Friends Provident International

Your guide to taxation when returning to Australia

Like many Australian expatriates, you may choose to return to Australia to live for a period or even permanently. It is important that your financial plans are flexible enough to meet changes in your lifestyle, such as becoming tax resident in Australia.

There are many things to consider when moving from one country to another. Careful tax planning is important, as this can help you boost your finances by preventing tax eroding your savings and investments unnecessarily.

Tax planning does not need to be complex. If you stay up to date with the latest reliefs and allowances and invest your money in tax-efficient products, you can ensure that you don't pay any more tax than you need to.

This should be an ongoing process rather than a one-off activity, as taxes change regularly. You can get help with this from your financial adviser.

This guide provides you with information designed to assist with your financial planning on becoming a tax resident of Australia. As this document is only a guide and we do not give tax, legal or investment advice, please ensure you always speak with your financial adviser before making any decisions.

Understanding your Australian tax status

The Australian tax system operates on a worldwide basis. This means that if you are a returning Australian expatriate, your income and capital gains are taxable in Australia, regardless of which country they arise in. There are some exceptions, if you are a new resident to Australia – please speak to your financial adviser for more information on this topic.

As an Australian resident, you will pay income tax and you will need a tax file number. If you are working, your employer will withhold tax from your salary and send it to the Australian Taxation Office (ATO) and you will lodge an annual tax return for a final assessment that includes your other income and capital gains. If you have income from overseas, such as pensions and property, these must be included along with your local Australian income.

The national Australian tax system is administered by the ATO. On your return to Australia, you will need to submit annual tax returns using your unique Tax File Number.

The extent of your liability to Australian tax will depend on your residence status but as this is assessable on a case-by-case basis, it's important to consider your personal circumstances.

Residence

The ATO will use criteria established in legislation, taxation rulings and case law and has a number of tests designed to establish residence or non-residence in a tax year. Please note that the terms non-residence and foreign residence mean the same thing.

You might be living away from Australia but continue to be an Australian tax resident. So, if your intention is to cease tax residence, you must make sure you have become sufficiently detached from Australia, otherwise your worldwide income will remain liable to Australian income tax.

The 'resides test'

If you live in Australia in a settled manner, particularly if it's for more than six months, then you will quite likely pass the 'resides' test and be a tax resident. The ATO will consider factors, including the location of your family and business/employment along with your assets and social arrangements, in assessing whether you pass this test.

Even if you do not pass the 'resides test', there are three statutory tests that the ATO will then consider to determine your residence status.

The statutory residence tests

1 The domicile test

This test is particularly relevant, if you have left Australia to live overseas. You may now no longer pass the 'resides test' because you have physically left Australia, but that does not necessarily mean that you have shed your tax residence.

'Domicile' is a legal concept which refers to your usual home and you are generally considered to have acquired it at birth. If you were born in Australia and have lived there permanently for a number of years before deciding to spend some time overseas, you may not necessarily have changed your Australian tax domicile.

Unless the ATO considers your usual place of abode to have changed from Australia to a new country, you will remain resident for tax purposes. A 'usual place of abode' does not mean that you must live there indefinitely, but it must be more than in just a temporary or transient manner.

Various factors will be considered by the ATO to determine whether you have changed your domicile, including:

- Your intended and actual length of time overseas – is it substantial enough?
- Your intention to return to Australia.
- Whether you have established a home overseas and if your family is with you.
- Your Australian house – is it let subject to a formal tenancy agreement?
- Whether you have settled in one place or if you are moving frequently and therefore not able to show permanence in one particular country.
- The personal and economic ties you have retained with Australia.

2 The 183 day test

Another test the ATO can apply is the 183 day test. The income tax year runs from 1 July to 30 June. If you spend more than 183 days in Australia during the tax year, you will be considered tax resident. However, should the ATO agree that Australia is not your usual place of abode then, despite being present for more than six months, you might not be taxed as a resident.

