administrative approach:
  - taxpayer must an ordinary company incorporated under AU / NZ law & reasonably determine PoEM
  - taxpayer's group annual accounting income is less than AU$250m or NZ$260m

Competent Authority Determinations

Administrative Approach: New Zealand

- gross passive income < 20% of total assessable income & intangibles < 20% of total value of its assets
- taxpayers must not have been subject to compliance activity by IRD or ATO in relation to residency
- taxpayers must not be engaged in an objection, challenge, settlement or litigation with IRD or ATO

Checklist of issues on residence of companies

- The following should be considered for an "exit"
  - For companies incorporated in Australia, they will retain Australian tax resident status
  - Where the directors / shareholders are residing abroad, consider the tax residency of the company in that relevant country
  - If the company is also resident of the foreign country, consider the relevant DTA and the tie breaker test – place of effective management
  - If dual resident , a competent authority determination may be required
  - Consider ASIC / Corporations Law requirements – for example, one resident director required

Board of Taxation Review – Residence of companies

- Board of Taxation has submitted its report to the Treasury on corporate tax residency recommending 'economic connection to Australia' concept of tax residency
- 2020 Budget measure to give effect to companies incorporated offshore will be treated as tax residents where there is a 'significant economic connection to Australia'
- Test satisfied where:
  - Company's core commercial activities undertaken in Australia, and
  - Central management and control is in Australia
- Can apply from 17 March 2017, otherwise first income year after date of assent
- No draft legislation has been released on this measure

Residence of Trusts

Discretionary trusts – residence

- a Trust (that is not a Unit Trust) is a resident trust of Australia where:

  a trustee is an Australian resident, or

  the central management and control of the trust is in Australia

- under 1st limb of the definition, a trust is a resident trust in relation to an income year if one of its trustees is a resident at any time during the year of income.
- the 2nd limb of the definition requires consideration of CMC of the trust - it is therefore important to consider where decision making is made
- to maintain Australian tax residence - may consider nominating an Australian company as trustee to ensure residence test is met even if individuals are abroad making decisions

Discretionary trusts – residence

- CGT event I2 happens to all non-TAP assets and its indirect Australian real property interests (and options or rights in respect of such interests)
- the trust is taken to have disposed of the affected assets at market value when residence ceases and unlike individuals, trusts cannot defer this capital gain/loss
- non-resident trusts generally only taxable on Australian sourced income and the trustee of the trust would be liable for tax to the extent of undistributed Australian income
- capital gains and capital losses in relation to CGT assets that are not TAP are disregarded (Taxation Determination TD 2017/23)
- Any non-TAP capital gain distributed from a non-resident trust to Australian residents - s99B ITAA 1936 may apply – included in assessable income of beneficiary

Discretionary trusts – distributions to non-residents

- where Australian resident trust makes distributions to non-residents, the trustee is assessed on the distributions
- trustee is liable for tax with respect to a presently entitled beneficiary who is a non-resident at the end of the year of income [s 98(3) ITAA 1936]
- with respect to the period of non-residence, the trustee is only liable for tax in relation to Australian-sourced income
- the tax paid by the trustee under s 98(3) ITAA 1936 in relation to the non-resident beneficiary is not a final tax
- the beneficiary remains liable for Australian tax and would be entitled to a credit for the amount of tax paid by the trustee

Discretionary Trusts – distributions to non-residents

- interest and dividend income is taxed under the withholding tax rules and excluded from s98 ITAA 1936 and is not assessable to the beneficiaries.
- the withholding tax is collected from the trustee under the pay as you go withholding rules in the *Taxation Administration Act 1953*
- fully franked dividends paid to non-residents would not be subject to further taxation/withholding in Australia but important to note anti-avoidance provisions
- accordingly, care must be taken where a Trust has made distributions to non-residents and the funds are then "used" by an Australian resident – s100A ITAA 1936 may apply

Unit trusts - residence

- a unit trust is a resident trust for CGT purposes for an income year if it meets the unit trust residency requirement at any time during the year
- the separate definition for CGT purposes is important should a trust cease to be a resident trust for CGT purposes

One of these requirements was satisfied:	Any property of the unit trust was situated in Australia.	The trustee of the unit trust carried on a business in Australia.
And also one of these:	The central management and control of the unit trust was in Australia.	One or more Australian residents held more than 50% of the beneficial interests in the income or property of the trust.

