DOING BUSINESS IN AUSTRALIA

LEGAL AND FISCAL ASPECTS

PREPARED BY:

LWK PTY LIMITED
Chartered Accountants
Business Advisers and Consultants

Suite 201, Level 2
65 York Street
Sydney NSW 2000
Australia

Telephone: 61+2+9290 1588
Facsimile: 61+2+9290 2997
Email: reception@lwkca.com

Nexia
International

FOREWORD

The objective of this publication is to provide some guidance for those wishing to invest or do business in Australia.

As many regulations and laws change at short notice, this document should serve only as a reference source rather than providing comprehensive answers or definitive advice, for which specific consideration and expert advice should always be sought.

The Principals of LWK have been in business for over 30 years and LWK is a member of the worldwide association of independent accountants, Nexia International.

LWK practises in a wide range of financial services including audit, accountancy, taxation, management, advisory and business migration services. We would be pleased to advise on any of these aspects including the technicalities of investing in Australia.

LWK Pty Limited

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1. INTRODUCTION

1.1 The Commonwealth of Australia

The Commonwealth of Australia is a federation established in 1901. The federation consists of six states and several territories, being the states of New South Wales, Victoria, Queensland, Tasmania, South Australia and Western Australia, and the Australian Capital Territory (the seat of Federal Parliament), the Northern Territory and various external island territories.

The relationship between the Commonwealth Government and the various State and Territory Governments is regulated by the Australian Constitution which has been in place since Federation. Matters of national concern such as defence and foreign affairs, trade, commerce and currency, social services and pensions, marriage and divorce, bankruptcy and insolvency have been vested in the Federal Government. The State and Territory Governments retain jurisdiction in domestic matters such as education, health, roads, energy and environmental concerns. The Australian Constitution is a written document, however numerous issues have been referred to the Courts to assist in its interpretation.

1.2 The Australian Political System

The Australian political system, at both federal and state levels, is comprised of two dominant parties. The Liberal Party, of conservative complexion, in coalition with the smaller National Party, primarily representing rural interests and the Labor Party which is democratically socialist in its ideology.

Federal elections are held at least once every three years and history dictates that one party usually defeats the other only marginally. Despite this, the Federal Government has changed only nine times over the past 30 years, the current Coalition Government took place on 18 May 2019.

1.3 The Australian Legal System

The Australian legal system is based upon the common laws of the Westminster system established in the United Kingdom, complemented by Australian common law and statutory law enacted by the Federal, State and Territory Parliaments.

Australia has a well-established system of appellant courts at both a Federal and State level. The highest court in Australia is the High Court, established in 1903 by the Australian Constitution. The High Court is the final appellant court available in Australia.

1.4 Australian Geography and Demography

The Australian continent (including Tasmania) covers an area of some 7,682,000 square kilometres. From the east coast to the west coast the distance is approximately 4,000 kilometres and the distance from the north to south is approximately 3,700 kilometres.

Owing to the fact that the centre of Australia is extremely arid and for other obvious commercial reasons, the principal cities of Australia are to be found on the coast, with the exception of the Federal capital, Canberra, which is situated inland and approximately mid-way between Sydney and Melbourne.

The current population of Australia is approximately 25.0 million and there is a very high degree of urbanisation. Approximately 67% of the population lives in urban areas and some 67% of the population resides in the capital cities in each state.

Current approximate population figures are as follows:

State/Territory	Population	Change %
New South Wales	8,172,500	0.4
Victoria	6,661,700	0.0
Queensland	5,194,900	1.1
Western Australia	2,670,200	0.9
South Australia	1,770,800	0.5
Tasmania	541,500	0.6
Northern Territory	246,600	0.5
Australian Capital Territory	431,500	0.8

Australia's population is mainly of European origin. In recent times there has been a significant increase in Asian immigration. Sydney and Melbourne are the main commercial centres and in the financial services sector. Sydney is the most important of Australian cities. Melbourne is an important centre for longer established and large manufacturing and mining enterprises.

English is virtually the only language commonly used throughout Australia.

2. FOREIGN INVESTMENT

2.1 Foreign Acquisitions and Takeovers Act

2.1.1 Australian foreign investment policy is administered by the Treasurer with the assistance of the Foreign Investment Review Board.

The objectives of the Board are to examine proposals by foreign interests for investment in Australia in order to make recommendations on those proposals and to generally advise the Federal Government on foreign investment matters.

The policies of the Board are derived from the Foreign Acquisitions and Takeovers Act, 1975 and by ministerial statements made by the Treasurer.

2.1.2 A foreign person is defined in the Act to be:

a. a natural person not ordinarily resident in Australia;

b. a corporation or the trustee of a trust in which any individual not ordinarily resident in Australia, a foreign corporation or a foreign government holds a substantial interest; or

A substantial interest is:

i. for an entity—the person holds an interest of at least 20% in the entity; or

ii. for a trust (including a unit trust)—the person, together with any one or more associates, holds a beneficial interest in at least 20% of the income or property of the trust.

2.2 Foreign Investment Review Board

2.2.1 Certain proposals for foreign investment falling within the scope of the Foreign Acquisitions and Takeovers Act must be submitted to the Foreign Investment Review Board. These include:

a. acquisitions of interests in Australian real estate and land (including interests that arise via leases, financing and profit sharing arrangements) that involve:

i. any residential land irrespective of value;

ii. agricultural land valued at $1,216 million for investors from Chile, New Zealand and the United States, or valued at $50 million for investors from Thailand, or cumulatively valued at $15 million for other investors;

iii. any vacant commercial land irrespective of value;

iv. developed commercial land valued over $1,216 million for investors from FTA partner countries, or valued over $281 million for other investors, or valued over $61 million for low threshold land;

b. acquisitions of interests in Australian business that involve:

i. non-sensitive business valued at $1,216 million or more and sensitive business value at $281 million or more for investors from FTA partner countries that have the higher threshold;

ii. all the business sectors valued at $281 million or more for other investors;

iii. agribusiness valued at $61 million for all investors (including all FTA and non FTA partner countries);

iv. an acquisition of interest of 20% or more in any business valued above $281 million (or the higher threshold of $1,216 million for agreement country investors from Chile, China, Japan, Korea, New Zealand and the United States) require prior approval;

v. direct interest in an Australian entity or business or to start a new Australian business by all foreign government investors irrespective of value;

c. takeovers of off-shore companies that have Australian subsidiaries or assets also apply the monetary thresholds;

d. proposals where any doubt exists as to whether they are notifiable. (Funding arrangements that include debt instruments having quasi-equity characteristics will be treated as direct foreign investment)

2.2.2 Other investment proposals not within the scope of the Foreign Acquisitions and Takeovers Act but requiring examination by the Board include:

a. investments in the media sector of 5% or more requires notification and prior approval regardless of the value of investment;

b. all direct investments by foreign governments or their agencies, regardless of size.

2.2.3 A new business includes;

a. the establishment of a business in Australia by a foreign interest not already operating a similar business in Australia.

b. the establishment of a new hotel or tourist facility, a new mining or raw materials processing project, and a new project in the agricultural, pastoral, forestry or fishing sectors, even if the foreign interest is already operating a similar business in Australia; and

c. the diversification of a foreign interest into an activity not previously undertaken by it in Australia.

2.3 Examination of Proposals

2.3.1 On 26 February, 1992, the Government announced a liberalisation of foreign investment policy guidelines in the following sectors: rural properties, agriculture, forestry, fishing, resource processing, oil and gas, mining (excluding uranium), manufacturing, non-bank financial intermediaries, insurance, stockbroking, tourism (hotels and resorts) and other services (excluding urban real estate, banking, civil aviation, media, shipping, airports and telecommunications).

2.3.2 No changes were made to the notification requirements of proposals; however, in the above sectors the following proposals, once registered, will normally no longer be examined or required to meet the national interest test:

a. the acquisition of 20% or more of a company or business valued by total assets and consideration below AUD 281 million (or the higher threshold of $1,216 million for agreement country investors from Chile, China, Japan, Korea, New Zealand and the United States) ;

b. the takeover of an off-shore company with Australian subsidiaries or assets valued below AUD 281 million.

2.3.3 In the above sectors, proposals below the new threshold will normally be approved without examination, and proposals valued at AUD 281 million (AUD 1,216 million) or more will continue to be examined, and will be approved unless contrary to the national interest.

2.4 Australian Participation

2.4.1 The Government considers that Australians should have adequate opportunities to participate as fully as practicable in the development of Australia's industries and natural resources. Specific guidelines for Australian participation are set down only in relation to the acquisition of banking, transport and telecommunications.

2.4.2 In respect of proposals to undertake investments in other sectors of the economy, Australian participation is welcomed but is not a requirement.

2.5 Real Estate

2.5.1 Proposals for the acquisition of domestic real estate by foreign interests are required to be submitted for examination by the Foreign Investments Review Board unless they are specifically exempted (refer 2.3.3). Acquisitions of urban real estate that do not involve any new development and that are intended purely to earn investment income or to benefit from capital appreciation are not normally approved as they provide little or no benefit to Australia.

Under current government policy, approval will be refused for the purchase of developed residential real estate for occupation or investment by foreign interests except in the categories set out below.

