The Tax Summit

Session 3.3: Australian tax for foreign residents

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The Tax Summit

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1. Introduction

It's amazing to me that people will move thousands of miles away to another city, they think nothing of it. They get on a plane, boom. They're there. They live there now...[1]

Jerry Seinfeld's observation about how people's attitudes towards moving and travel over time is apt in a discussion about tax residency. Unfortunately the legal meaning is not quite as simple. The legal tests also have not kept pace with the ways in which people live their lives and move around the world as well – and whilst there is change likely on the horizon simplicity, certainty and ease in changing residency is not assured.

Tax residency as a legal concept determines the jurisdiction in which tax is levied on a person or corporate entity. [2] Where workforces are mobile and remote working becomes more possible tax residency issues arise. This paper will focus on characterization and taxation of the hypothetical 'plane-goers' (and 'boat goers') in Australia – how do we characterize them for tax purposes, and why does it matter?

First we will provide an overview of current state foreign residency, with particular focus on the legal tests to determine the residency of individuals and corporations. The tax implications for both individuals and corporations of being a foreign resident will also be discussed.

Next, some core updates to the taxation of foreign residents in recent years will be discussed. Particular attention will be given to High Court decision in *Bywater* [3] and the proposed legislative changes in the 2021-22 Federal budget to both individual and corporate residency rules which have not yet been enacted, as well as to the ATO's interpretation and Amended PCG 2018/9 which was issued on June 28 2023.

The final part of this paper considers double tax agreements. It offers an overview of new and pending double tax agreements, as well as an analysis of the tie breaker provisions using the *Pike* case as an example. Finally, it considers the interaction of double tax agreements with state taxes with a particular focus on the legality of states imposing additional levies on foreign citizens of countries with which Australia has a DTA.

The takeaways:

- Determining residency status with certainty is challenging but critical.
- The landscape is changing and whilst transitional measures are anticipated it would be prudent to be considering both the current and future state of the law.
- Seeking advice from practitioners that specialize in residency is highly recommended both before making any significant change.

[1] 'The Trip' (Part 1), *Seinfeld* (Season 4, Episode 1).

[2] See Professor R Parson, *Income taxation in Australia,* 1986, pp 4-7

[3] Commonwealth of Australia, *Budget Measures* (Budget Paper No 2, 11 May 2021), pages 21-22

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2. Tax residency – current state

In order to understand why tax residency matters, it is important to first consider the concept of residency as it exists in the tax law.

The definition of the word 'reside' is critical to the juridical understanding of residency. Indeed, in *Miller*, Latham CJ stated that there was no 'interpretation of the word 'reside' by the courts which [made] it impossible to apply the ordinary meaning of the word' in considering the taxpayer's residency.[4] Reference was made to the Oxford English Dictionary in *Miller*, and this definition continues to be used by the Commissioner of Taxation (**Commissioner**). That definition is:[5]

> *'to dwell permanently or for a considerable time, to have one's settled or usual abode, to live in or at a particular place.'*

It is this definition of 'reside' which informs the 'ordinary concept' of residency for tax law purposes.[6] To some degree, it can be said that the idea of where someone resides also assists the law in establishing a dichotomy between Australian and non-Australian tax residents.

The definition of 'resident' in section 6(1) of the *Income Tax Assessment Tax 1936* is such that there must necessarily be a corresponding 'non-resident.'[7] The *Income Tax Assessment Act 1997* provides that a 'foreign resident' is someone who is not a resident.[8] Thus, the threshold question for whether a taxpayer can be classified as a foreign resident can only be answered by reference to whether they are an Australian resident.

Section 6(1) defines a tax resident as follows:[9]

> *'**Resident'** or '**resident of Australia'** means:*
>
> *(a) a person, other than a company, who resides in Australia and includes a person:*
> *(i) whose domicile is in Australia, unless the Commissioner is satisfied that the persons place of abode is outside of Australia;*
> *(ii) who has actually been in Australia, continuously or intermittently, during more than one-half of the year of income, unless the Commissioner is satisfied that the person's usual place of abode is outside Australia and that the person does not intend to take up residence in Australia; or …*
>
> (b) *a company which is incorporated in Australia, or which, not being incorporated in Australia, carries on business in Australia, and has either its central management and control in Australia, or its voting power controlled by shareholders who are residents of Australia.*

This paper does not address or discuss in detail the additional subparagraph (a) (iii) of this definition, which classifies a member by reference to their membership of a superannuation scheme.

[4] *Commissioner of Taxation v Miller* [1946] 73 CLR 93 at [99] (Latham CJ)
[5] *Miller* at [99] c/f *Levene v Inland Revenue Commissioners* (1928) AC 217, at [222]
[6] TR 2023/1 at [17-20]
[7] *Income Tax Assessment Act 1936* (**ITAA 1936**)
[8] *Income Tax Assessment Act 1936* (**ITAA 1936**), s6(1), definition of 'non-resident'; *Income Tax Assessment Act 1997*, s995-1 definition of 'foreign resident'.
[9] ITAA 1936, s6(1), definition of 'resident'

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2.1 Individual residency

The subparagraphs in the definition set out in section 6(1)(a) establish separate tests for individuals. Relevantly, to be a resident of Australia, a person must:

- Reside in Australia (**Ordinary Concepts Test**); or
- Be 'domiciled' in Australia, unless the Commissioner is satisfied that the persons place of abode is outside of Australia (**Domicile Test**); or
- Actually have been in Australia, for more than one half an income year, unless the Commissioner is satisfied that the person's usual place of abode is outside of Australia and that the person does not intend to take residence in Australia (**183 Days Test**).

The tax residency of an individual can be different from his or her migration status.[10] If each of the legislative tests are failed the relevant individual is considered (and taxed as) a foreign resident. [11]

The primary test for residency remains the Ordinary Concepts Test.

The Commissioner has a discretion in respect of the Domicile Test and the 183 Day Test to determine that the person's usual place of abode is outside of Australia. That discretion does, to the extent that it must be exercised reasonably,[12] limit situations in which individuals who do not actually live in Australia can be considered Australian residents.[13]

The Commissioner's approach to individual residency and the tests set out in section 6(1) is outlined in TR 2023/1 – we consider this approach to be reflective of generally accepted positions and a good reflection of the current state of Australian case law on the subject matter. But as noted by Rich J in *Miller*, the question of whether a person is a resident is a question of fact and degree. [14] There is 'no single factor' that can be said to be paramount. [15] As such, each case must be considered on its own facts with a degree of judgment required to make the call that can only be exercised by those that act and advise regularly in this space.

2.1.1 Ordinary Concepts Test

Under the Ordinary Concepts Test, which has its foundations in the word 'reside', the relevant question is whether the Taxpayer's 'settled or usual abode' is Australia. The Commissioner lists factors relevant to this consideration in TR 2023/1 at [20]:

- Period of physical presence in Australia
- Intention or purpose of presence
- Behaviour whilst in Australia

[10] TR 2023/1 at [10];
[11] ITAA 1936, s6(1) definition of 'non-resident'; ITAA 1997, s995-1 definition of 'foreign resident'; see also TR 2023/1 at [3].
[12] CITE *Li* for the proposition that discretions must be exercised reasonably.
[13] CITE *Pike* for the proposition that there are limitations.
[14] TR 2023/1 at [10]; **See also:** *Commissioner of Taxation v Miller* [1946] HCA 23 (***Miller***) per Rich J: … '*the question whether a person is a resident… depends not upon the applicability of some definite rule of law but upon… whether he comes within a field which is very loosely defined. The question is ordinarily one of degree, and therefore of fact;* The ATO position that a factual inquiry is relevant is set out in TR 2023/1 at [4]
[15] TR 2023/1 at [4]

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- Family, and business or employment ties
- Maintenance and location of assets, and
- Social and living arrangements

The factors listed in TR 2023/1 (and its predecessor) cannot be said to be exhaustive and there is limited guidance as to how much weight to place on each – critically, there is no substitute for the text of the legislation.[16]

The weight given to factors will therefore vary in the individual facts of taxpayers. Recent case law cements this – the taxpayer in *Harding* was an Australian who had been living as an expatriate in the Middle East,[17] and when he left Australia, had a 'strong and fixed intention' to make a home overseas.[18] Mr Harding had worked for 15 or 16 years in the Middle East, returned to Australia for 3 years where he lived with his family, and subsequently moved to the Bahrain with a plan for his family to move there.