3 The Superannuation test

You may be a Commonwealth government employee posted overseas in your role as an officer of a government department such as Foreign Affairs and Trade. If you're an active contributing member of the Commonwealth Superannuation Scheme, you, your spouse and children will remain Australian tax resident.

In summary – the importance of taking advice

It's important to consider whether your actions and lifestyle create a tax residence or retain a liability to Australian tax.

A permanent move where you settle and show an established pattern of habitual behaviour will mean you pass the 'resides test'. However, you might move to Australia and then leave again after only a short period. In this instance, if the ATO viewed your intentions as being to make Australia your permanent home, you may be considered resident for that tax year despite only being there for a few months.

The Australian tax system

Australia has a number of federal, state and local government taxes and the ATO is the federal government authority responsible for administering the tax laws. This guide only covers the federal taxes on income and capital gains and considers the position on your death. Please note that there are no estate or gift taxes payable in Australia.

As an Australian resident you will pay tax on a progressive basis on your worldwide income and capital gains. Chargeable gains on the disposal of assets are included in your assessable income and taxed at your marginal rate. You will be entitled to the current tax-free threshold of **AUD 18,200** (tax year 2017/18) and you will have to pay the Medicare levy, a tax to fund health care in Australia. Please note that as a new arrival part-way through the tax year, your tax free threshold will be pro-rated for the year in question.

If you are a foreign resident, you are generally only taxed in Australia on Australian sourced income but you will not be entitled to the tax-free threshold. However, you will not have to pay the Medicare levy.

Income Tax

Your taxable income is derived from your assessable income after certain deductions. Your assessable income is made up of your ordinary income from work and investments, plus capital gains.

The income tax rates and bands for the tax year 2017/18 are as follows:

Taxable income (AUD)	Tax on this income
0-18,200	Nil
18,201-37,000	19%
37,001-87,000	32.5%
87,001-180,000	37%
180,001 and over	45%*

Medicare levy
In addition to the above, you will pay a Medicare levy used to fund health care in Australia. From 1 July 2014, this levy was increased to 2% of taxable income. Also, if your taxable income is above **AUD 90,000** and you don't have private medical insurance, you will pay a surcharge which, depending on income levels, can be as high as 1.5% of your taxable income. Some people with low incomes may qualify for a reduction. There are also some exemptions.

*The Temporary Repair Levy ceases to apply from 1 July 2017.

Capital Gains Tax

In Australia, Capital Gains Tax (CGT) isn't actually a separate tax. So when you redeem an investment giving rise to a chargeable gain, it is included as part of your assessable income for that tax year. As an Australian resident, you will be liable to CGT on gains arising from the disposal of your worldwide assets.

Some of your assets will be exempt from the charge to CGT, such as your main residence. The tax is payable when you sell certain types of investment, including managed funds and shares. If you make a profit on the sale of the asset, the chargeable gain after certain deductions will be taxable, but the amount on which tax is levied will be reduced by allowable losses (where you have sold assets such as shares or real estate for less than what they cost you).

If you originally purchased the investment before 21 September 1999, you have the option of using the indexation method, which increases the base cost to take account of inflation.

If you have held the investment for more than 12 months, you could reduce the chargeable gain after any losses by applying the discount method. This enables you to halve the gain on which tax is payable. However, if you had disposed of the asset after 8 May 2012 and were a foreign resident during any part of the ownership period, the discount applied on the chargeable gain may be reduced or removed.

If you have not held the investment for 12 months, then you must use the basic method of deducting the base cost from the capital proceeds.

An example of how to calculate your taxable profit:

	Investment A (AUD)	Investment B (AUD)
Sale Proceeds	**60,000**	**18,000**
Brokerage and stamp duty for purchase and sale	**1,000**	**1,000**
Investment amount >12 months	**50,000**	**20,000**
Gain assessable for tax	Gain **9,000**	Loss **3,000**

Your assessable gain after accounting for allowable losses in the above example is **AUD 6,000**. This is the gain on investment A, less the loss on investment B. Using the discount method, you will pay tax on (**AUD 6,000** x 50%).