2.5.2 The following real estate acquisitions are normally approved unless they are thought to be contrary to the national interest:

a. acquisition of second-hand dwellings as their principal place of residence by temporary residents in Australia provided that: i) the property is used as their principal place of residence in Australia, ii) the property is vacant at settlement and no part of the property is rented, and iii) the dwelling is sold within 3 months when it ceases to be their principal residence;

b. acquisition of established dwellings by foreign companies seeking accommodation for their Australian-based staff provided that the property is solely used to accommodate Australian-based employees of the business, and the company sells the property if it is expected to remain vacant, or has remained vacant, for 6 months or more;

c. acquisition of vacant land for the purpose of building residential dwellings provided the development is completed within 4 years from the date of approval, and the evidence of completion of the dwellings is submitted within 30 days of being received.

d. acquisition of new dwelling provided that the dwelling has not been previously occupied; or directly acquisition from the developer provided that the dwelling has not been occupied for more than 12 months in total. However, it does not include established residential real estate that has been refurbished or renovated.

e. acquisition of established dwellings for the purpose of redevelopment (that is genuinely increase the housing stock) provided that: i) the existing residence cannot be rented out prior to demolition and redevelopment, ii) the existing dwelling is demolished and construction of the new dwellings are completed within 4 years of the date of approval, and iii) the evidence of completion of the dwellings is submitted within 30 days of being received. However neither temporary residents nor foreign non-residents are approved to purchase an established dwelling to redevelop into a single new dwelling.

f. acquisition of vacant commercial land regardless of the value and provided that continuous construction is commenced within 5 years of the date of approval, and the land is not sold until the construction is complete.

g. acquisition of developed commercial land by investors from Free Trade Agreements (FTA) partner countries provided that the property value is less than $1,216 million.

h. acquisition of developed land by investors from non-agreement countries for low threshold commercial land that value is less than $61 million, and for non-low threshold commercial land that is no more than $281 million.

2.5.3 Exemptions are available for urban real estate acquisitions by:

a. acquisition of residential real estate by Australian citizen;

b. acquisition of residential real estate by New Zealand citizen;

c. acquisition of residential real estate by Australian permanent resident;

d. acquisition of residential real estate made in joint names by Australian citizen/ New Zealand citizen/ Australian permanent resident and their foreign spouse. However, it does not include purchasing property as tenants in common;

e. acquisition of residential real estate by an Australian corporation that would not be a foreign person if interests directly held in it by Australian citizens living abroad, Australian permanent visa holders or New Zealand citizens were disregarded;

f. acquisition of residential real estate by the trustee of a resident trust, if at the time of the acquisition, the trustee would not be a foreign person if interests directly held in it by Australian citizens living abroad, Australian permanent visa holders or New Zealand citizens were disregarded;

g. acquisition of residential real estate by a charity operating in Australia primarily for the benefit of persons ordinarily resident in Australia

h. acquisition of new dwellings from the developer, where the developer holds a New Dwelling Exemption Certificate.

i.acquisition of a time share scheme where the foreign person's total entitlement (including any associates) to access the land is no more than 4 weeks in any year;

j.acquisition of an interest by will or by devolution of law (such as, a court order regarding the division of property in a divorce settlement, but not if both parties simply agree to transfer property without a court's intervention);

k. direct acquisition of property from the Government (Commonwealth, State, Territory, or local governing body) or acquisition of an entity wholly owned by the Government;

2.5.4 The acquisition of agricultural land used wholly and exclusively for carrying on a substantial commercial primary production business valued at less than AUD 1,216 million does not require approval for investors from Chile, New Zealand and United States, valued at less than AUD 50 million for investors from Thailand and for other investors threshold of $15 million applies.

2.6 Approval Criteria

2.6.1 Foreign investment proposals are dealt with on a case by case basis against criteria, which take into account economic, social and other national interest considerations.

The available benefits of the proposal should be seen to outweigh any costs, including those associated with the reduction or lack of Australian ownership and control.

In the examination process it is the practice to consult other Government departments and authorities on a confidential basis.

2.6.2 The criteria, in broad terms, are whether the proposal will result in:

a. net economic benefits to Australia,

b. increased competition, lower price levels or greater efficiency;

c. industry rationalisation;

d. improvement in the quality and variety of goods and services available in Australia;

e. development of, or access to, new export markets;

f. increased employment opportunities for Australians;

g. any detriment to Australian revenue;

h. new technology or skills;

i. stimulation of economic growth;

j. compliance with Government policies;

k. Australian involvement in equity participation and management; and

l. desirable impact on decentralised development and the environment.

It is not necessary to satisfy all of the criteria in order to warrant approval and the extent to which proposals are required to meet the criteria vary from case to case.

The breadth of the foreign investment policy might seem formidable but the present climate is more welcoming than it once was and potential foreign investors may expect to be well received.

2.7 Specific Policy Applications

Some specific applications of foreign investment policy:

2.7.1 Media

All foreign persons, including investors from FTA countries, need to notify the Government and get prior approval to make investments of 5% or more in the media sector, regardless of the value of the investment.

2.7.2 Minerals

The acquisition of a mineral right, mining lease, mining tenement or production licence will require foreign investment approval if it involves acquiring an interest in Australian urban land including:

a. an interest in a lease or licence giving rights to occupy Australian urban land where the term of the lease or licence is reasonably likely, at the time the interest is acquired, to exceed 5 years; or

b. an interest in an arrangement involving the sharing of profits or income from the use of, or dealings in, Australian urban land.

Approval is not required if the lease or licence is acquired from the Commonwealth, a State or Territory, or a local governing body.

2.7.3 Banking

Foreign investment in the banking sector needs to be consistent with the Banking Act 1959, the Financial Sector (Shareholdings) Act 1998 (FSSA) and banking policy, including prudential requirements. Any proposed foreign takeover or acquisition of an Australian bank will be considered on a case-by-case basis and judged on its merits.

The Government will permit the issue of new banking authorities to foreign owned banks where the Australian Prudential Regulation Authority (APRA) is satisfied the bank and its home supervisor are of sufficient standing, and where the bank agrees to comply with APRA's prudential supervision arrangements.

2.7.4 Civil Aviation

a. Domestic Services
Foreign persons (including foreign airlines) can generally expect approval to acquire up to 100 per cent of the equity in an Australian domestic airline, unless this is contrary to the national interest.

b. International Services
Foreign persons (including foreign airlines) can generally expect approval to acquire up to 49 per cent of the equity in an Australian international carrier (including Qantas) individually or in aggregate provided the proposal is not contrary to the national interest.

2.7.5 Shipping

The *Shipping Registration Act 1981* requires a ship to be majority Australian-owned if it is to be registered in Australia, unless it is operated by a foreign resident under a demise charter and is exempted from the requirement to be registered during the term of the charter.

2.7.6 Airports

The Airports Act 1996 limits foreign ownership of some airports to 49%, with a 5% airline ownership limit; and cross-ownership limits between Sydney airport (together with Sydney West) and either Melbourne, Brisbane, or Perth airports:

- The cross-ownership provisions in the Airports Act 1996 apply when a foreign person has more than a 15% stake in the Sydney airport (together with Sydney West) airport-operator company and one of the Perth, Brisbane, or Melbourne airport-operator companies. Also for stakes of 15% or less, the Minister may declare practical control.

2.7.7 Telecommunications

Foreign persons should be aware that the *Telstra Corporation Act 1991* imposes limits on foreign ownership of Telstra. Aggregate foreign ownership of Telstra is restricted to 35% and individual foreign investors are only allowed to own up to 5%.

2.7.8 National land register

Under the *Register of Foreign Ownership of Agricultural Land Act 2015* foreign investors are required to report their existing agricultural landholdings and any acquisitions or disposals to the Australian Taxation Office regardless of the value of that land. All existing holdings were required to be registered with the Australian Taxation Office by 29 February 2016 and any new interests must be registered within 30 days of acquisition.

2.8 Thin Capitalisation

Effective from 1 July 2001 and under the Income Tax Assessment Act 1997, statutory restrictions are placed on the deductibility of finance expenses (such as interest). The purpose of these provisions is to regulate the level of debt deductions available in Australia to *foreign controlled* Australian entities having regard to their Australian assets. The legislation covers Inward Investing Entities and Outward Investing Entities, both of which are also categorised as either an Authorised Deposit-Taking Institutions (ADIs) such as banks or a non Authorised Deposit-Taking Institutions (non-ADIs). Separate thin capitalisation rules and variations apply to each category.

There are separate rules for different Australian entities (such as company, trust or partnership) to determine if it is foreign controlled. There are also extensive anti-avoidance provisions which cover situations of de facto control.

On 25 September 2014, the Tax and Superannuation Laws Amendment (2014 Measures No 4) Bill 2014 had been passed by the parliament and amendments made on Thin Capitalisation are as follows:

i) Reduction of the safe harbour debt limit from a debt-to-equity ratio of 3:1 to 1.5:1 for general entities;

ii) Allowing the worldwide gearing ratio to be available to inbound investors and reducing the ratio from 120% to 100%;

iii) Increasing the safe harbour capital limit for ADI from 4% to 6% of their risk weighted Australian assets; and,

iv) Increasing the De Minimis threshold from $250,000 to $2,000,000.

v) Introducing a new ‘inbound’ worldwide gearing debt test.

2.8.1 Inward investing entities

For non-ADI a deduction for Australian income tax purposes is denied in respect of finance expenses payable on debts which exceeds the maximum allowable debt. Maximum allowable debt is the greater of (i) an amount calculated according to a set of “safe harbour” rules or (ii) an arm’s length debt amount.