The Commissioner's appeal was focused on the Ordinary Concepts Test, and the Commissioner sought to rely on the taxpayer's objective connections with Australia including that Mr Harding:[19]

(a) was born in Australia and held an Australian citizenship;
(b) built a family home in Queensland close to his parents and siblings and retained ownership of the same;
(c) lived in the family home when he periodically returned to Australia;
(d) maintained his bank accounts, Medicare Account, Australian health insurance and driver's license; and
(e) made various substantial investments in Australia.

In considering the factors relied upon by the Commissioner, the Court noted that the 'quality and nature of those connections either supported a finding that Mr Harding was not a resident of Australia'.[20]

Harding demonstrates the core proposition that the application of the Ordinary Concepts Test turns fundamentally on the taxpayer's facts. For instance, whilst Mr Harding's absence in and of itself would not have resulted in non-residence.[21] The contrast between *Harding* and *Pike* – considered below as it is primarily a DTA case – does so even more starkly. So many factors were similar in each – but the tiebreaker/the differentiator was a pattern of behaviour that led to an ultimate finding Mr Harding prioritised his career over his family in contrast to the ultimate finding made for Mr Pike which was that he prioritised family over career.

2.1.2 Domicile Test

The domicile test is more formulaic than the notion of 'ordinary concepts.' It considers first whether there is a legal relationship of 'domicile' between a person and Australia.[22] The test is only relevant where that legal relationship exists.

[16] See *Dempsey v Federal Commissioner of Taxation* [2014] AATA 335, at [101] per (Logan J)
[17] *Harding v Commissioner of Taxation* [2019] FCAFC 29 (**Harding**)
[18] *Harding* at [13]
[19] *Harding* at [15]
[20] *Harding* at [64]
[21] See *Sneddon v Commissioner of Taxation [2012]* AATA 516 at [49]
[22] TR 2023/1 at [CITE]

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At law, there are three types of domicile that a person can have – being origin, choice, and dependency.[23] A taxpayer will only ever have one domicile at any time.[24] To acquire a domicile of choice, both a legal presence in a country and an intention to make an indefinite home in that country are required.[25]

Even where an Australian domicile is established by reference to any of the three categories noted above, the test as set out in section 6(1) of the ITAA 1936 requires the Commissioner to be satisfied that the individual's permanent place of abode is outside of Australia.

The relevant question is whether, despite their Australian identity, the taxpayer has 'definitely abandoned their residency in Australia and commenced living permanently overseas.' [26] Permanency does not require that the stay be indefinite or forever – but it does require an extended period of time (what constitutes such extended period differs from case to case but the vast majority of case law considering the test has settled on the relevant period being somewhere between 2 years and 3 years. Whilst the ATO acknowledge that the legal test requires an inquiry of fact and degree, a 'rule of thumb' has been established as a benchmark in TR 2023/1.[27] Broadly, 2 years is considered to be a substantial period of time to establish a permanent place of abode in the view of the Commissioner.

The concept of 'abode' is relevant to the notion of a permanent place of abode. That is that an abode need not be a single dwelling – it can be established by a pattern of behaviour that demonstrates an individual regularly stays in the same place or moves between various places within a single country.

However, the Commissioner would not consider people who move from country to country to have changed their place of abode.[28] A digital nomad with an Australian citizenship would likely remain a tax resident of Australia. There are other professions for whom breaking residency under the domicile and place of abode test can be particularly difficult also. Those professions include those in international shipping industries and the aviation industry.

The principal place of abode limb of this test relies on the Commissioner's state of satisfaction which can be taken not to be met in the absence of the Commissioner directly turning his mind to the issue – strategic consideration is therefore required as to how to deal with this at the assessment, objection and litigation phase.

2.1.3 183 Days Test

The 183 Days Test is often (but erroneously) understood to be the most simplistic test for individual residency.

The 183 Days Test is the third limb of the definition – which sets out that a taxpayer will be a resident of Australia if they have been present for 183 days or more in an income year, unless the Commissioner is satisfied that both their usual place of abode is overseas and they do not have an intention to take up residency in Australia. [29]

It is complexities around how the 183 days are to be determined and the carve outs for usual place of abode and intention to take up residency that create the often underappreciated complexity in the 183 Days Test.

[23] *Domicile Act 1982* (Cth) (**Domicile Act**); See also TR 2023/1 at [56] and [57].
[24] *Domicile Act*, s7
[25] *Domicile Act*, s10
[26] TR 2023/1 at [62]
[27] TR 2023/1 at [77]
[28] TR 2023/1 at [68]
[29] TR 2023/1 at [83]

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With respect to the day count requirement, the inclusion of the word 'intermittently' means that there is no requirement for a continuous 183 day presence in Australia. Instead, each day a person is present is included. Each part day during which travel to or from Australia is undertaken is also included as a full day.

The usual place of abode test also differs to the permanent place of abode test in some respects – as "usual" has a different meaning to "permanent" and allows greater leeway for there to be more than one "usual" place of abode at any given time than does the "permanent" requirement.

Addy is the best authority on the intent requirement.[30] In *Addy*, the taxpayer was a UK national who held an Australian working holiday visa, and was subject to Australian tax on income from her employment in Australia.[31] The taxpayer left Australia in 2017 and returned to the family home in Kent, taking all her possessions with her.[32] Whilst the High Court decision concerning double tax agreements is discussed below, the Full Federal Court commented on the 183 Days Test – the taxpayer was not considered to be a resident of Australia for the whole of the 2017 income year, due to her intention to return to the UK permanently and actual departure in 2017.[33] This issue was not in dispute in the High Court appeal.

The carve outs in this test rely on the Commissioner's state of satisfaction which can be taken not to be met in the absence of the Commissioner directly turning his mind to the issue – strategic consideration is therefore required as to how to deal with this at the assessment, objection and litigation phase.

2.1.4 How are foreign resident individuals taxed differently?

As a threshold issue, section 6-5 of the ITAA 1997 delineates between foreign and Australian residents. Section 6-5 states:[34]

> *(2) If you are an Australian resident, your assessable income includes the ordinary income you derived directly or indirectly from all sources, whether in or out of Australia during the income year.*
>
> *(3) If you are a foreign resident, your assessable income includes:*
>
> > *(a) the ordinary income you derived directly or indirectly form all Australian source during the income year; and*
> >
> > *(b) other ordinary income that a provision includes in your assessable income for the income year on some basis other than having an Australian source.*

Non-residents are treated differently in numerous ways including the following:

(a) Non-residents are not eligible for the tax free threshold. Personal income tax is instead payable at the following rates for the 2023/24 financial year:[35]

Taxable Income	Tax Payable
0 - $120,000	32.5c for each $1
$120,001 - $180,000	$39,000 + 37c for each $1 over $120,000
$180,001 +	$61,200 + 45c for each $1 over $180,000

[30] *Federal Commissioner of Taxation v Addy* [2020] FCAFC 135 (**Addy**)
[31] *Addy*, [31]-[39]
[32] *Addy*, [41]
[33] *Addy*, [312] (Steward J)
[34] ITAA 1997, ss 6-5(2); 6-5(3)
[35] ATO: Individual Income Tax Rates for Foreign Residents

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By comparison, domestic tax residents are able to avail of a tax free threshold up to $18,200 and overall more favourable rates.