DTA’s & trusts

- whether or not trusts are covered by DTA’s can depend on whether a trust is a defined ‘person’ for the purposes of the DTA
- for example, the Australia: New Zealand DTA defines the term ‘person’ includes an individual, a trust, a partnership, a company and any other body of persons;
- other DTA’s may not make reference to a trust directly but certain definitions may be wide enough to capture trusts
- for example, the United Kingdom: Australia DTA defines a person to include ‘any other body of persons’

DTA's & trusts

- if a trust is not a 'person' for the purposes of the DTA, it would not be eligible for the treaty benefits allowed by the DTA
- if a trust is a dual resident of two countries under the provisions of a DTA, generally it will come down to the 'PoEM' tie breaker
- depending on the outcome of the tie breaker, you then have to consider which country would have taxing rights in relation to the type of income (e.g. interest, dividends, capital gains etc.)

Checklist of issues for trusts

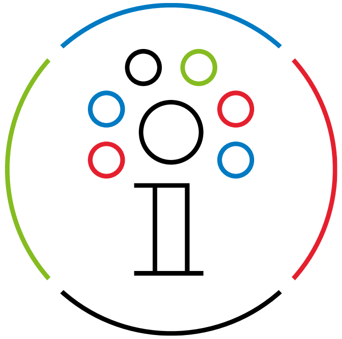
- the following issues should be considered:
  - will there be any individual Australian resident Trustees
  - if none, consider incorporating a Trustee company to ensure one resident Trustee remains
  - if Trust retains Australian residency, consider dual residency provisions based on applicable DTA
  - if Trust ceases to be an Australian resident, consider CGT issues on deemed disposal of certain types of assets

Poll Question 2.

Bob, Alex & Wendy are trustees of the BAW Trust (established in BVI). Bob becomes a tax resident of Australia. The BAW trust is therefore considered to be a tax resident of Australia.

a) True

b) False



Tax Residence of SMSF's

SMSF's – Residence

- A superannuation fund is an Australian superannuation fund at a time, and for the income year in which that time occurs, if:
  - the fund was established in Australia, or any asset of the fund is situated in Australia at that time; and
  - at that time, the central management and control (CMC) of the fund is ordinarily in Australia; and
  - at that time either the fund had no active members, or it has active members who are Australian residents and who hold at least 50% of:
    - the total market value of the fund's assets attributable to superannuation interests; or
    - the sum of the amounts that would be payable to active members if they voluntarily decided to leave the fund.

SMSF's – Residence

Established or assets in Australia

- established in Australia means the initial contribution made to establish the fund is paid to and accepted by the trustee in Australia
- if the fund was not established in Australia, it may still meet the requirement if an asset of the fund is situated in Australia

SMSF’s – Residence

CMC in Australia

- who, when and where of the strategic and high-level decision-making processes and activities of the fund which may include who formulates the investment strategy
- day to day activities (banking, acceptance of contributions) may not amount to CMC as it is not strategic in nature
- CMC can be situated outside Australia for a period of 2 years if the period of absence is temporary - if the period of absence is permanent, 2-year concession will not apply

SMSF's – Residence

Active member test

- passed if the fund has no active member - a person is not an active member if:
  - the member is a foreign resident;
  - the member is not a contributor at that time; and
  - the only contributions made to the fund for the member since the member became a foreign resident were made in respect of a time when the member was an Australian resident.
- means if a client is non-resident, this test is passed if they do not make any contributions during a period of non-residency.
- if the fund HAS active members - the 50% requirement for total fund assets or amounts payable on ceasing to be a member must be satisfied

SMSF's – Residence

- if any of the tests above are failed, fund is treated as non-complying and it would result in it not being an Australian superannuation fund - TR 2008/9 confirms:
  - a fund that ceases to be a complying superannuation fund in a particular year of income because it fails to satisfy the definition of Australian superannuation fund at a particular time faces a number of taxation consequences
  - in the income year that it becomes non-complying, it must include in its assessable income an amount equal to the total of the market values of the fund's assets - this amount is taxed at the highest marginal tax rate
- means it is essential you advise your clients prior to any permanent intended migration abroad because this cannot be "fixed" prospectively and is a question of fact