Where the total debt exceeds the maximum debt allowed, the finance expenses paid on the interest bearing debt, to the extent of the excess, is denied deductibility against domestically derived income.

For ADIs, debt deductions will be reduced where the equity capital used to fund the Australian operations is less than the “minimum capital amount”.

The thin capitalisation rules do not apply if the total of debt deductions does not exceed AUD 2,000,000 for an income year.

2.8.2 Outward investing entities

Where an Australian entity invests overseas, either through a controlled foreign entity or overseas branch, it is possible for the entity to allocate excessive Australian debt to its Australian operations in order to maximise interest deductions in Australia and minimise overseas expenses for making foreign exempt income. The thin capitalisation rules aims to limit the extent to which an Australian entity can claim deductions for its Australian debt.

For a non-ADI, a portion of debt deduction (to the extent that it is not attributable to overseas business and investment) will be denied if for that year the entity “adjusted average debt” exceeds its maximum allowable debt.

While the rules for non-ADIs focus on levels of debt, the rules for ADIs focus on minimum levels of capitalisation. All or part of a debt deduction will be disallowed if its “adjusted average equity capital” is less than the entities “minimum capital amount”.

The thin capitalisation rules do not apply if:

i. the total debt deductions (including interest, borrowing costs and other fees etc) do not exceed AUD 2,000,000; or

ii. the average value of Australian asset is 90 per cent or more of the average value of total assets for the year.

3. FOREIGN EXCHANGE AND CURRENCY TRANSACTION CONTROL

3.1 The Cash Transactions Reports Agency

Exchange control in Australia is governed by the Australian Transactions Reports and Analysis Centre (AUSTRAC). AUSTRAC monitors businesses which deal in cash, who are required to supervise the identification of their customers and to monitor and report upon the transactions which they conduct on behalf of their customers. These businesses are called "cash dealers".

3.2 Currency Transaction Reporting

3.2.1 The main features of the Financial Transactions Reports Act are:

a. Cash dealers will generally be required to report to the AUSTRAC (suspect transactions, cash transactions of AUD 10,000 or more or the foreign currency equivalent, international funds transfer instructions).

b. Cash dealers need to verify the identity of persons who are signatories to accounts, and also prohibiting accounts being opened or operated in a false name.

c. A cash dealer who is party to a transaction and who has reasonable grounds to suspect (rather than believe) that information it has concerning the transaction may be relevant to the investigation of a crime must report the transaction, whether or not otherwise required to do so.

A cash dealer who makes such a report is immune from any suit or proceeding, e.g. for breach of confidence and by providing information protects itself against prosecution for money laundering. Failure to report is an offence.

3.2.2 A cash dealer is required to obtain financial transaction documents and account and signatory information. The Act also prohibits the opening or operation of accounts with cash dealers in false name. A false name is defined as any name other than a name by which the person or corporation is commonly known.

3.2.3 All cash transactions information reported to the AUSTRAC will be made available to the other relevant authority on a direct and unrestricted basis, including the Commissioner of the Australian Federal Police, the Integrity Commissioner, the Chief Executive Officer of the Australian Crime Commission, the Commissioner of Taxation, or the Chief Executive Officer of Customs. This information will also be available to law enforcement agencies including the Australian Customs Service, the National Crime Authority and comparable law enforcement agencies in the States and Territories.

3.2.4 Transactions to avoid the reporting rules, including structuring transactions so that they have a face value of less than AUD 10,000, the providing of false or misleading statements or the communication of information that is incomplete are offences.

3.3 Cash Dealers

Cash dealers are defined in the Act in very broad terms so as to result in the application of the reporting requirements to an extensive range of persons and corporations. These include the following:

- financial institutions
- financial corporations
- insurer or insurance intermediaries
- securities dealers and futures brokers
- trustees or a manager of a unit trust
- persons that deal in travellers cheques and money orders
- persons who collect, hold, exchange or remit currency on behalf of other persons
- currency and bullion dealers
- casinos and gambling houses
- totalisator agency boards.

4. BUSINESS STRUCTURES

4.1 Introduction

Carrying on a business enterprise in Australia can be undertaken using various business structures. Small businesses are often operated as sole traders or in partnership. As businesses grow, incorporation of a business to form a company may be desirable to take advantage of certain financial and taxation benefits. Regardless of the size or operation of the enterprise, each business structure must comply with certain rules and regulations set down by Australian authorities. A brief examination of these structures and regulations is provided below.

4.2 Sole Traders

4.2.1 Any person of full age and capacity may commence a business enterprise in Australia. When a person carries on this business by himself he is commonly known as a sole trader. Subject only to satisfying relevant licensing requirements, the nature of which depends on the business operations proposed, a person may operate as a sole trader of any lawful business anywhere in Australia.

A sole trader must disclose all revenues derived and expenses incurred in the derivation of this revenue in an annual income tax return. The net result being subject to tax in Australia.

4.3 Partnerships

4.3.1 A partnership is the relationship which exists between two or more persons carrying on business in common with a view to profit.

The essential feature distinguishing a partnership from a sole trader is that each partner must carry on the same business with his fellow partners.

Each partner is deemed to be an agent of the other partners and on behalf of the partnership as a whole. In this regard each partner may make contracts, undertake obligations and dispose of partnership property in the ordinary course of partnership business. All partners are exposed, jointly and severally to third parties for the actions of other partners and the liabilities of the partnership.

Membership in an ordinary partnership is limited to 20 partners. A group of more than 20 must be incorporated as a company. In the case of certain professional partnerships, such as those formed by lawyers and accountants, this number may be as high as 400.

4.3.2 Partnerships may be created with very little formality. In Australia there is no legal requirement for a written partnership agreement to constitute an ordinary partnership, although it is desirable that partners formalise their relationship in a written agreement.

State legislation, such as the *Partnership Act 1892 (NSW),* will govern an oral agreement and supplement a written one.

The contents of a partnership agreement will depend on the objects of the partnership and the nature of its business. In general, provisions may be made for:

a. nature and place of business;

b. duration of partnership;

c. name of firm;

d. provision of capital;

e. banking operations;

f. sharing of profits and losses;

g. management;

h. accounts;

i. expulsion of partners;

j. termination of partnership;

k. arrangements on death or retirement of a partner or on dissolution of the firm; and

l. arbitration of disputes.

4.3.3 A partnership is not a taxable entity: Although a partnership tax return is lodged in each financial year, each partner is separately assessed to tax on their share of the net taxable income of the partnership.

4.3.4 One of the most attractive features of a partnership as a business vehicle is the ability of its members to share in the losses of the business by writing off those losses against the profits of other activities for taxation purposes. This facility is not available to shareholders of a limited company in respect of losses of the company, unless it is a wholly owned subsidiary for the fiscal year in which the loss is incurred and the group elects to adopt the Consolidation rules under the Income Tax Assessment Act.

4.4 Limited Partnership

4.4.1 Limited partnerships are recognised by statute on an individual state basis so that members of a firm who do not take part in the management of the business may limit their personal liability in respect of transactions of the firm.

4.4.2 If a partnership carries on its enterprises in any name other than the name of the partners, the partnership is required to register its business name under Business Names legislation existing in each State or Territory in which the partnership operates.

4.4.3 Limited partnerships are treated as companies for taxation purposes.

4.5 Unincorporated Joint Ventures

4.5.1 Joint ventures are often established to carry on an enterprise where the participants do not desire to form a separate legal entity, such as an incorporated company or partnership to carry out the operation.

Essentially, a joint venture is an asset sharing arrangement whereby two or more participants, share the costs of production and receive a share of any resulting output in return. The participants in a joint venture are usually limited liability companies. Legal ownership of joint venture assets is shared by the parties as tenants in common.

Joint ventures are widely used in Australia for exploration, development of mineral resources, mining and technological research projects.

4.5.2 Tax deductible expenditure in the joint venture may be off-set by the participants against taxable income from other sources.

Income is received separately by individual participants with no profit being earned by the joint venture. The joint venture is not a taxable entity and each participant lodges its own tax return in which it claims its share of the costs of the joint venture.

4.5.3 Unlike a partnership, each participant is generally responsible only for its agreed share of liabilities of the joint venture. Given that this situation is strictly adhered to the joint venture is distinguished from a partnership as far as exploitation and disposal of the product of the enterprise.

4.5.4 It is essential that the terms of a joint venture are set out in a detailed agreement which should, at least, cover ownership of assets, sharing costs of production, the term of the venture and mutual covenants of the participants, including a denial of partnership.

4.5.5 A joint venture is a flexible structure which is now being seen as having potential for use in a wider range of projects, including film and television transactions.

4.6 Companies

4.6.1 Many business operations in Australia are carried out under the ambit of an incorporated company. Companies are incorporated and regulated under the Corporations Act which is administered by the Australian Securities and Investments Commission (ASIC).

Four classes of company may be formed:

a. a company limited by shares;

b. a company limited by guarantee;

c. an unlimited company; and

d. a no liability company, which is restricted to mining activities.

4.6.2 Companies having a share capital are either public or proprietary companies. The main points of distinction are:

a. Membership

A public company must have at least one member but there is no upper limit.

A proprietary company must also have at least one but not more than 50 non-employee shareholders.

b. Share Capital

Provided each type of company has the requisite number of members there is no minimum paid up capital.