(b) Non-residents are not required to pay the Medicare Levy.[36] Consequently, they do not have access to Medicare in Australia.

(c) Foreign resident's liability to CGT is determined by considering whether the relevant asset is taxable Australian property.[37] Assets that are taxable Australian property are set out in section 855-15 of the ITAA 1997. Foreign residents also do not get the benefit of most CGT concessions and exemptions. Conversely, domestic residents are subject to a far broader CGT regime.

The above are examples only, it is noted that there are various other different tax outcomes which hinge on individual residency.

2.2 Corporate Residency

The tax law establishes three alternative tests for corporate residence in Australia. [38]

(a) The company is incorporated in Australia (**Incorporation Test**); or
(b) The company 'carries on business' in Australia and either:
    a. its central management and control is in Australia (**CMC Test**); or
    b. it voting power is controlled by shareholders who are residents of Australia (**Voting Power Test**).

The Board of Taxation, in its *Review of Corporate Residency*, use the below decision tree to explain the concepts of corporate residency:[39]

[36] ITAA 1997, s251S
[37] ITAA 1997, s855-10
[38] ITAA 1936, s6(1)
[39] Board of Taxation, *Review of Corporate Residency*, p16, paragraph 2.4

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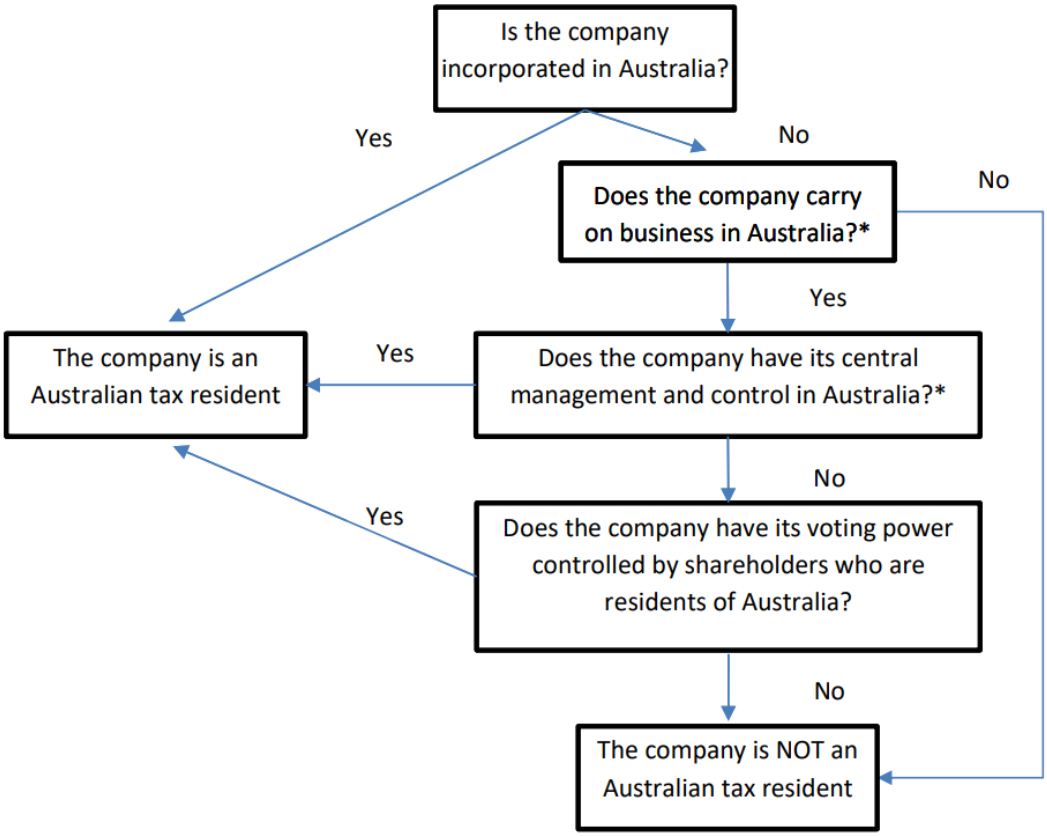

** In some circumstances, the exercise of central management and control would also constitute carrying on of business.*

This paper will focus predominantly on the CMC Test and Voting Power Test, as the Incorporation Test is a routine question of fact. Therefore, this paper is particularly relevant for foreign incorporated companies (corporations **not** incorporated in Australia) in the process of either quantifying their tax total liabilities in Australia or quantifying the operational effect of ceasing to be an Australian resident. These tests illustrate the fluidity of residency, where a change in voting power or CMC may result in a change in residency status.[40]

2.2.1 CMC Test

The concept of a place of central management and control is imported from the test adopted by the House of Lords in *De Beers Consolidated Mines Ltd v Howe* (**De Beers**) and was articulated by the majority in *Bywater* as follows:[41]

> *'[w]here the company's operations are controlled and directed and the question of where a company's operations are controlled and directed is invariably a question of fact to be determined, not according to the construction of the company's constitution, but upon a scrutiny of the course of business and trading.'*

It was further observed in *Bywater* that ordinarily, the place where directors meet will be the 'effective' place of central management and control. This principle was firmly illustrated in the finding that the central management and control of the relevant companies was in Australia in circumstances where the board of directors

[40] Chris Peadon and Annabel Burnett, 'Corporate Tax Residency', *Tax Specialist*, Vol 26 (4), April 2023, page 193

[41] *Bywater Investments Ltd v Commissioner of Taxation; Hua Wang Bank Berhad v Same* (2016) 154 ALD 30, 42 [40].

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(residents of Switzerland) had effectively (if not entirely intentionally) delegated their authority to an Australian resident.

Prior to *Bywater*, the ATO administered the residency test on the basis that there were two conditions: one that the company must carry on a business in Australia; and two that its CMC is in Australia and its voting power is controlled in Australia. This position was outlined in TR 2004/15.

It is important to note that *Bywater* demonstrates the meaning of 'effective' place of management in a limited set of real circumstances: prior to the COVID-19 pandemic. Subsequently, as travel for business, remote working and virtual board meetings are becoming ubiquitous for even relatively small corporations with international footprints, answering this question of fact becomes more difficult and, by the same token, more pertinent. Ultimately, the High Court's decision stands for the notion that directors who 'rubber stamp' decisions are not exercising management or control when the true decisions are being made by others. Further, it reinforces some of the policy objectives behind the concept of shadow directors under the *Corporations Act*.

2.2.2 Voting Power

If a foreign incorporated company fails the CMC Test, it may still be deemed an Australian resident for tax purposes if its shareholders are predominantly Australian tax residents. However, due to the sometimes-complex nature of share ownership, the assignment of rights, 'actual control' as distinct from 'control' and absent court authority on how to properly apply this test, it can be complicated for foreign incorporated companies to apply in practice to determine their residency status.

The High Court decision in *Federal Commissioner of Taxation v Commonwealth Aluminium Corporation Ltd*[42] may have some persuasive force on what amounts to 'controlling' voting power in this context. The joint judgement provided by Stephen, Mason and Wilson JJ suggests that the Voting Power Test has a primary focus on the residency status of each person who effectively controls the voting power of a company share.[43]

But there does remain ambiguity – this limb of the corporate residency test is in need of entities willing to litigate to provide more certainty.