SMSF’s – Residence

- if the client intends on making superannuation contributions whilst non resident, they can set up a public fund to ensure the active member test is passed within the SMSF assuming no contributions will be made to it
- to ensure CMC is present in Australia, there are a few options available including (but not limited to):
  - giving power of attorney to local Australian tax residents who will exercise CMC;
  - appointing an approved trustee and making a fund a Small APRA fund
- alternatively, the SMSF can be wound up and the benefits can be rolled into a public fund but may not be possible where the SMSF does not have liquid assets (e.g. property)

Checklist of issues for SMSF’s

- Issues to consider at the time of “exit”:
  - does a member become a non-resident on departure
  - if non-resident, does the two–year temporary absence concession apply
  - consider the ‘active member’ market value proportion rule
  - if the concession does not apply, the fund may become non-complying by the members becoming non residents
  - consider the deed and avenues available to ensure CMC of the fund remains in Australia

Other

Foreign resident CGT withholding

- subdivision 14-D of the *Tax Administration Act 1953* contains the requirements on foreign resident capital gains withholding tax
- From 1 January 2025, where certain TARP is acquired from a foreign resident, s14-200 imposes an obligation on the purchaser of the asset to withhold 15% from the proceeds
- Before 1 January 2025, where certain TARP valued at $750,000 or more, WHT rate was 12.5%
- the withholding is paid to the ATO at the time of settlement
- this is a non-final refundable tax credit and in certain scenarios, the non-resident can vary the withholding amount to a lesser amount (e.g. carried forward losses)

Foreign resident CGT withholding

- in certain circumstances (for example, carried forward losses), the taxpayer can apply for a variation to reduce the amount to be withheld on settlement
- withholding not required in the following situations:
  - transactions before 1 January 2025 involving TARP or an indirect Australian real property interest which has a market value of less than $750,000
  - transactions conducted through a stock exchange or crossing system
  - arrangements already subject to an existing withholding obligation
  - securities lending arrangements
  - transactions involving vendors who are subject to formal insolvency or bankruptcy proceedings (in Australia or elsewhere)
  - where a clearance certificate or declaration is obtained

CGT 50% general discount

- S 115-105 ITAA 1997 denies the CGT discount where a person is a foreign (or temporary) residents of Australia for any direct gains (i.e. where they hold the CGT asset directly) occurring after 8 May 2012.
- the discount percentage is calculated in line with the requirements laid out in s 115-115 of ITAA 1997
- effectively, there are two methods to calculate the discount percentage depending on whether or not the taxpayer was resident at 8 May 2012 being
  - market value method – which preserves the CGT discount for the increase in market value from the date of purchase to 8 May 2012; or
  - apportionment method – which calculates the discount percentage based on the number of days a person was resident vs non resident

CGT 50% general discount

- the market value method is only available to individuals who were Australian tax residents at 8 May 2012
- if the individuals were foreign (temporary) residents at that date, the apportionment method must be used
- important to keep adequate records to substantiate the taxpayer's residency history along with their visa status whilst in Australia
- the ATO have issued a CGT discount worksheet which can help in calculating the reduced discount percentage for affected clients
- also important to note that dual residents may be eligible for the 50% discount

CGT main residence exemption

- foreign resident may be able to access the CGT main residence exemption if they satisfy the 'life events test', which requires:
  - that at the time of the CGT event, the person has been a foreign resident for a continuous period of six years or less (if > than six years, taxpayer is an 'excluded foreign resident')
  - during the person's period of foreign residency, one of the specified circumstances occurred or the CGT event occurred in relation to a family law matter

CGT main residence exemption

- ‘specified circumstances’ will include:
  - terminal medical condition (taxpayer, taxpayer’s spouse or child under the age of 18)
  - death (taxpayer’s spouse or child under the age of 18)
  - a CGT event in relation to a family law matter includes divorce or separation that happens under family law. If CGT event has not occurred because of family law, then unable to access main residence exemption even if matter has occurred during their period of foreign residence

Closing

- there are significant planning opportunities where you have groups migrating from Australia but it is very important to get on ‘the front foot’ during the early stages of a planned migration
- getting the basics wrong could result in an unfavorable outcome for the client resulting in a substantial tax liability
- there are various other issues besides tax which should be consider which may include estate planning , wills etc.
- do not underestimate the importance of the first question of an individual tax return – “Are you an Australian resident?” because the answer will have a substantial impact on the entire group