A proprietary company must, by its constitution, restrict the right to transfer its shares, e.g., subject to approval of its directors or only after rights of pre-emption in favour of other shareholders have been exercised.

Shares in a listed public company should be freely transferable.

The constitution of a proprietary company must prohibit any invitation to the public to subscribe for shares in or debentures of the company or to deposit money with the company. A public company does not suffer this restraint although any public issue or offer may only be made by the medium of a prospectus registered by the Australian Securities and Investments Commission (ASIC) or with the benefit of an exemption from this requirement granted by the Commission.

c. Directors

A public company requires a minimum of three directors, at least two of whom must be Australian residents.

A proprietary company need only have at least one, and one Director must be an Australian resident.

d. Secretaries

A public company must have at least one secretary who must ordinarily reside in Australia.

A proprietary company is not required to have a secretary but, if it does have one or more secretaries, at least one of them must ordinarily reside in Australia.

e. Financial Reports and Audit

Public companies and large proprietary companies must file a copy of their financial reports and the reports of the directors and auditors each year. Auditors must be appointed.

A small proprietary company must also appoint an auditor and file a copy of their financial reports and the reports of the directors and auditors each year if one of the following conditions applies:

i) required by shareholders with at least 5% of the votes,
ii) requested by the Australian Securities and Investments Commission,
iii)the company is controlled by a foreign company.

The financial statements of the company must be prepared in accordance with applicable approved accounting standards which carry the force of law in Australia under the Corporations Act.

In addition to these obligations, it is the responsibility of the directors of all companies to form an opinion that:

i. the financial statement is drawn up so as to give a true and fair view of the financial position and performance of the company for each financial year;

ii. there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable; and

iii. the accounts of the company have been prepared in accordance with the Corporations Act and comply with Accounting Standards and Corporations Regulations.

4.6.4 In the case of all companies:

a. neither a body corporate nor a person under 18 years may be a director;

b. shareholders have no personal liability for the debts of the company beyond an obligation to contribute any capital unpaid on the shares which they hold in a company limited by shares or to pay the amount guaranteed by them to the company where the company is limited by guarantee.

4.6.5 All Australian companies governed by the Corporations Act have the rights, powers and privileges of natural persons (as well as those peculiar to companies) unless limitations exist or have been adopted in its constitution.

4.6.6 Any company incorporated in Australia may carry on business or establish a place of business in any State or Territory.

4.6.7 A foreign company may not commence to carry on business or establish a place of business in Australia unless it is registered as a foreign company.

Registration is achieved by filing a certified copy of its constitution, evidence of its existence in the form of a certificate from the regulatory authority in the place of incorporation, a list of officers and the name of a natural person who has been authorised by the company to accept service of notices on its behalf.

It must file a copy of balance sheet, profit and loss statement and cash flow statement and any other documents as the company is required to prepare by the law applicable in the company's place of origin in each year.

A registered foreign company has the same power to hold land in the State or Territory in which it is registered as if it were incorporated there.

4.6.8 All companies registered in Australia will be issued with an Australian Company Number (ACN) or Australian Registered Body Number (ARBN) in the case of a foreign company which is unique to each company.

The number is required to be displayed on all public documents, including:

- Business letters
- Statements of account
- Invoices
- Receipts
- Orders
- Written advertisement making a specific offer

The number is also required to be displayed on eligible negotiable instruments such as:

- Bills of Exchange
- Promissory Notes
- Cheques
- Letters of credit which are issued or signed on behalf of the company

The number will also be displayed on all documents required to be lodged with the Australian Securities and Investments Commission under the Corporations Act.

The ACN/ARBN must appear on the common seal itself. However, use of the common seal is not obligatory.

4.6.9 Legislation for registering business names exists in all States and Territories and is administered by the State Governments.

4.6.10 Registration of a business name should not be used as a means of protection of a trading name. The proprietor of a registered name does not thereby obtain any ownership rights to the name. In any case, the Governments are always vigilant to reject applications which they suspect are made for this purpose.

Apart from using the name so as to create a reputation for it in the marketplace, one legitimate means of protection is to incorporate a subsidiary company under the desired name. If the name is inherently distinctive and otherwise eligible, an application may be made either by an Australian entity or a foreign party, to register it as a trade mark in Australia under the Trade Marks Act, 1995.

4.7 Trusts

4.7.1 A trust is a fiduciary relationship in which one person, known as the trustee, is the holder of an interest in property (the trust fund) subject to an equitable obligation to use and to keep the trust property for the benefit of another person or some specific object or purpose (the beneficiary).

4.7.2 Traditionally trusts have been used as repositories for family wealth to create a series of limited successive interests, to provide employee benefit schemes, as vehicles for public investment in large projects, to facilitate borrowings by a public company from a large number of individual lenders and for charitable purposes.

Having for many years, been the subject of favourable tax treatment in Australia in comparison to companies, trusts have assumed a significant role in business and investment activities.

Australian tax is levied at progressive rates according to the taxable income of the taxpayer. Trusts themselves are not liable to taxation provided that the entire net taxable income of the trust in each financial year is distributed or allocated by the trustee to beneficiaries with a present entitlement and not under a legal disability which would prevent immediate use or enjoyment of the income.

This provides an incentive for the principal income receiver in a family to split the income with other members of the family so as to take advantage of lower marginal tax rates and thereby reduce the total tax liability.

It is possible for the goodwill and assets of a business to be transferred into an Australian trust with authority, in a written deed of settlement, for the trustee to carry on that business for the benefit of the beneficiaries. This is known as a trading trust. A trustee of a trading trust is personally liable to third parties for debts incurred but is entitled to an indemnity out of the trust fund for those liabilities which were properly incurred in accordance with the trustee’s powers. In any case, most trustees of trading trusts are proprietary companies with a minimum paid up capital and no assets in their own right. The directors and shareholders of such trustee companies are normally family members of the participants in a particular business venture.

Beneficiaries of most trusts can enjoy the advantage of limited liability.

4.7.3 There are three types of trusts commonly used:

a. a fixed trust where the quantum of the interests of a small range of beneficiaries in capital and income is stipulated in the trust instrument;

b. a discretionary trust where the trustee has an absolute discretion regarding the distribution of capital and income amongst a wide range of nominated beneficiaries;

c. a unit trust where the trustee holds the trust fund for the benefit of the beneficiaries, known as the unit holders, each having a number of units of entitlement in the trust carrying a right or differential rights to beneficial ownership of the capital and annual income of the trust. This vehicle particularly suited to a business venture carried on by several persons or groups not connected by family ties. It is a tax effective alternative to a partnership. Unit holders are generally trustees of other discretionary trusts who may then spread the annual income received amongst a number of beneficiaries to take advantage of the tax considerations already referred to in 4.7.2. The deed of settlement for a unit trust should exclude personal liability on the part of unit holders.

4.7.4 All trustees are subject to the rule against perpetuities which forbids the creation of interests in property which endure for an excessively long period, ie. more than 21 years after the death of a party living at the date of creation of the trust. Specific legislation in a number of States, such as the Perpetuities Act, 1984 in New South Wales, authorises the creation of trusts for terms not exceeding 80 years. So far as the life span of natural persons is concerned this confers a benefit comparable to the perpetual succession of corporations.

4.7.5. The tax liability on income received by minors are as follows:

Income	Tax Rates
\$0 - \$416	Nil
\$417 - \$1,307	Nil + 66% of the excess over \$416
over \$1,307	45% of the total amount of income that is not excepted income

4.7.6. The income of publicly owned trading trusts is taxed at the rate applicable to companies.

5. DIRECT TAXATION

5.1 The Legislation

The income tax system in Australia is effective through a variety of separate Acts of the Commonwealth Parliament:

a. the Income Tax Assessment Act, 1936 and the Income Tax Assessment Act, 1997 are the principal Acts dealing with, but not imposing an income tax;

b. the Income Tax Regulations are made pursuant to the two principal Acts to prescribe how certain parts of those Acts are to be implemented;

c. the Income Tax Rates Act impose the actual tax on income as determined under the Income Tax Assessment Acts;

d. International tax treaties are given force of law by the International Tax Agreements Act, 1953 which provides that the treaties shall have effect despite any inconsistencies with other Australian tax legislation;

e. the Taxation Administration Act, 1953 and Regulations made under it deal with the administration and powers of the tax authorities in the areas of tax clearance certificates, offences and prosecutions.

5.2 Personal Income Tax

Tax is payable by residents of Australia on their world-wide income and by non-residents on their income derived within Australia.

The current tax rates are (from 1 July 2021):

Income Range (AUD)	**Marginal Rate of Tax Payable**	
	Residents	**Non-Residents**
$0 - $18,200	Nil	32.50%
$18,201 - $45,000	19%	32.50%
$45,001 - $120,000	32.50%	32.50%
$120,001 - $180,000	37%	37%
$180,001 - and over	45%	45%

The Australian financial year runs from 1 July to 30 June.

Wage earners pay tax by instalment deductions which are withheld from salary by an employer. Other income is subject to a system of tax payment called PAY-AS-YOU-GO (PAYG) on either an annual or quarterly basis dependent upon the extent of the taxpayer’s liability.

5.3 Partnerships

Partnerships carrying on business in Australia are required to lodge a Partnership Return with the Australian Taxation Office. Partnerships as such are not liable to taxation. However, partners must include in their own personal Income Tax Returns the share of the partnership income which each partner is entitled to receive. Individual partners are also entitled to claim their respective share of any partnership loss.