[42] (1980) 30 ALR 449.

[43] Ibid, 460.

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3. Proposed changes

This part deals with recent key updates in the individual and corporate residency spaces.

3.1 Individual Residency: Proposed Changes

3.1.1 Background

In May 2016 the Board of Taxation (**the Board**) commenced a self-initiated review of Australia's individual tax residency rules. The Board first presented its findings to the Government in '*Review of the Income Tax Residency Rules for Individuals'* in May 2017 (**2017 Report**) concluding that the rules required modernisation. Reasons included that the current domestic residency rules:[44]

- 'no longer reflect global work practices in an increasingly global mobile labour force';[45]
- 'impose an inappropriate compliance burden on many taxpayers with relatively simple affairs as the rules are inherently uncertain to apply, include outdated concepts and rely on a 'weighting' system that leads to inconsistent outcomes, which also gives rise to integrity risks,' an example cited being employees and employers agreeing to 'extend the period of the employment/assignment in a contract, even though both parties may actually intend the actual length to be shorter';
- Adopt concepts, such as domicile, that are specific to countries with a common law basis and which are foreign to individuals from other backgrounds;
- leave open the possibility of there being residents of nowhere;
- include a superannuation test that no longer captures Government officials to which it was intended to apply; and
- 'are an increasingly prevalent area of dispute for taxpayers and the ATO given the fundamental difference in tax consequences for residents and non-residents';

In the 2017 Report the Board recommended a two-step process with separate definitions for individuals establishing and ceasing residency and bright-line day count tests followed by more detailed objective tests in complex cases.[46]

At the request of the Minister for Revenue and Financial Services, in 2018 the Board undertook a further period of consultation around the recommendations in the 2017 Report and also how Australia could draw on

[44] Board of Taxation, '*Review of the Income Tax Residency Rules for Individuals'* May 2017, pages 7 8, 15, 38 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2018/07/T307956-income-tax-res-rules.pdf.
[45] This observation was also made by the Federal Court in *Harding v FCT* [2018] FCA 837, [5].
[46] Board of Taxation, '*Review of the Income Tax Residency Rules for Individuals'* May 2017, page 7 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2018/07/T307956-income-tax-res-rules.pdf.

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residency tests in other countries.[47] The guiding principles that the Board focused on as design principles were: [48]

- **Adhesive residency** – that it should be harder to cease residency than it is to establish it.
- **Certainty** – being straightforward and providing clear and consistent outcomes for the majority.
- **Simplicity** – removing complexity through clear, reasonable rules removing subjectivity.
- **Integrity** – not making it easier for individuals that have close ties to Australia to be able to manipulate the system.

With those guiding principles in mind the new residency rules proposed by the Board are intended to re-focus assessment of individual tax residency in three ways: [49]

- Making physical presence a primary measure of residency;
- Focusing on Australian connections; and
- Adopting objective criteria and removing any requirement to test intention.

The Board's report following that further consultation '*Reforming Individual Tax Residency Rules – a model for modernisation'* was published in March 2019 (**2019 Report**). The 2019 Report, similar to the 2017 Report, recommends a two-step test with the first step being a physical presence test based on a bright line day rule, and two separate secondary tests for commencing and ceasing residency combining bright-line day count tests and factor based objective tests in complex cases. [50]

As part of the 2021/2022 budget the government announced that it will replace Australia's individual tax residency rules with a new framework based on recommendations of the 2019 Report. [51] The changes are to apply from 1 July following Royal Assent, expected to be 1 July 2022. [52] The stated objective of the new framework is to modernise the existing rules, to provide greater certainty and reduce compliance costs.[53]

[47]Board of Taxation '*Review of the Income Tax Residency Rules for Individuals Consultation Guide*' September 2018 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Consultation-Guide.pdf.
[48]Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, pages 5, 8, 9 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.
[49]Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 5 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.
[50] Board of Taxation, '*Review of the Income Tax Residency Rules for Individuals'* May 2017, page 7 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2018/07/T307956-income-tax-res-rules.pdf.
[51] Budget 2021-22 Budget Measures Budget Paper No. 2 2021-22 page 22 accessed at https://budget.gov.au/2021-22/content/bp2/download/bp2_2021-22.pdf.
[52] Budget 2021-22 Budget Measures Budget Paper No. 2 2021-22 page 22 accessed at https://budget.gov.au/2021-22/content/bp2/download/bp2_2021-22.pdf.
[53]Budget 2021-22 Budget Strategy and Outlook Budget Paper No 1, page 20 accessed at https://budget.gov.au/2021-22/content/bp1/download/bp1_2021-22.pdf.

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3.1.2 Proposed Tests

Exposure draft legislation is yet to be released – but there is a Treasury consultation paper that gives guidance as to what is to be expected. As stated above, the proposed tests adopt a two-stage approach. The proposed tests are:

Stage one tests:

- Physical presence
- Special case: government officials

Stage two tests

a. Commencing residency
b. Ceasing short term residency
c. Ceasing long term residency
d. Special case: overseas employment

Each proposed test and the interrelationships between them is considered below. A flow chart depicting the expected new domestic residency tests is included as Appendix B.

3.1.3 Stage One Tests

Physical presence

The stage one test, and primary test, is based on physical presence in Australia and will be a 'bright line test' – that is, a person who is physically present in Australia for 183 days or more in any income year will be an Australian tax resident.[54]

Parts of days are to be included as whole days.[55]

It is possible that there will be exceptions. The Boards recommendations are that any exception should: [56]

- be for circumstances beyond the individual's control such as significant illness or natural disaster;
- only be exercisable to exclude days spent in Australia; and
- require an application be made to the ATO rather than relying on self-assessment.

Special Case: Government Officials Test

There is a proposed secondary stage one bright line test for a subset of the population only. That subset of the population is overseas government officials.

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[54] Budget 2021-22 Budget Measures Budget Paper No. 2 2021-22 accessed at https://budget.gov.au/2021-22/content/bp2/download/bp2_2021-22.pdf.

[55] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 26 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf; This is also the case for each of the other day count tests.

[56] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, pages 26, 28 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.

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The test proposed is to treat all individual's deployed on foreign government services (whether Federal, State or Territory government) as residents. [57]

This test is proposed as an alternative to the current 'superannuation test' an initial purpose of which was to capture government officials but which no longer effectively does so given that government employees and officials are no longer forced to be members of Government based superannuation funds.

The inclusion of a government officials test is consistent with a number of foreign jurisdictions that have adopted that treatment for individual's deployed overseas for government services. [58]

3.1.4 Stage Two Tests

Individuals who do not meet the stage one tests will be subject to stage two tests, being tests that differ depending on whether they were Australian resident or not in the prior year, and which in line with the Board factoring the principal of adhesion into design make it more difficult to cease residency the longer an individual has been tax resident in a particular location.[59]

Commencing and Ceasing Residency Tests

The stage two tests combine day-count tests and a factor test based on four objective factors (**Factor Test**). The day count tests differ for three scenarios: commencing residency, ceasing short term residency and ceasing long term residency – long term residency defined as having been Australian resident for at least three consecutive years immediately prior. The three tests proposed are:

a. **Commencing residency:** must spend 45 days or more in Australia during the income year and satisfy the Factor Test.

Ceasing short term residency: must spend less than 45 days in the current income year in Australia and satisfy the Factor Test.

Ceasing long term residency: must spend less than 45 days in the current income year in Australia and less than 45 days in Australia in each of the two preceding income years.

Whether the 45 day specification and Factor Tests strikes the right balance are the subject of consultation – and as such could change.

As proposed the ceasing long term residency test is a significant departure from the current tests, in that it means that residency is maintained for at least two income years regardless of factors or time spent in Australia (the special case overseas employment test considered below being the only exception).