Non-residents do not always benefit from the main residence exemption, and they are potentially subject to a withholding regime of 12.5% on gains from 1 July 2017 (previously 10%).

Tax position on your death

Australia does not currently levy inheritance tax on your estate when you die and death does not constitute a disposal of your assets for CGT purposes. Therefore, when your representatives transfer assets to your beneficiaries, there is no immediate tax to pay. Your heirs inherit those assets either at the market value on your death, or at your base cost of acquisition depending on when they were purchased.

Please note that if your representatives sell assets during the administration of your estate, then the normal CGT rules will apply and tax may be payable on the arising profit.

You should take advice on how assets will be treated because there is a difference between those you acquired before 20 September 1985, compared to assets acquired after this date. The outcome could be significant for your beneficiaries because post-September 1985 assets are inherited at their original base cost, meaning your heirs inherit liability to CGT on the full increase in value over the holding period of the asset.

An asset inherited that was originally purchased before September 1985 is inherited at the market value on your death. This means only profit arising thereafter becomes taxable when the recipient disposes of it.

The following example helps to illustrate the difference in the above, by comparing a share purchase of **AUD 100,000** by the deceased before and after September 1985.

Share purchase date	Before 20 September 1985 (AUD)	After 20 September 1985 (AUD)
Market value at death	**400,000**	**400,000**
Beneficiary deemed acquisition cost	**400,000**	**100,000**
Beneficiary sells shares two years after inheritance for **AUD 450,000**, benefitting from the CGT discount method.		
Gain assessable for tax	**25,000**	**175,000**

Unilateral relief for foreign taxes paid and Double Taxation Agreements

As an expatriate, you could find yourself liable to taxation in your home country on income arising overseas that has already been taxed in the source country. In Australia, relief from this situation may be provided by way of either:

- unilateral relief given by the ATO against taxes already paid; or
- through a double taxation agreement (DTA) between Australia and the source country.

Unilateral relief may be granted by the ATO when an Australian resident has paid non-reclaimable tax on the income in the country in which it arises. The tax already paid would normally be allowed as a credit towards your Australian income tax liability.

Australia has over 40 DTAs in force that determine which country has the taxing rights over your income when that income arises outside Australia. You should take professional advice on how a DTA may operate, if you have income arising overseas.

Tax efficiency of international life plans when you return to Australia

International life plans taken out while you are an expatriate could maintain their tax efficiency on your return to Australia.

Policyholder taxation after returning from overseas

Life insurance and critical illness policies

- Lump sum benefits are not taxable on receipt.

Regular premium and single premium unit-linked savings policies

- Enjoy the benefits of gross investment returns inside your policy.
- Switch funds inside your policy without paying CGT.
- Chargeable gains known as bonuses are assessable income and taxable at your marginal rate.
- Only bonuses received within the ten-year eligibility period are assessable income.
- Premium increments of more than 25% of the previous year's premium amount extend the eligibility period.

Insurance-based savings plans can bring you a number of tax-planning benefits, if you decide to return to Australia.

However, as legislation and ATO interpretation are subject to change, it is important you consult with your adviser before proceeding. In addition, while we would not expect there to be Australian GST implications, you should take advice, as this will depend on your individual circumstances.

Capital accumulation – gross roll up

International life insurance products are generally not subject to tax while the investments accumulate in value. This means your savings can grow free of tax, with the exception of certain withholding taxes.

Managing your investments – switching funds

As your investments grow, you may wish to switch funds to realise gains and invest in new opportunities. Buying and selling funds directly can create a liability to CGT, but by using life assurance products, you should be able to avoid this and make decisions driven by investment performance rather than tax considerations.