The obligation to lodge a Partnership Return applies in many situations where a partnership does not in fact exist in law. The receipt of income from jointly held property, even though the property is not held by the owners as partners, requires the lodgement of a Partnership Income Tax Return. At general law, the joint receipt of income from the joint ownership of property would not necessarily constitute a partnership business. Nevertheless, for convenience, the income tax law requires a joint return that is the Partnership Return to be lodged.

The "net income" of the partnership is determined by deducting all the allowable deductions from the partnership's assessable income. A "partnership loss" is the excess of allowable deductions over assessable income. A "partnership loss" is not carried forward for deduction against future years' assessable income, but the individual partners are allowed their share of the loss as a deduction against their respective assessable incomes.

5.4 Fringe Benefits Tax

Fringe benefits granted to employees of a non-cash nature, are taxed in the hands of employers on the basis of their assessed value.

The Fringe Benefits Tax Assessment Act, 1986 specifically identifies categories of benefits and provides for the assessed value to be determined either by a statutory formula or an actual usage basis, supported by substantiation rules. The specific categories of benefits include:

a. car fringe benefits;

b. debt waiver fringe benefits;

c. loan fringe benefits;

d. expense payment fringe benefits;

e. housing fringe benefits;

f. living away from home allowance fringe benefits;

g. board fringe benefits;

h. car parking fringe benefits;

i. employee entertainment fringe benefits;

j. property fringe benefits;

k. residual fringe benefits;

The current rate of tax is 47.0% of the grossed up value of the benefits. Where the FBT liability exceeds AUD 3,000 (based on the previous year's annual fringe benefits tax liability), the tax is collected by three quarterly instalments with the fourth and final instalment being payable with the annual return lodged in April each year. The tax paid is an allowable income tax deduction.

Foreign based employers need to be aware of this tax when structuring remuneration packages for their Australian based employees.

Where a remuneration package is paid by a non-resident employer not subject to the Fringe Benefits Tax Assessment Act, the employee will be liable for income tax in respect of the value of allowances relating to the employment.

5.5 Resident Companies

Most companies pay tax at a flat rate of 30% of taxable income while the rate of 25% applies for those small business company with annual turnover less than $50 million in 2021-2022 income year and 80% or less of their assessable income is passive income. There is no minimum level of income which is not subject to tax.

The taxable income of companies (other than those acting as trustees) is calculated in the same way as for individuals.

Generally speaking, the Australian Taxation Office will not permit taxpayers to adopt a substituted fiscal year other than the one ending on June 30. Approval may be granted where a company has a non-resident parent company with an alternative balance date.

5.6 Imputation System

5.6.1 Franking Credits and Debits

The basis of the imputation system is that tax paid by a company on its income is imputed to shareholders who receive dividends. From a shareholders' viewpoint, this means that dividends are tax free to the extent of the imputed tax and are known as "franked" dividends.

The legislation adopts the concept of a franking account. A company has a franking surplus in its account at a particular time in a franking year where the total credits of the company arising in the franking year (up to the time a dividend is paid) exceed the total franking debits of the company to that time.

A company that has a franking surplus is required to use it when it pays dividends to its shareholders. In order to receive the various franking credits and franking debits a company must be sufficiently resident in the year of income to which those credits and debits relate. A company will be sufficiently resident if it is either resident for more than one half of the year of income or is resident at all time during which the company exists. This ensures that a franking credit will not arise just because the company is resident at the time it receives an assessment for a particular year of income.

The residence test applies to franking credits in respect of the payment of company tax instalments, service of company tax assessments, service of an amended company tax assessment increasing company tax liability and the reduction of a foreign tax credit previously allowed.

The sufficiently resident requirement applies to a particular year of income to which the franking credit relates. Thus an assessment of company tax for a year of income received in a later year requires the company to have been sufficiently resident for the year of income to which the assessment relates.

The company must also be sufficiently resident to debit its franking account in respect of the application of a company tax instalment against a company tax assessment, the service of an amended assessment reducing the income tax liability and the allowance of a foreign tax credit. In order for a company to be able to frank a dividend it must be a resident at that time. The payment of a franked dividend gives rise to a franking debit.

5.6.2 Franked Dividends

A shareholder who is a resident individual at the time of the payment of the franked dividend is required to return as assessable income the grossed up amount of the dividend consisting of the amount received plus the amount of the underlying company tax attributable to the dividend. The assessment issued to the taxpayer will have tax calculated on the taxable income, including the grossed up dividend, and will allow as a rebate an amount not exceeding the franking credits.

Where franked dividends are paid to a non-resident there is no withholding tax levied on such dividend. Franked dividends received by non-residents are not subject to any Australian tax, however the withholding tax provisions continue to apply to unfranked dividends paid to non-residents.

Where franked dividends are received by partnerships, generally the Income Tax Assessment Act seeks to look through the partnership, the franking credit will be available for the partners to utilise.

Where such dividends have been received by a trustee, the Act looks through trusts, provided there is net income of the trust estate, the franking credit will be available for the beneficiaries to utilise.

For a resident company which derives income from foreign sources a franking debit will arise where the Commissioner serves a notice of determination that the foreign tax credit is allowable or a determination increasing the foreign tax credit. Where an assessment for tax includes the allowance of a foreign credit, no franking credit will arise in respect of that amount of tax in respect of which foreign tax has been paid and is subject to the credit. A franking credit will arise where the Commissioner serves a notice of determination reducing a foreign tax credit in respect of tax paid or payable.

The allowance of a foreign tax credit reduces the franking surplus which would otherwise be available for a distribution as a franked dividend.

The effect of this is that shareholders in companies which derive a substantial portion of their income from foreign sources, which income is subject to tax in foreign countries and allowable as a credit in Australia, will receive mainly unfranked dividends.

5.7 Trust Estates

A trustee is generally not liable to pay income tax on the income of the trust if beneficiaries presently entitled and not under any legal disability are assessed in respect of such income.

Beneficiaries are liable to tax on that income, aggregated with any other income derived by them, at normal personal or company rates. The net income of a trust estate is calculated as if the trustee were a taxpayer.

Losses incurred by a trust are not capable of distribution to beneficiaries for tax purposes, however they can be carried forward to off-set against income derived in future years.

Where a trustee is separately assessed on income to which no beneficiary is presently entitled (other than in the case of a deceased estate) the maximum personal rate applies.

In the case of beneficiaries under a legal disability and in the case of non-resident beneficiaries the trustee is liable to pay tax imposed on that part of the trust income to which that beneficiary is entitled, without the benefit of any deductions. Where the beneficiaries have an obligation to lodge a tax return they will receive a credit for amounts paid by the trustee.

5.8 Capital Gains and Capital Losses

Capital gains form part of a taxpayer's assessable income, while capital losses are only capable of being off-set against capital gains. The main characteristics of the capital gains and capital losses tax legislation are:

a. it applies only to the actual disposal of an asset, however there are extensions by definition that apply to deemed disposals and deemed or notional assets;

b. the limited exemptions in the legislation include a taxpayer's principal residence and gains with respect to payments of superannuation and life assurance policies;

c. death will not constitute a disposal, but will constitute a roll-over where the asset was acquired before 20 September, 1985 for a consideration equal to the market value of the asset, or a new cost base for assets acquired subsequent to 19 September, 1985;

d. the tax applies to property acquired after 19 September, 1985;

e. the tax only applies to the capital gain after (i) deduction of the cost base adjusted for the inflation index (applied to assets acquired before 21 September 1999 with inflation index frozen at 30 September 1999) or (ii) applying a statutory discount on the nominal gain (depending on the type of entity holding the assets);

f. the tax is imposed at ordinary rates for companies;

g. for assets acquired prior to 21 September 1999, the tax applying to individuals is subject to a notional five year averaging of the income tax rate;

h. actual capital losses may be off-set against capital gains realised either in the current year or any subsequent year.

It is important to identify what assets may be subject to the provisions of this legislation and how a disposal occurs.

5.8.1 Asset

An asset is defined to mean any form of property and includes:

a. Any form of property created or constructed or otherwise coming to be owned without being acquired, but does not include a motor car and other specified vehicles.

b. An option, a debt, a choice in action, any other right, goodwill and any other form of incorporeal property.

c. Currency of a foreign country.

d. An interest in partnership assets.

Personal use assets are also defined and different rules apply in relation to any disposal of this classification of assets.

The legislation applies to non-residents in respect of the disposal of taxable Australian property which include:

a. a direct interest in real property, or a mining, quarrying or prospecting right to minerals, petroleum or quarry materials

b. a CGT asset that you have used at any time in carrying on a business through a permanent establishment in Australia

c. an indirect Australian real property interest. This is an interest in an entity, including a foreign entity, where: i) you and your associates hold 10% or more of it; ii) the value of your interest is principally attributable to Australian real property

d. an option or right over one of the above

e. land or buildings situated in Australia;

f. an asset that has at any time been used by a taxpayer carrying on a trade or business wholly or partly at or through a permanent establishment in Australia;

g. a share, or an interest in a share, in a resident private company;

h. a share, or an interest in a share, in a resident public company where the taxpayer or his associates own not less than 10% in the issued share capital of the company at any time during the 5 years before the CGT event happens;

i. an interest in a resident partnership;

j. an interest in a resident trust estate;

k. a unit in a resident unit trust where at any time during the period since 19 September, 1985 or five years immediately preceding the time of disposal, whichever is the lesser, the taxpayer or associates or the beneficiaries owners own not less than 10% of the issued units of the unit trust.

l. an option or right to acquire an asset previously referred to in this section; and

m. assets to which the anti-avoidance provisions relating to off-shore restructuring of taxable Australian asset holdings apply.