The Factor Test is of relevance for the commencing residency and ceasing short term residency tests.

[57] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 6 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.
[58] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 6 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.
[59] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 6 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.

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If less than two factors are satisfied in the ceasing short term residency scenario then the individual will be considered a non-resident for the income year; if two or more factors are satisfied for the commencing residency scenario then the individual will be considered an Australian tax resident for the income year.

The factors proposed for the Factor Test are the following connections to Australia:

b. **Right to reside permanently in Australia:** this factor is satisfied if an individual has the right to reside permanently in Australia for immigration purposes and includes rights by way of permanent visa or citizenship. Individuals on transitional or temporary visas will not satisfy this factor.

Australian accommodation: this factor is satisfied if the individual has an arrangement to access accommodation in Australia at any time during an income year. The right need not be a legal right but it must relate to identifiable premises at any point in the income year and must be more than a mere expectation that for example family members would make their residences available. It is also recommended that the accommodation must have the nature of residential accommodation and therefore not include hotels or over short term lodging arrangements.[60]

Australian family: the relationships of relevance are an individual's spouse and children, this factor being satisfied if an individual's spouse or any of their children under 18 years of age are generally located in Australia at any point during an income year.

Australian economic interests: an individual will have Australian economic connections where they are employed in Australia, actively participate in carrying on a business in Australia or, directly or indirectly, have interests in certain Australian assets. With respect to the carrying on a business limb the Board's recommendation is that directorship of an Australian company not automatically satisfy the test but that the involvement with a business should be a relatively low threshold, that individuals that are trustees of a trust that carries on business in Australia should satisfy the test and that employees of businesses should be excluded from the factor as the employment limb is more applicable to their circumstance.[61] The assets of relevance for that limb are: taxable Australian property, bank accounts with Australian banks with significant cash deposits, interests in family trusts (determined by reference to the family trust election family group) and receipt of Australian social security payments in the preceding year.[62] Interests in foreign pension funds that hold taxable Australian property should not be included, and Australian accommodation that satisfies the Australian accommodation factor is to be excluded from consideration under the test[63] On the other hand interests in foreign managed investment vehicles entitling the holder on returns on taxable Australian property should satisfy the test, tracing to identify indirect interests

[60] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 85 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.
[61] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 93 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.
[62] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 94 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.
[63] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 95 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.

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should not be limited, and interests in Australian superannuation funds can be included if the individual is a contributing member or drawing a pension. [64]

The Factor Test will result in different outcomes compared to the existing residency tests.

A key difference between the Factor Test and the existing resides, permanent place of abode and usual place of abode tests is that the Factor Test focuses solely on the individual's connection with Australia (subject to a small number of specific exceptions) and as such does not require a weighting or assessment of whether that connection is stronger or weaker than any connection that exists elsewhere in the world. [65] As such the new tests are not proposed to have regard to days overseas, family overseas, foreign accommodation, economic or financial interests.[66]

The singular focus on Australian connection increases the likelihood of individuals being assessed as Australian resident under Australia's domestic rules and also resident of another country under that countries residency rules, making either the DTA tiebreaker tests or foreign tax offset provisions of increasing relevance.

Also unlike the existing domestic residency tests, the Factor Test does not test intention (either objectively or subjectively) – the factors are either satisfied or they are not.

Harding is an example of a case in which the conclusion as to domestic Australian residency would have differed due to the above differences. Whilst in that case the Full Federal Court determined Mr Harding was a non-resident due to his intent under the existing domestic residency rules, had the Factor Test instead applied he would have been found to meet all four factors and to therefore have been an Australian resident based on his having obtained permanent resident status, owning a home in which his family lived and staying in that home when in Australia, his family being in Australia and his having bank accounts and the house in Australia.

3.1.5 Special Case: Overseas Employment Test

There is also a proposed stage two test that applies only to a subset of the population. The subset of the population to which it applies is expatriate employees that have been Australian resident for at least three consecutive years immediately prior to commencing an overseas assignment. It is intended to replace and streamline the ceasing residency tests for long term expatriate employees. [67]

The proposed overseas employment test would enable individuals that have been Australian resident for at least three consecutive years immediately prior to commencing an overseas assignment to become non-resident if they also meet the following conditions:

a. being employed overseas with an employment period of over two years from commencement; and
b. having accommodation available in the place of employment for the entire employment period; and
c. spending less than 45 days in Australian in each income year of the employment period.

As proposed, the rule is likely to lead to expatriate employees having different residency status to other members of their family that move overseas with them in at least the first two years outside of Australia. That

[64] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 95 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.
[65] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 11 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.
[66] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 11 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.
[67] Board of Taxation, '*Reforming Individual Tax Residency Rules – A Model for Modernisation'* March 2019, page 6 accessed at https://taxboard.gov.au/sites/taxboard.gov.au/files/migrated/2019/12/Tax-Residency-Report.pdf.

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is because those other family members would remain subject to the ceasing long term residency test to determine their residency status if they too were Australian resident for at least three consecutive years immediately prior to moving overseas.

Temporary Residents

Temporary resident rules are proposed to continue operating, and potentially be expanded to a wider class of visa holder, to enable holders (generally visitors, international students, visiting professors, authors, entertainers and corporate executives) to have their foreign income exempt from Australian taxes.

Individual Resident in Multiple Countries

Individuals can be resident in more than one country at the same time. [68] Where an individual has competing claims of residency in other countries, these will continued to be resolved under double tax treaty alignment provisions and foreign income tax offset rules.

The Board of Tax proposed a change to include a domestic tax provision providing that where an Australian is treated as a resident of another country under one of Australia's DTA's the individual should also be treated as a 'non-resident' for domestic tax law purposes for the part of the income year to which that conclusion is applicable. The Treasury consultation paper indicates that change will not be implemented – and as such there will continue to be differences between how domestic non-residents and treaty non-residents are taxed in Australia.

3.1.6 Corporate Residency Update: Amended PCG 2018/9

A. Background

Prior to the decision in *Bywater,* the position on the definition of corporate residency was reflected in TR 2004/15. It was understood that section 6(1) of the ITAA 1936 imposed separate requirements for foreign incorporated companies to be considered Australian tax residents being:[69]

(a) it carry on its business in Australia **and**
(b) have either:
    (i) its central management and control in Australia, or
    (ii) its voting power controlled by Australian resident shareholders.

The *Bywater* decision was widely understood to have held that the location of a company's central management and control is to be determined having regard to the factual reality around who actually makes decisions as opposed to legal constructs based on who by reason of their position holds that authority. In the authors opinion that interpretation remains open to debate. *Bywater* was a decision based on an extreme fact pattern and near total relinquishment of decision making authority by directors to a person not formally holding the office of director. In the context of the extreme facts the decision was perhaps not surprising. But there are other older authorities that have espoused different views - such as *Esquire Nominees.*[70] *Esquire Nominees* was a case in which there was similarly near total relinquishment of decision making authority to a person not holding formal office. But the difference was that the individuals that purported to relinquish that

[68] *Levene v Commissioner of Inland Revenue* (1928) 13 TC 486.
[69] ITAA section 6(1); TR 2004/15 at [5]
[70]

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control held office as trustees and as such the Court concluded that it was ineffective and that the trustees still had ultimate responsibility for decisions made due to the fiduciary duties they each owed to the trusts beneficiaries. Therefore, central management and control was still determined by where the trustees were located and not where the other decision maker was located.

