

# AUSTRALIAN TAX ADVISER

2405 : NOVEMBER 2023

The IFX Legal Tax Team

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### INFORMATION EXCHANGE CORPORATION

L17, 40 Mount Street,  
North Sydney NSW, 2060

E: [admin@ifx.com](mailto:admin@ifx.com)

T: 61 2 9956 7775

W: [www.ifx.com.au](http://www.ifx.com.au)

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## SECTION 1 – PROFESSIONAL DEVELOPMENTS

### RESIDENCY, CITIZENSHIP AND THE TAXATION OF INCOME IN AUSTRALIA

From questions we have received, there seems to be some confusion about the income tax implications of receiving income in Australia from foreign sources. There are also issues regarding Australian income received by foreign citizens. To address these issues, it might be useful to categorise this income into various types.

#### ¶5.1 Citizenship versus residency

These concepts are often confused, because an individual's citizenship does not always make that person liable to income tax on their foreign income – residency on the other hand, does. In common with most OECD countries, Australia imposes income tax on both a *residency* and a *source* basis. Simply put, Australia reserves the right to impose tax on any income that arises within its jurisdiction.<sup>1</sup> Likewise, Australia will impose income tax on Australian residents regardless of where that income arises – domestically or locally.

So, if a person is a *non-resident* for tax purposes, that person will only be liable to Australian income tax on income tax has a *source* in Australia. On the other hand, if a person is a *resident* for tax purposes, he or she will be liable to Australian income tax on *all* income regardless of its source.

The issue is made more topical in Australia because of the structure of our income tax tables, which allow residents to earn up to \$18,200 per annum before they pay any income tax. Income above that level taxed at the rate of 19c for each \$1 over \$18,200.

Non-residents, on the other hand are taxed at the rate of 32.5% on all income up to \$120,000. This was originally put in place to compensate residents for the fact that the Medicare levy (and surcharge) did not apply to non-residents. Other implications of being a non-resident individual taxpayer include not being eligible for tax offsets and not being able to apply the 50% CGT discount on capital gains.<sup>2</sup>

#### ¶5.2 The residency tests

The 'resides' or 'ordinary concepts' test is the primary test of residence, and it is seen as a question of fact.

##### *The 'resides test'*

The 'resides' test considers whether a person resides in Australia under *ordinary concepts*. If an individual taxpayer is a resident according to the ordinary meaning of the word 'resides', they will be an Australian resident and the remaining residence tests need not be considered. Given that there is no legislative definition of the word 'resides', it has, arguably, acquired a judicial meaning that may be distinguishable from its ordinary

<sup>1</sup> Exceptions are typically contained in Australia's various Double Tax Agreements.

<sup>2</sup> In addition, in the event that the *Treasury Laws Amendment (Reducing Pressure on Housing Affordability Measures No. 2) Bill 2018* becomes law, non-residents might not be eligible for the main residence exemption.