5.8.2 Disposals and Acquisitions

Where a change has occurred in the ownership of an asset the change is deemed to have effected a disposal of the asset by the person who owned it immediately before the change and an acquisition of the asset by the person who owned it immediately after the change.

A change of ownership of an asset may occur in any way, including the following:

a. by the execution of an instrument;

b. by the entering into any transaction or contract;

c. by the transmission of the asset by operation of law;

d. by the delivery of the asset;

e. by the doing of any other act or event; and

e. for the occurrence of any event.

Other provisions extend the actual disposal concept to deemed disposals and acquisitions in various circumstances, including on emigration or immigration and by loss or destruction.

5.8.3 Emigration and Immigration

Where a non-resident becomes a resident of Australia, every asset that was owned by the person immediately prior to becoming a resident, with the exception of:

a. taxable Australian assets; and

b. any other asset acquired prior to 19 September, 1985 (is deemed to have been acquired by the person at the time of becoming a resident for a consideration equal to the market value of the asset at that time).

The capital gains and capital loss provisions apply to any subsequent disposal of those assets.

Where a resident taxpayer ceases to be a resident he is deemed to have disposed of every asset owned immediately prior to departure, with the exception of:

a. taxable Australian assets; and

b. any other asset acquired prior to 20 September, 1985.

This deemed disposal will not occur on the cessation of residency if the taxpayer:

a. is an individual who was in Australia on 6 April 2006 and has remained as an Australian resident since that date; and

b. was a resident for a total period of less than five years during the previous 10 years; and

c. the asset was owned by the taxpayer prior to becoming a resident or otherwise inherited by death.

If you are an individual, you can choose to disregard all capital gains and capital losses you made when you stopped being a resident. If you ceased being a resident and you make this choice, those assets are taken to be taxable Australian property until the earlier of:

a. A CGT event happening to the assets, or

b. you again becoming an Australian resident.

5.8.4 The legislation also deals with:

a. leases;

b. trusts;

c. shares;

d. convertible notes;

e. options;

f. industrial property;

g. prospecting mining rights;

h. insurance and superannuation;

i. goodwill;

j. the exemption of the principal residents; and

k. roll-over relief relating to the transfer of assets between spouses upon breakdown of marriage, statutory licences, involuntary disposals, property rights, crown leases and various forms of restructuring.

5.8.5 Transitional Provisions

Transitional provisions apply to assets acquired prior to 20 September, 1985 where there are changes in the majority underlying interests in an asset or the underlying property in a private company, partnership or private trust. In the former situation the assets held are deemed to have been acquired on the date that the disqualifying event occurred for the market value at such date. In the latter case, the disposal of shares or an interest in a partnership or trust may result in a deemed capital gain arising.

5.8.6 Determination of a Capital Gain or Capital Loss

The computation of the capital gain or capital loss arising from the disposal of an asset is made having regard to the disposal price and, in the case of a capital gain, either the cost price or indexed cost price. It is the reduced cost price which must be deducted from the disposal price to determine a capital loss.

If a taxpayer has:

a. received or is entitled to receive an amount of money as a result of or in respect of the disposal, the disposal consideration is that amount;

b. received or is entitled to receive property other than money in respect of the disposal of an asset, the disposal consideration includes the market value of the property; and

c. disposed of an asset to a party who is not at arm’s length for either no consideration or inadequate consideration, the taxpayer is deemed to have received as consideration in respect of the disposal an amount equal to the market value of the asset at the time of disposal.

In determining the cost base of an asset disposed of, the cost base is the sum of:

a. the consideration in respect of its acquisition;

b. the incidental costs to the taxpayer of the acquisition;

c. any expenditure of a capital nature incurred by the taxpayer to the extent to which it was incurred for the purpose of enhancing the value of the asset and is reflected in the state or nature of the asset at the time of disposal;

d. any expenditure of a capital nature incurred by the taxpayer to the extent to which it was incurred in establishing, preserving or defending the taxpayer's title, or a right over the asset;

e. the non-capital costs of owning an asset (restrictions apply) and;

f. the incidental cost to the taxpayer of the disposal.

For assets acquired before 21 September 1999, there are two methods to determine a capital gain:

i. the indexed cost base is calculated by applying the indexation factor for the period subsequent to incurring the costs. The resultant capital gain is arrived at by deducting the indexed cost base of the asset from the disposal consideration; or

ii. the nominal gain is worked out without the cost base being indexed. The resultant capital gain is arrived at by deducting the nominal gain by a discount percentage (50% for individual and trust; 33 1/3% for a complying superannuation fund). Company is not eligible for a capital gain discount. Further, it should be noted that the removal of CGT discount for foreign resident has now become law. The 50% capital gain discount is only available to foreign resident on capital gain accrued prior to 8 May 2012 provided the real estate are held for more than 12 months and a written market valuation is obtained from a certified valuer.

For assets acquired after 21 September 1999, indexed cost base method is not available.

In calculating the capital loss the cost base is reduced by any outgoings for which the taxpayer would have been entitled to a deduction for income tax purposes. The disposal consideration is then deducted from this reduced cost base to determine the capital loss.

5.9Other Tax Matters

5.9.1 Entertainment Expenses

Expenditure on entertainment (food, drink, recreation, accommodation or travel associated with it) is not an allowable deduction whether or not associated with business. This applies equally to employers and employees.

Exceptions are available:

a. where a taxpayer provides entertainment in the ordinary course of business, e.g., restaurants or airlines;

b. for entertainment in the form of promotional give-aways available to the public at large;

c. for expenditure in promoting or advertising goods or services to the general public:

d. for allowances paid to employees which are assessable in the hands of the employees;

e. for providing in-house dining and recreation facilities to employees on working days.

From 1 April, 1994 employee entertainment expenses will generally become income tax deductible to the employer but will be subject to fringe benefits tax (see 5.4).

5.9.2 Substantiation

Individuals and partnerships, but not companies and trusts, are required to keep a contemporaneous record of specified expenditure on car and travel expenses and some other deductible expenses detailing amounts, dates and descriptions of expenditure. Without this record no deduction will be available.

5.9.3 Negative Gearing

Negative gearing is the practice of borrowing on the security of income producing assets so that the annual interest on the debt and other outgoings, which are tax deductible, exceeds the annual income derived from the property.

5.10 Death and Gift Duties

Death, estate and gift duties have been abolished throughout Australia.

6. KEY ISSUES IN AUSTRALIAN INCOME TAX LEGISLATION

6.1 Income

Assessable income comprises two main classes of receipts:

a. those which are income in accordance with ordinary concepts and usages, e.g., income received as salaries or wages, sales made by business, etc;

b. those which are not in the former category but are made assessable income by reason of specific provisions in the legislation, e.g., increases in trading stock, recoupment of depreciation, etc.

There is no definition of "income" in the legislation. The Australian Courts have drawn a basic distinction between income and capital with the result that an amount which is capital in nature is not taxed unless some express statutory provision requires it. One illustration is capital gains tax. The distinction between income and capital has meant that where a taxpayer acquired property as a genuine investment, e.g., shares for the dividend income they will produce, then any profit on the subsequent disposal of that property is treated as capital (refer section 5.8 for tax implication).

6.2 Allowable Deductions

The taxable income of any Australian taxpayer is determined by deducting from assessable income allowable deductions in two basic groups.

6.2.1 Those expenses necessarily incurred in gaining or producing the assessable income or in carrying on a business are allowable deductions to all taxpayers, whether resident or non-resident. The following conditions must be satisfied:

a. the losses and outgoings were incurred in the relevant year by the taxpayer;

b. they are deductible to the extent to which:

i.they are incurred in gaining or producing the assessable income; or

ii. they are necessarily incurred in carrying on a business for the purpose of gaining or producing assessable income;

c. they are not capital, or of a capital, private or domestic nature;

d. they are not incurred in relation to the gaining or production of exempt income.

A deduction is allowed for losses and outgoings which have been incurred and it is not necessary that payment should actually have been made. However, no deduction is generally allowed for provisions made for expected expenditure such as for doubtful debts or employee leave.

6.2.2 The legislation authorises deductions for certain specific items and prescribes the conditions under which such expenditure is deductible, for example:

a. repairs;

b. commission;

c. legal expenses;

d. borrowing expenses;

e. losses incurred through embezzlement, larceny or misappropriation;

f. expenditure on scientific research and development;

g. gifts;

h. superannuation contributions for the benefit of employees;

i.subscriptions to associations;

j.bad debts.

6.3 Residence

6.3.1 A natural person is treated as resident for the purpose of Australian income tax law if that person's domicile (broadly, the place that is your permanent home) is in Australia or if you're actually present in Australia for more than half the income year (183 days), whether continuously or with breaks, you may be said to have a constructive residence in Australia, unless it can be established that your usual place of abode is outside Australia and you have no intention of taking up residence here. On the other hand, an individual will be a non-resident if he can demonstrate to the satisfaction of the Commissioner of Taxation that his permanent place of abode is outside Australia.