Following the *Bywater* decision, the Commissioner withdrew TR 2004/15 and issued TR 2018/5 and PCG 2018/9 (**2018 Guidance**) which set out the ATO position with regards to the CMC Test. [71] The 2018 Guidance reflects the understanding that if a company has its central management and control in Australia, it necessarily carries on a business in Australia for the purposes of establishing residency. There are other cases cited as also supporting this proposition including *Malayan Shipping*.

In response to *Bywater* and the Board of Taxation's report titled 'Review of Corporate Tax Residency', and the Morrison Government announced retrospective amendments to adopt the Board's recommendations.

The proposed amendments sought to "amend the law to provide that a company that is incorporated offshore will be treated as an Australian tax resident if it has a 'significant economic connection to Australia."[72] The proposed test was a reversion to the pre-*Bywater* position and would be "satisfied where both the company's core commercial activities are undertaken in Australia and its central management and control is in Australia."[73]

PCG 2018/9 contained a 'transitional compliance' approach, which has been extended in anticipation of the announced changes which have not been enacted since the change of government in 2022. The transitional period was most recently extended for companies impacted in their efforts to change their governance arrangements within the original timeframe, between and including 15 March 2017 to 30 June 2019, to 30 June 2023.

To be eligible for this treatment, immediately prior to the withdrawal of Taxation Ruling TR 2004/15, the following must apply to the foreign incorporated company:[74]

(a) it relied on TR 2004/15 and on that basis it was not a resident of Australia;
(b) it had not undertaken or entered into either:
    (i) any artificial or contrived arrangements that affected the location of its central management and control, or
    (ii) any tax avoidance scheme whose outcome depends, in whole or part, on it being a non-resident;
(c) it is an ordinary company incorporated under a foreign equivalent to the Corporations Act and is not a foreign hybrid within the meaning of section 830-5 of the ITAA 1997; and
(d) it would become a resident under the CMC Test of residency under TR 2018/5, solely because its central management and control is located in Australia,

Where foreign incorporation companies meet the above criteria, the Commissioner would not review the residency status of a foreign incorporated company provided that, during the transitional period, it:[75]

(a) changes its governance arrangements, so that its central management and control is exercised outside Australia by the end of the transitional period;
(b) does not commence carrying on business in Australia (other than because its central management and control is exercised in Australia); and
(c) does not undertake or enter:

[71] TR 2018/5
[72] CITE
[73] CITE
[74] PCG 2018/9DC1 at [102].
[75] PCG 2018/9DC1 at [103].

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(i) any artificial or contrived arrangements that affect the location of its central management and control (e.g., if board meetings are undertaken in another country where that company has a substantive commercial presence, merely flying Australian directors overseas to attend those board meetings would not alone be regarded as artificial or contrived); or

(ii) any tax avoidance scheme whose outcome depends, in whole or part, on whether it is a resident or non-resident.

PCG 2018/9 DCI

On 28 June 2023, the Commissioner issued an amended version of PCG 2018/9 entitled PCG 2018/9 DC1 (**Amended PCG**). The Amended PCG puts taxpayers on notice that it will seek to enforce the *Bywater* position – the transitional compliance approach having expired on 30 June 2023. It sets out factors which the ATO will have regard in applying the CMC Test including:

(a) board minutes of a company showing where high level decisions were made and who made them;[76]
(b) the scale of the business, which may distinguish management and control from every day transactions;[77]
(c) identification of the people who are in substance making high level decisions which constitute 'central management and control', which might result in holding companies having such power if the directors of its subsidiary act as its mouthpiece;[78]
(d) corporate group activities and the extent to which directors of subsidiaries in a corporate exercise discretion or are also directors of an ultimate Australian-resident holding company;[79] and
(e) the multi-locational origin of decisions, which encourages foreign incorporated companies to consider whether the majority of their decisions are made.[80]

Given that the proposed changes are unlikely to be enacted, the Amended PCG essentially affirms the Commissioner's approach to *Bywater* and provides a frame of reference for foreign incorporated companies to assess their risk of audit or review of their residency status.

Some examples of moderate and high risk features identified by the Commissioner include where a foreign incorporated company:

(a) states that its directors, who spend majority of their time in Australia, make high level decisions in Australia when the structure of the business or roles of those directors indicates otherwise;
(b) has lapses in directional standards or corporate governance, which might include a haphazard approach to accurately minuting board meetings;
(c) has circumstances relating to the exercise of central management and control without commercial backing;
(d) appears to have 'shadow directors';
(e) is not a resident of a foreign jurisdiction and does not consider itself a resident of Australia;
(f) purports to be a foreign resident but its tax and profit outcomes would indicate otherwise;
(g) undertakes or enters an artificial or contrived arrangement affecting the location of its central management and control;
(h) has a tax avoidance scheme , whose outcome depends on the location of the company's residence;
(i) has arrangements that abuse board processes (e.g., backdating of documents or falsifying the attendance of any board member); or

[76] PCG 2019/DC1 at [11].
[77] PGC 2019/DC1 at [15] - [17].
[78] PCG 2019/DC1 at [28], [33] - [35], [50].
[79] PCG 2019/DC1 at [39] - [40].
[80] PCG 2019/DC1 at [73] - [80].

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(j) has no evidence of substantive decision making in the foreign jurisdiction it claims to be resident of.

Clearly there has been some tension between the Commissioner's view and the Board of Taxation's recommendations which the Morrison Government sought to adopt. The Amended PCG has a significant potential impact of reclassifying companies incorporated overseas as Australian residents.

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4. Double Tax Agreements

Where an individual or company is a tax resident of multiple countries when applying the domestic residency definitions applicable on those countries, it is necessary to consider how double tax agreement (**DTA**) provisions apply.

There are various DTA residency tests under the DTA's to which Australia is a party. Not all DTA's contain the same tests, and even where the wording of the tests have similarities the interpretation could differ given the jurisdictions between which the test is stated to apply and the domestic rules of those countries. Further, the manner in which the tests cascade and which of the tests is to be given priority over the other can vary between DTAs. For those reasons the comments which follow are general in nature only.

Common tests found in DTA tiebreaker provisions, are tests based on where individuals have

a. A permanent home;
b. A habitual abode; and
c. Personal and economic ties

It is worth noting that many DTA's also have different treatment for different categories of income in this situation – including by way of example employment, royalty and dividend income. As such, it is possible that treaty tax residents are taxed differently to domestic tax residents. Treaty non-residents are also taxed differently to domestic non-residents as the former gets the benefit of some tax concessions, including CGT main residence exemptions that the later does not. Early proposals for law change indicated an intention for this to change going forward for individuals – but the most recent consultation paper released suggests that it will not.

Section 4.1 below provides an overview of recent and pending DTA's which Australia is or will likely be a party to – highlighting key discussion points in these. Section 4.2 considers the application of the common residency tests in the context of the recent Full Federal Court decision in *Pike*. Section 4.3 discusses the interaction between DTA's and state taxes.

4.1 New/Pending DTA's

The most recent DTA which Australia entered into is with Israel.[81] The Israel DTA was signed in March 2019 and came into force for residency purposes from 1 July 2020. The key taxing provisions of the DTA that turn on either individual or corporate tax residency are outlined below. We note that the core provisions in the Israel DTA cover the full gamut of issues that are dealt with in most (if not all) DTA's to which Australia is a party.

(a) **Taxation of business profits:** the Israel DTA includes provisions, including in article 7, to determine the taxation of business profits, ensuring that profits are only taxed in the country where the business is physically located.[82] This helps to avoid scenarios where a company may be subject to taxation on the same profits in both countries – although complexity can arise as to what physical location means where presence in each country is similar.
(b) **Dividends:** The Israel DTA typically reduces the withholding tax rate on dividends paid between the two countries, often to a lower rate than the standard domestic tax rate,[83] which acts to encourage

[81] *Convention between the Government of Australia and the Government of the State of Israel for the Elimination of Double Taxation with respect to taxes on income and the prevention of tax evasion and avoidance* (**Israel DTA**)
[82] Israel DTA, Article 7(1)
[83] Note that the standard dividend withholding rate for unfranked dividends in Australia is 30%.