Withdrawing money to support you in the future

There may come a time when you want to start using your investment to supplement other sources of income such as your pension, or for capital expenditure such as buying a property. You will be able to set up a regular 'income' withdrawal or take ad hoc payments or fully surrender the plan, if it is no longer required.

As an Australian tax resident, you will be assessed for income tax on the chargeable gains arising from life assurance policies in accordance with the income tax legislation. These gains are known as bonuses and only become taxable when you actually receive them and not while they are accumulating in the policy.

If you hold your policy for more than ten complete policy years since its commencement, you will not be taxed on the bonus because, after this time, it is no longer included as part of your assessable income.

If a bonus payment occurs within the first 8 years, it will be fully assessable for income tax, but in years 9 and 10 only two thirds and one third of the bonus respectively are assessable.

Examples

	AUD
Initial investment	**100,000**
Current surrender value in year 7	**150,000**
Example 1	
Withdrawal in year 7	**25,000**
Bonus amount assessable for income tax	**8,333** (25,000/150,000) x 50,000
Example 2	
Full surrender in year 7	**150,000**
Bonus amount assessable for income tax	**50,000** (150,000–100,000)
Example 3	
Current surrender value in year 11	**180,000**
Full surrender in year 11	**180,000**
Bonus amount	**80,000**
Bonus amount assessable for income tax	**Nil**

You should be aware that it is not possible to add significantly large sums to an existing investment and still avoid a possible tax charge after ten years. Rules exist that are designed to restart the ten-year period from the start of the policy year in which the new investment is made.

In the event the policy terminates on your death, the payment is not assessable income on receipt by a taxpayer. Also, the estate of the deceased will not be subject to CGT on the proceeds as they will be received for no consideration resulting in any gain or loss being disregarded.

Succession planning to avoid payment delays on your death

As an expatriate, you may have acquired assets in different countries with different laws on how they will be taxed and be passed on, if you die.

An international life company may require sight of a Grant of Representation before paying any monies on your death to your personal representatives. Before this Grant can be applied for, your representatives will first have to obtain the equivalent legal documentation in your home country. This whole process can be lengthy, creating considerable delays before investments can be passed on to those who need them.

You can avoid such delays by planning ahead and using beneficiary nominations and trusts, where appropriate, to ensure the smooth transfer of wealth to your beneficiaries. Our estate planning guide for Australian expatriates, 'Passing on your wealth', may also be of interest to you. You can find this from your financial adviser, or on our website. Estate planning is a complex matter and we recommend that you obtain independent advice on how best to proceed.

This guide has covered: understanding your tax status, the Australian tax system and the tax efficiency of international life plans.

When discussing returning to Australia with your adviser, you may also wish to cover:

01 Obtaining valuations on your Australian and overseas property assets for CGT purposes.

02 Taking advice on the tax implications of retaining overseas assets.

03 Using surplus cash to boost your Australian superannuation investments.

04 Ensuring you hold no more than **AUD 250,000** in foreign currency accounts otherwise tax will be payable on any gains at your marginal income tax rate.

05 Reinstating your Medicare card and private health insurance.

06 Reinstating your name on the electoral roll.

07 Ensuring your Australian income tax returns are up to date.

08 Checking that your Australian driving licence is still valid.

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Visit our website to learn more about our range of flexible savings, investment and protection plans.

Speak to your financial adviser today to see how we could help you plan for your return to Australia.

About Friends Provident International

We are a leading financial services provider, with a reputation of trust, commitment and integrity, offering financial solutions to customers throughout their lives.

Friends Provident International has over 35 years of international experience and our heritage dates back over 180 years.

Please note that the tax rates and provisions provided in this document are taken as at 1 January 2018 and are subject to change.

This document is for information only. It does not constitute investment advice or an offer to provide any product or service by Friends Provident International.

Please seek professional advice, taking into account your personal circumstances, before making investment decisions. We can accept no liability for loss of any kind incurred as a result of reliance on the information or opinions provided in this document.

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