The government has indicated as 11 May 2021 that it is proposing to replace the individual tax residency rules with a new, modernised framework. The primary test will be straightforward – a person who is physically present in Australia for 183 days or more in any income year will be an Australian tax resident. Individuals who do not meet the primary test will be subject secondary tests that depend on a combination of physical presence and measurable, objective criteria.

The new framework is based on recommendations made by the Board of Taxation in its 2019 report on the residency rules. It will apply from the first income year after the enabling legislation receives assent.

6.3.2 A corporation will be resident of Australia:

a. if it is incorporated here; or

b. although not incorporated in Australia it carries on business in Australia and either:

   i. has its central management and control in Australia; or

   ii. has its voting power controlled by shareholders who are themselves residents of Australia.

   The most important single factor in locating central management and control of a company is where the meetings of directors take place.

6.4 Source

Generally speaking, the determination of the source of particular items of income is made in accordance with general legal principles and involves an assessment of the relevant facts. The Income Tax Assessment Act does, however, create specific tests for certain types of income. For example, interest paid on borrowings secured against Australian property is treated as having a source in Australia irrespective of the place from which payment is made.

6.5 Foreign Currency Gains and Losses

The issue of foreign currency gains and losses arise as a result of Section 960-50 of the Income Tax Assessment Act which requires transactions to be expressed in Australian currency.

The assessibility and deductibility of gains and losses may be summarised as follows:

a. Repayment of liabilities for trading activities result in any exchange gains being assessable and losses deductible according to the general concepts of income and outgoings.

b. Gains and losses of a capital nature relating to borrowings utilised for the purpose of producing assessable income are governed by specific legislation. Where the foreign exchange gains or losses of a capital nature relate to contracts entered into on or after 19 February 1986, they are assessable or deductible, as appropriate. The effect is that foreign exchange gains and losses of a capital nature are treated in the same way as exchange gains and losses on borrowings or loans of a revenue nature, provided that the borrowings or loans were used for producing assessable income.

c. Gains and losses made on forward cover contracts and hedge contracts to eliminate or reduce the foreign exchange risk are also assessable or deductible.

d. Other transactions in foreign currency will be subject to the capital gain and capital loss provisions.

7. TAXATION OF NON-RESIDENTS

7.1 Individuals

Non-resident individuals are subject to tax on income derived in Australia at the rates shown in the table at 5.2.

7.2 Companies

Non-resident companies which carry on business in Australia through a branch or derive income from Australian sources pay tax at normal corporate rates.

7.3 Withholding Tax

7.3.1 Dividends and interest derived by a non-resident who does not have a permanent establishment in Australia, irrespective of his place of residence, are subject to withholding tax.

In the case of unfranked dividends, the rate of withholding tax is 30% of the gross amount of the dividend or, in the case of countries with which Australia has double tax agreements, 15% applies (United States and United Kingdom resident companies may receive a 0% or 5% on unfranked dividends received in some cases). Franked dividends do not attract withholding tax when remitted overseas.

The rate of withholding tax applicable to interest paid by a resident of Australia to a non-resident is 10% of the gross amount.

7.3.2 Income derived by a non-resident that consists of a royalty is deemed to have an Australian source where either:

a. a resident has paid the royalty and such royalty is not an outgoing incurred by the resident carrying on business through a permanent establishment outside of Australia; or

b. a non-resident has paid the royalty and it is an outgoing incurred by the non-resident in carrying on business at or through a permanent establishment in Australia.

Such royalties are subject to Australian tax provided that the payments are income according to ordinary concepts and are not capital payments.

Royalties cannot be remitted to a non-resident unless the payer first informs the Australian Taxation Office and deducts a sum sufficient to meet the tax liability determined by that Office.

Royalties are subject to withholding tax at 30%. Under most treaties, the rate is reduced to 15%, however other rates may apply.

. 7.3.3 Withholding taxes are deducted from the gross amount of the payment at source by the payer of the dividend, interest or royalty.

. 7.3.4 Foreign resident capital gains withholding (FRCGW) rate and threshold for contracts entered into on or after 1 July 2017:

a. for real property disposals where the contract price is $750,000 and above;

b. the FRCGW withholding tax rate will be 12.5%.

7.3.5 A permanent establishment is a place at or through which a business is carried on, including a place:

a. where a person carries on business through an agent;

b. where a person has, is using or is installing substantial equipment or machinery;

c. where a person is engaged in a construction project; and

d. where the person is engaged in selling goods manufactured, assembled, processed, packed or distributed by another person for, or at or to the order of, the first-mentioned person and either of those persons participates in the management, control or capital of the other person or another person participates in the management, control or capital of both of those persons - the place where the goods are manufactured, assembled, processed, packed or distributed.

It does not include:

a. a place where the person is engaged in business dealings through a bona fide commission agent or broker who, in relation to those dealings, acts in the ordinary course of his or her business as a commission agent or broker and does not receive remuneration otherwise than at a rate customary in relation to dealings of that kind, not being a place where the person otherwise carries on business;

b. a place where a person is carrying on business through an agent i) who does not have or does not habitually exercise a general authority to negotiate and conclude contracts on behalf of the person; or ii) whose authority extends to filling orders on behalf of the person from a stock of goods or merchandise situated in the country where the place is located, but who does not regularly exercise that authority, not being a place where the person otherwise carries on business; or

c. a place of business maintained solely for the purpose of purchasing goods or merchandise.

Each double tax treaty also has a definition of permanent establishment which needs to be referred to in particular cases.

7.4 Trust Income

Where a non-resident beneficiary is presently entitled to a share of the income of a trust estate which is attributable to sources within Australia the trustee will be assessable to Australian tax in respect of this income. The share of income of the trust estate to which the non-resident beneficiary is presently entitled and which is attributable to sources within Australia will also be included in the beneficiary's assessable income.

Any tax paid by the trustee in respect of the entitlement of the beneficiary will be offset against the assessment of the beneficiary. However, where the tax paid by the trustee exceeds the beneficiary’s tax payable, the beneficiary will not be entitled to a refund.

In this way the Act imposes on trustees a form of collection of tax at source on behalf of non-resident beneficiaries of trust estates.

7.5 Double Tax Agreements

Australia has treaties with 45 countries to provide relief from international double taxation and to prevent fiscal evasion. Those countries are:

Argentina
Austria
Belgium
Canada
Chile
China
Czech Republic
Denmark
Fiji
Finland
France
Germany
Greece
Hungary
India
Indonesia
Ireland
Italy
Japan
Kiribati
Malaysia
Malta
Mexico
Netherlands
New Zealand
Norway
Papua New Guinea
Philippines
Poland
Romania
Russia
Singapore
Slovakia
South Africa
South Korea
Spain
Sri Lanka
Sweden
Switzerland
Taipei
Thailand
Turkey
United Kingdom
United States
Vietnam

The agreements are always bilateral and modify the rights of the parties to tax income and profits under their individual domestic laws.

Generally speaking the agreements are substantially similar although each has some unique features and must be looked at individually.

The one consistent theme is that:

a. certain income is taxed in its place of origin;

b. certain income is taxed in the place of resident of the recipient; and

c. other income is taxed on a modified basis in the place of source with the place of residence also being entitled to tax the income and allow a credit in respect of either withholding tax or tax paid in the place of source.

7.6 Foreign Tax Credit System

Resident taxpayers must include all foreign income as part of their Australian assessable income (whether subject to foreign tax or not) and claim as a credit whichever is the lesser of:

a. certain approved taxes paid in respect of foreign income, reduced in accordance with any relief, available to the taxpayer under the law relating to that tax; or

b. the Australian tax payable in respect of the foreign income.

An exception to the foreign tax credit system is contained in Section 23AG of the Income Tax Assessment Act 1936 which exempts from Australian tax all earnings in respect of foreign services for a continuous period of not less than 91 days provided the earnings are derived in a foreign country and are not exempt from tax. However, from 1 July 2009, the application of the above section is restricted to income earned by foreign aid works, foreign charity workers and selected Government employees. For all other resident employees who no longer qualify for the exemption under section 23AG, their foreign sourced income will be subject to Australian income tax but on the other hand will be entitled to claim a foreign tax offset.

From 1 July 2004, an Australian company is not entitled to foreign tax credits for foreign tax paid on dividends paid by a foreign company whereby the Australian company holds at least 10% of voting power in the foreign company paying the dividend. These dividends are regarded as “non-portfolio dividends” and are non-assessable non-exempt income under Section 23AI of the Income Tax Assessment Act 1936. Foreign tax credit for foreign tax paid on dividend distributed prior to 1 July 2004 is available to Australian company under the former Section 160AFC of the Income Tax Assessment Act 1936 (now overridden by Section 23AJ).

Non-portfolio dividends received by a resident company from a company that is a resident of a foreign country are non-assessable non-exempt income

Foreign tax means tax imposed by a law of a foreign country (other than a unitary tax) and includes:

a. tax upon income;

b. tax upon profits or gains, whether of an income or capital nature;

c. tax deemed to have been paid in respect of a dividend; or

d. any other tax being a tax that is subject to an agreement having the force of law under the International Tax (International Agreements) Act, 1953.

Excess foreign tax credits can be carried forward for a maximum of five years for application against tax payable on foreign income of the same class.

Foreign interest income is effectively quarantined. The foreign tax credit in respect of it is calculated separately from the credit available for other foreign income.

Certain dividends are deemed to be interest for the purpose of these rules.