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cross border investment. If the beneficial recipient of a dividend from one country is a resident of the other country, the withholding rate would be:[84]

i. 5% of the gross amount of the dividend if the recipient is a company (other than a REIT which is a resident of Israel), which directly holds at least 10% of the voting power in company paying the dividends over a 365 day period; or
ii. 15% of the gross amount of the dividend in all other cases.

(c) **Interest:** a maximum withholding tax rate on interest payments to residents of the other country as follows:[85]

i. no tax for interest derived from government and central banks;
ii. 5% for interest derived by certain pension funds and financial institutions; and
iii. 10% for all other interest payments

(d) **Royalties:** There is a reduced rate of withholding required for royalty payments (5%) paid by a resident on one state to a resident of another (relevant to IP rights such as patents, trademarks, or copyrights).[86]

(e) **Capital Gains:** There are provisions which relate to the taxation of capital gains – in particular those arising from the sale of 'immovable property',[87] which impacts application and jurisdiction of capital gains tax on gains realised from industries such as real estate and mining.

(f) **Employment:** The Israel DTA contains rules regarding the taxation of income earned by employees and independent contractors. The DTA provides that employees will typically pay tax on their salary or wages in the country in which they are employed (ie. where the income is sourced).[88] There is an exception which are informed by the rules for individual residency (discussed above) which, if they apply, mean that tax on income would be payable in the taxpayer's country of residence, irrespective of the source. This happens where:[89]

i. the taxpayer is in the source country for less than 183 days; and
ii. the remuneration is paid by an employer who is not a resident of the source country; and
iii. the remuneration is not from the employer's permanent establishment in the source country

Whilst the Israel DTA offers clear benefits for cross-border transactions, there are pitfalls that taxpayers in both countries should bear in mind, in particular, the 'deemed source rule.' This is not unique to the Israel DTA, and taxpayers seeking to rely on any such treaty should be aware of this.

The 'deemed source rule' is used in DTA's to determine the source of certain types of income for tax purposes. The source of income is essential to determining which country has the right to tax that income, including under a DTA. To prevent double taxation and allocate taxing rights, the deemed source rule creates a legal fiction – to treat the income as if it has a specific source for tax purposes, even where, under domestic laws, it may be considered to have a different source.

Most of Australia's tax treaties do include a deemed source rule, which was recently litigated in *Satyam Computer Services*.[90] In that case, amounts paid by Australian consumers of IT services provided by the taxpayer's employees in India were considered to be 'royalties' under the double tax agreement with India, but not under the Australian domestic law. It was held that these amounts were liable to tax in Australia as article 23 of the double tax agreement deemed the source of the royalties to be Australia.

[84] Israel DTA, Articles 10(1), 10(2)
[85] Israel DTA, Article 11
[86] Israel DTA, Articles 12(1), 12(2)
[87] Israel DTA, Article 6
[88] Israel DTA, Article 14(1)
[89] Israel DTA, Article 14(2)
[90] *Satyam Computer Services Limited v Commissioner of Taxation* [2018] FCAFC 172 (*Satyam Computer Services*)

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An example of a deemed source rule in the Israel DTA is in respect of director fees. Article 15 states:

> *Director's fees and other similar payments derived by a resident of a Contracting State in that person's capacity as a member of the board of directors of a company which is a resident of the other Contracting State may be taxed in that other State.*

Director fees paid to an Israeli resident director of an Australian company, who lives and works in Israel, might not typically be taxable in Australia. However, Article 15 allows Australia the right to tax those director fees as they are deemed as having an Australian source. Although there would in most cases be double tax relief, there is an additional compliance hurdle for taxpayers to consider.

4.2 The tiebreaker tests – *Pike*

Pike[91] is a recent Full Federal Court decision in which DTA tiebreaker residency tests were considered – in that case the tests set out in Article 4(3) of the Australia Thailand DTA.[92] The tiebreaker tests are similarly set out in Article 4(2) of the Israel DTA.

Broadly the facts of that case were that:

- Mr Pike was born in Zimbabwe in 1972.
- Mr Pike was in a long term de-facto relationship with Ms Thornicroft, also born in Zimbabwe.
- Together Mr Pike and Ms Thornicroft had two sons born in 1995 and 1999.
- Mr Pike developed a career in the tobacco industry in Zimbabwe.
- In 2004 Mr Pike and his family left Zimbabwe due to the economic crisis and food shortages.
- Mr Pike and Ms Thornicroft retained ownership of a home in Zimbabwe.
- Australia was chosen as a destination as Ms Thornicroft was offered a job in Australia.
- In February 2005 Ms Thornicroft was granted a 457 visa and Mr Pike and their sons were also granted visas allowing them to live in Australia.
- On 17 March 2005 the family travelled to Australia. Mr Pike and Ms Thornicroft took out a lease of a property in Brisbane in their joint names.
- Mr Pike established an Australian bank account in his own name when the family first moved to Australia and, shortly after that, a joint Australian bank account with Ms Thornicroft. He also obtained a credit card with an Australian bank.
- Mr Pike returned to Zimbabwe shortly after arrival in Australia to serve out his existing employment contract and sell some assets.

[91] *FCT v Pike* [2020] FCAFC 158.

[92] Agreement between Australia and the Kingdom of Thailand for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income, signed 31 August 1989, [1989] ATS 36.

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- Mr Pike sought employment in the tobacco industry in Australia but was unable to find any as the Australian tobacco industry was contracting by that time. He was also unable to enrol in tertiary studies. He therefore looked at international contracts.
- In March 2006 Mr Pike travelled to Thailand having become aware of an opportunity there and in late 2006 was offered and commenced a role based in Thailand. His initial contract was for six months, however in June 2006 he entered into a further contract for an indefinite duration.
- Mr Pike was granted a work visa by the Thai government, he opened a bank account in Thailand and had his salary paid into that account. Mr Pike continued to be based in Thailand for his employment for the next 8 years.
- Mr Pike returned to Australia to visit his family but circumstance required he spend most of his time in Thailand.
- Mr Pike occupied a number of rented apartments or cottage accommodation in Thailand during that period which he furnished and which his family could stay at when they visited. Mr Pike also joint local sporting clubs.
- Mr Pike continued to jointly rent Australian properties with Ms Thornicroft through the period he was employed in Thailand. In September 2010 Ms Thornicroft and Mr Pike purchased a property in Australia with the intention of building a home and sold their Zimbabwe house. It was not possible to build the house and the Australian land was sold in 2013.
- Ms Thornicroft ceased working in 2011 due to injury.
- Both before and after Ms Thornicroft's injury Mr Pike supported her and their sons by regular financial contributions. Mr Pike also supported his parents and brother who were based in Zimbabwe.
- Ms Thornicroft, Mr Pike and their sons were granted permanent residency in Australia in 2009.
- In August 2010 Ms Thornicroft and their sons obtained Australian citizenship.
- Mr Pike made enquiries about Australian citizenship in 2010 but did not make an application for Australian citizenship in April 2013. When he did so he gave as his residential address the then rented family home at Taringa. He also specified as his home telephone number the landline (inferentially) connected to those premises. In contrast, his mobile telephone number was his Thai number and the contact email address he specified was his Thai work email address. He specified his then current citizenship as Zimbabwean. He also stated on the application that he intended to be absent from Australia for work for six weeks over the forthcoming 12 months. His application was refused. He made a further application and was successful in October 2013. He was issued with an Australian passport in 2014. He did not renounce his Zimbabwe citizenship.
- Mr Pike relocated to Tanzania for employment in 2014 and then to Dubai in 2016.
- The number of days Mr Pike spent in Australia in each year were as follows:

