Heading overseas to work? Beware of your Tax Residency Status

Thousands of Australians head offshore each year to expand their horizons and a lucky few will fund their adventure by working overseas. Some may live overseas and work for an extended period, but there can often be confusion about the tax implications for taxpayers who take advantage of such offshore opportunities.

WHY IS TAX RESIDENCY IMPORTANT?

A person who is a “resident” for Australian tax purposes is taxed on their Australian sourced and worldwide income, whereas a person classed as a “non-resident” is taxed only on Australian sourced income.

Further, an individual who is a non-resident is not eligible for the $18,200 tax-free threshold, so all assessable income is taxed right from the first dollar. There are also variances in the marginal tax rates applied.

In cases where an Australian individual goes overseas for employment, even for some years, the individual’s tax residency status is a key factor in how much tax that person is required to pay in Australia. Another factor to keep in mind is the tax law of the country in question, or whether there exists a “double taxation agreement”.

A double taxation agreement sets out which country has the rights to tax each type of income that may be earned. This is to minimise the chances of the same income being taxed in Australia and being taxed in the other country under their tax laws.

The rules in these agreements generally take precedence over the local tax laws of each country. Where the agreement gives the other country the right to impose tax, the income earner is subject to the taxation laws of that country. It is important to know which countries have such agreements, and the relevant outcomes, so consult this office should you have questions.

In the case where an Australian individual takes up a post overseas but retains a domicile in Australia, the Australian Taxation Office is likely to consider that the taxpayer retains Australian residency for tax purposes. Should however the taxpayer rent out their home here or otherwise divest themselves of their domicile, due to an extended time of overseas employment, it is more likely that the individual is a foreign resident for tax purposes for the period they are overseas. But having said that, the outcomes are very much determined on a case-by-case basis.

IF YOU REMAIN AN AUSTRALIAN TAX RESIDENT

Any income that comes from working outside Australia– including salary, wages, commissions, bonuses and allowances – is typically regarded as foreign employment income. Such income may be paid by a foreign or an Australian employer. As an Australian tax resident, this foreign employment income is normally taxable in Australia and has to be included in your Australian tax return.

However, if you have paid tax on that employment income overseas, you should be able to claim some or all of the foreign tax as a credit against your Australian tax liability. This ensures that you are not double-taxed (as noted, you will need to consider the operation of any double taxation agreements). This credit is referred to as a "foreign income tax offset".
You can claim this for the Australian-dollar equivalent of the foreign tax paid on income, profits or gains (including gains of a capital nature) that are included in your Australian assessable income. In some circumstances, the offset is subject to a limit, which broadly equates to the amount of Australian tax that would be payable.

To be entitled to a foreign income tax offset:
- you must have actually paid, or be deemed to have paid, an amount of foreign income tax
- the income or gain on which you paid foreign income tax must be included in your assessable income for Australian income tax purposes.

IF YOU CEASE AUSTRALIAN TAX RESIDENCY

As a tax non-resident, you will only need to submit an income tax return if you have Australian-sourced income — and there is no need to lodge a return if the only Australian-source income you receive is interest, dividends or royalties that has had the correct amount of non-resident withholding tax deducted and remitted.

All Australian-sourced interest, dividends and royalties derived after you ceased to be an Australian resident are subject to the non-resident withholding tax provisions. Basically, the payer of the income has to withhold tax (at varying rates) on your behalf and you receive the income net of the withholding tax. As the withholding tax is a final tax, the income should not be included in your Australian tax return.

As a tax non-resident, if you dispose of assets you would only be subject to capital gains tax (CGT) if the asset qualifies as "taxable Australian property". This includes Australian real property and certain holdings of shares in companies that have a majority of their assets as Australian real property.

Further, when you become a non-resident, you are deemed to have sold all your CGT assets that aren't taxable Australian property for their respective market values at that time. So it is theoretically possible to pay the tax before you sell the asset, although you can generally elect to defer any capital gain or loss until you later sell the asset. If you make such an election, your CGT assets are taken to be "taxable Australian property" and so will fall within the Australian tax net if it is later subject to a taxing event (such as disposal).