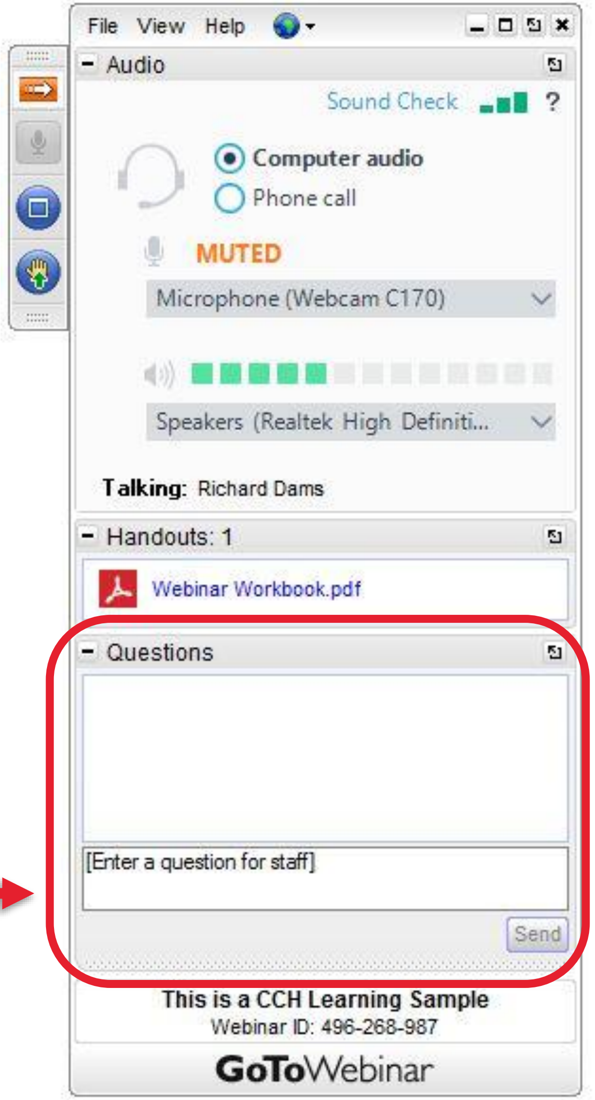
Key Takeaways from today's session

- there are significant planning opportunities where you have groups migrating from Australia, but it is very important to get on 'the front foot' during the early stages of a planned migration
- getting the basics wrong could result in an unfavourable outcome for the client resulting in a substantial tax liability
- there are various other issues besides tax which should be consider which may include estate planning , wills etc.
- do not underestimate the importance of the first question of an individual tax return – "Are you an Australian resident?" because the answer will have a substantial impact on the entire group

Questions?

Alison Wood
CCH Learning Moderator

Type your question and click Send



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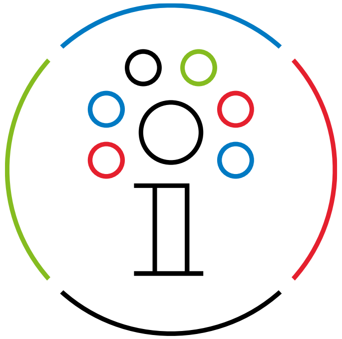

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- 12 June – Five Keys to a Healthy Life for Professionals
- 17 June – Update on SMSF Issues
- 17 June – Creating a Constructive Culture in a Defensive World
- 18 June – The Adaptive Leader – Navigating Uncertainty with Confidence
- 18 June – Excel – Handling Data

Questions?

You can type in the “Questions” box now,
Or contact me via:

Carlo Di Loreto
Partner - Tax Advisory
Crowe Australasia, an affiliate of Findex
carlo.diloreto@crowe.com.au

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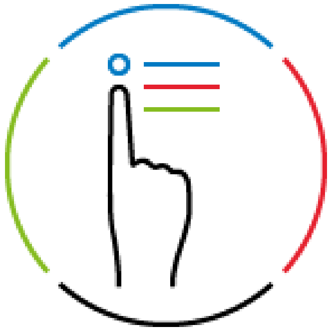

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