Income year	Days spent in Australia	Percentage of time spent in Australia

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2008	76	20%
2009	155	42%
2010	97	27%
2011	109	30%
2012	102	28%
2013	86	23%
2014	123	33%
2015	32	8%
2016	44	12%
2017	77	21%

Article 4(3) of the Australia Thailand DTA provided:

> Where by reason of the preceding provisions, an individual is resident of both Contracting States, the status of the person shall be determined in accordance with the following rules, applied in the order in which they are set out:
>
> (a) the person shall be deemed to be a resident solely of the Contracting State in which a permanent home is available to the person;
>
> (b) if a permanent home is available to the person in both Contracting States, or in neither of them, the person shall be deemed to be a resident solely of the Contracting State in which the person has an habitual abode;
>
> (c) if the person has an habitual abode in both Contracting States, or in neither of them, the person shall be deemed to be a resident solely of the Contracting State with which the person's personal and economic relations are the closer.

Article 4(4) provided:

> For the purposes of the last preceding paragraph, an individual's citizenship or nationality of a Contracting State shall be a factor in determining the degree of the person's personal and economic relations with that Contracting State.

Permanent Home

Applying Article 4(3) paragraph (a) it was concluded that Mr Pike had a permanent home in both Thailand and Australia – being the properties that he rented in Thailand and those that he rented jointly with Ms Thornicroft in Australia.

Habitual Abode

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The habitual abode test in paragraph (b) became relevant because permanent home (paragraph (a)) was inconclusive.

The habitual abode test does not specify the period of time over which the comparison must be made, but there are authorities in over to indicate that it can be a period spanning several income years.

Applying the habitual abode test it was again concluded that Mr Pike had a habitual abode in both Thailand and Australia.

To this end it was stated that 'Mr Pike's life routine had two aspects. One was that as, when and for as long as necessary, and always for more than half the year, he worked in or from Thailand and occupied there premises which he had made his home. The other was that as, when and for as long as possible, he lived with his family in Australia. The length of time as between each country for these purposes varied from year to year but, in relation to each country, he had an established residential habit.'[93]

The conclusion in *Pike* is consistent with OECD commentary. For example, the OECD commentary stated 'the [habitual abode] test will not be satisfied by simply determining in which of the two Contracting States the individual has spent more days during that period ... "habitual abode" [is] a notion that refers to the frequency, duration and regularity of stays that are part of the settled routine of an individual's life and are therefore more than transient ... it is possible for an individual to have an habitual abode in the two States, which would be the case if the individual was customarily or usually present in each State during the relevant period, regardless of the fact that he has spent more days in one State than in the other.'[94]

A consequence of this is that whilst the proposed new domestic residency tests aim to remove subjective criteria, criteria based on intent and wide ranging holistic weighting of competing factors from determination of residency status such aspects will remain of relevance because they will be necessary to consider where the DTA tiebreaker conditions become relevant.

Personal and economic ties

Paragraph (c) of Article 4(3) was relevant in *Pike* because both the permanent home (paragraph (a)) and habitual abode (paragraph (b)) tests were inconclusive.

As to how the personal and economic ties test applied the Full Federal Court concluded that it is a 'composite test and in each case it will be a matter of fact and degree as to whether a taxpayer's personal and economic relations, viewed as a whole, support ties closer to one contracting state over the other contracting state.'[95]

Applying this test to the whole of Mr Pike's facts it was ultimately concluded that his personal and economic ties were closer to Thailand, resulting in a conclusion he was a Thai resident under the DTA tiebreaker tests.

As with the conclusion on how the habitual abode test operates, a consequence of this is that whilst the proposed new domestic residency tests aim to remove subjective criteria, criteria based on intent and wide ranging holistic weighting of competing factors from determination of residency status such aspects will remain of relevance because they will be necessary to consider where the DTA tiebreaker conditions become relevant.

[93] *Pike v Commissioner of Taxation* [2019] FCA 2185, [97].
[94] 2017 OECD Commentary; *Pike v Commissioner of Taxation* [2019] FCA 2185, [98].
[95] *FCT v Pike* [2020] FCAFC 158, [39].

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4.3 DTA's and State Taxes

In *Addy*,[96] it was held that the 'backpacker tax' contravened the non-discrimination article contained in the DTA between Australia and the UK (**UK DTA**).

Since that decision all tax regulators in Australia have been considering how it applies to the taxes under their administration, with some State Revenue Offices accepting that it applies to State taxes under their jurisdiction whilst others have determined that it does not and a few have remained silent.

To give context to how the decision in *Addy* came about the UK DTA contains the following non-discrimination provision in article 25(1):

> *Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected.*

The dispute in *Addy* centred around whether the tax-free threshold applied as it would to Australian tax residents, or the threshold for working holiday makers under the *Income Tax Rates Act 1986* (Cth) would apply.[97] The Full Federal Court and the High Court held that Addy was an Australian tax resident. The High Court held that the 'backpacker tax' could not apply to the taxpayer as it contravened the non-discrimination provision in the UK DTA. The Court held:

> *The question is whether that more burdensome taxation was imposed on Ms Addy owing to her nationality. The short answer is 'yes'. When the position of Ms Addy is compared with that of an Australian national, as it must be, that is the only conclusion which may be drawn. Pt iii of Sch 7 to the Rates Act was applied to Ms Addy, a national of the United Kingdom. Ms Addy's circumstances in the 2017 income year including that of her residency in Australia for taxation purposes were relevantly the same as an Australian national. She did the same kind of work and earned the same amount of income from the same income source: yet an Australian national was required by Pt I of Sch 7 to the Rates Act to pay less tax. In contravention of Art 25(1) of the United Kingdom convention, the more burdensome taxation was imposed on Ms Addy owning her nationality and, for that reason, the tax rates in Pt III of Sch 7 did not apply to Ms Addy in the 2017 income year.*

It is possible that non-discrimination articles do extend to state taxes, though this issue has not been litigated. Various state revenue authorities levy an additional rate of duty or surcharge in respect of acquisition or holding real property by a foreign person (individual, company or trust).[98]

In February 2023, Revenue NSW announced that surcharge purchaser duty and surcharge land tax was incorrectly levied in respect of citizens of New Zealand, Finland, Germany, India, Japan, Norway, South Africa, and Switzerland.[99] It has been accepted that this mistake arose due to inconsistencies between levying surcharge duty and the DTA's between Australia and those countries which contain non-discrimination provisions. Refunds may be available for affected taxpayers who paid surcharge purchaser duty or surcharge land tax on or after 1 January 2021.

Despite often harmonious state tax provisions, other states and territories have not adopted the NSW position and continues to apply additional duty and land tax to all foreign purchasers. The author's view is that this is very much open to challenge and may conflict with the High Court's decision in *Addy*. Foreign purchasers or

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[96] *Addy v Commissioner of Taxation* [2021] HCA 34

[97] *Income Tax Rates Act 1986* (Cth), Schedule 7, Part III, table item 1.

[98] **For example:** Foreign Purchaser Additional Duty and Absentee Owner Surcharge levied in Victoria.

[99] https://www.revenue.nsw.gov.au/taxes-duties-levies-royalties/foreign-buyers-and-land-owners/international-tax-treaties

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owners of property should seek advice in relation to any relevant tax treaties (particularly those noted above). In such a situation, the tests for residency and provisions in DTA's such as tiebreaker provisions, will have a heightened relevance.

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