Where a foreign company derives interest and that income amounts to at least 10% of its total profits during the period it is deemed to have an interest pool. Dividends paid by the foreign company shall be deemed to have been paid out of the interest pool in the first instance and be deemed interest income derived by the resident company.

7.7 Taxation of Foreign Source Income

Where income is derived by a company that is controlled by Australian residents and that company satisfies the criteria necessary to be a controlled foreign corporation (CFC), the Australian resident's share of the income of the off-shore company will be attributable income assessable in the year in which the CFC balances. Generally, the CFC regime operates to attribute that income which is derived by a controlled foreign corporation, except where;

a. income derived by off-shore entities are subject to a taxation system comparable to that of Australia; or

b. income derived by an off-shore entity predominantly engaged in an active business.

7.7.1 The Control Rule

A foreign company will be controlled foreign company (CFC) where:

a. five or fewer Australian residents own or are entitled to acquire 50% or more of the interests in the foreign company; or

b. a single resident is assumed to have control of a company if the resident, either alone or together with associates, directly or indirectly holds an interest of 40% or more in the company; or

c. five or fewer Australian residents effectively control the foreign company.

The interests of a resident in a foreign company for this purpose will include both direct and indirect interests of the resident and the resident's associates.

7.7.2 Direct Control Interests

A company's direct control interest in a foreign company will be the largest of the percentages that you hold, or are entitled to acquire, of the following:

a. total paid-up share capital in the foreign company;

b. total rights to vote, or to participate in any decision making, in relation to the distributions of capital or profits, the changing of constituent documents and the varying of share capital of the company;

c. total rights to distributions of capital or profits of the company on winding up or other than winding up.

7.7.3 Tracing Rules

When determining whether a foreign company is a CFC, the indirect interests in the company of a resident, and the direct and indirect interests in the company of associates are taken into account in addition to the direct interests of the resident. Indirect interests are also taken into account for the purpose of determining whether a resident is an attributable taxpayer in relation to a CFC, and the percentage of the CFC's income that is to be attributed to the resident. These rules are called the tracing rules.

When determining the indirect interests held by a resident, it may be necessary to trace through various foreign companies, non-resident trusts and partnerships. The tracing rules will only be applied where an entity is a controlled foreign entity. The indirect interests will be determined by a simple multiplication of the interests of each entity in a chain.

7.7.4 The Active Income Exemption

Where a CFC satisfies the various tests under the Active Income Exemption, income derived by the off-shore company will not be attributed to the Australian resident shareholders.

There are three major requirements of the Active Income Test;

a. the CFC must carry on business through a permanent establishment in the country of residence;

b. the CFC must have kept accounts and comply with Australian substantiation requirements in respect of those accounts, prepared in accordance with accounting standards and give a true and fair view of its financial position; and

c. the CFC’s tainted income must be less than 5% of its gross turnover.

Tainted income includes the types of income that are readily susceptible to being shifted to tax havens and consists of passive income (e.g., dividends, interest, royalties and most kinds of gains on disposal of assets) and business income from transactions with related parties and Australian residents. Special rules apply in relation to financial intermediaries and insurance companies.

7.7.5 Determination of the Attributable Amount

When it is determined that a company is a CFC at the end of its statutory accounting period, the attributable income of the CFC will be calculated separately for each attributable taxpayer.

The attributable income of a CFC is calculated based on the rules that apply to Australian taxpayers under the Australian Income Tax Assessment Act.

An attributable taxpayer's share of the attributable income of a CFC is the attribution percentage (ie, the sum of the taxpayer's direct and indirect percentage interest in the CFC) multiplied by the attributable income of the CFC.

7.8 Transfer Pricing

7.8.1 Australia has strengthened its relationship with tax gatherers of other countries in the Asia-Pacific region with the purpose of improving information exchange and audit techniques to identify resident companies using transactions with related overseas entities as a means of profit shifting.

The Australian tax legislation is designed to effectively curtail international tax minimisation arrangements which many businessmen in other jurisdictions might regard as standard commercial practice. Examples are:

a. an Australian resident selling goods or providing services to an affiliate in a low tax country at below market price;

b. an Australian resident paying an inflated management or service fee to an off-shore affiliate or bearing expenses more properly attributable to that affiliate.

7.8.2 Division 13 of the Income Tax Assessment Act, 1936 allows the Commissioner of Taxation to examine transactions:

a. between Australian residents and non-residents which are not at arm's length; or

b. between two non-residents where one has a permanent establishment in Australia.

These transactions may involve goods, services, property rights and rights to receive or have the benefit of income.

Parties are taken to be at arm's length if the only relevant circumstances concerning their relationship are the details of the particular contract. Factors such as influence or control of one party over the other, common shareholdings or directorates will indicate that the arrangement is not one made at arm's length.

Examination is also possible where a sale to or from Australia is made on the understanding that a benefit will be made available to one of the parties outside Australia.

The parties to any of these transactions need not necessarily be independent entities or even legally related entities. A transaction between a head office and one of its branches located abroad may be used to shift profits or losses.

The Commissioner of Taxation is empowered to vary the consideration of the transaction for the purpose of determining the taxable income and tax payable by the Australian taxpayer who is a party to any such international agreement where the consideration is inadequate, excessive or non-existent. In each case the Commissioner may substitute the price that would have been paid if the parties had negotiated at arm's length. In practice information is sought from independent sources to support the decision. In cases of allocation of profits or expenditure between branches and a head office the Commissioner may vary the apportionment.

Application of Division 13 is not mandatory as the Commissioner has a discretion as to whether or not it should apply. It is safe to assume automatic application where taxable income would be removed from Australia.

7.8.3 Parties can enter into an Advance Pricing Arrangement with the Australian Taxation Office.

The Commissioner allows parties to apply for an Advance Pricing Arrangement (APA) which is an agreement between the parties, the Australian Tax Office and where appropriate, a foreign tax authority regarding the income tax treatment of international transactions, agreements or arrangements between related parties and associates. Under the APA program, the parties are required to present their pricing methodology together with supporting documentation to demonstrate and reflect an arm's length result. If the Commissioner accepts an APA, an annual report containing sufficient information to detail the actual results and to demonstrate compliance with the terms and conditions of the APA must be submitted within 90 days of the end of the relevant year.

8. INDIRECT TAXATION

8.1 Goods and Services Tax (GST)

8.1.1 GST on Supply and Input Tax Credit

GST is an indirect broad-based tax of 10% on the supply of most goods, services and anything else consumed in Australia. Since 1 July 2000, GST is paid in each step in the supply chain, with businesses charging GST in the price of goods, services or anything they supply. The supplying entities can claim input tax credits, which are GST they paid for goods and services used for operating their businesses. The effect of this is that the end-users or private consumers will ultimately bear the GST. The businesses within a chain of supply only act as progressive collectors of the tax but do not bear the ultimate burden of it.

8.1.2. Registration

To claim input tax credits and to be liable for charging GST, an entity must register with the Australian Taxation Office. Registration is compulsory if business's annual turnover is AUD 75,000 or more, or non-profit organisation has a turnover of AUD 150,000 per year or more.

8.1.3 Non Taxable Supplies

The following supplies are not subject to GST:

a. gifts
b. supplies by unregistered entities and not required to be registered
c. transactions that have no connection with Australia
d. appropriation made between government agencies
e. services provided as employees

8.1.4 GST Free Supplies

GST is also not payable on a GST-free supply similar to 8.1.3. If a supply falls within this category, the supplier is still entitled to claim input tax credits for the GST paid in its business input although no GST is charged on its supply.

The main types of GST-free supply are:

a. exports (conditions and restrictions apply)
b. health and medical care
c. education and child care
d. food for human consumption (exclude restaurant, takeaways, prepared food, bakery, confectionery, alcohol and most drinks)
e. charities, religions and gift-deductible bodies
f. international transport and travel
g. supply of going concern such as sale of business
h. grant of Crown Land

i. sale of farm land
j. water, sewerage and drainage
k. cars for disabled persons

8.1.5 Input Taxed Supplies

If a supply is “input taxed”, no GST is payable on it, but the supplier cannot claimed input credits for the GST paid on its business input that relate to that supply. Input taxed supplies include:

a. financial supplies such as loans and dealings in money (covering most financial institutions)
b. supply of private residential rental properties
c. sales of residential properties that are not newly developed or substantially refurbished
d. fund-raising activities of charities
e. certain transactions involving precious metals

8.2 Customs Duty

Certain goods imported into Australia are subject to customs duty, the rate of which depends on the tariff classification under which the goods fall and the country of origin. Duty is assessed on the price paid or payable for the goods as adjusted to take into account elements of value not already included in the price.

8.3 Land Tax

Land tax is levied by all Australian States and Territories upon the owners of real estate. The tax is payable on the aggregate "taxable value" of all real estate owned by a land owner whether he be an individual, company, trust or partnership.

Generally, the principal residence of a land owner is exempt from land tax. The tax is levied at AUD 100 plus 1.6% of land value in excess of AUD 755,000 for 2021 land tax year, meanwhile a premium land tax marginal rate of 2% will apply if the total taxable land value is above AUD 4,616,000.

In 2017, the NSW government introduced the land tax surcharge to foreign persons who own residential land in NSW. The current surcharge is 2% on the land value.

The potential liability to land tax should be considered when an investment in real estate is contemplated.

8.4 Stamp Duty

Stamp duty is a tax imposed by every Australian State and Territory on written instruments created to give effect to legal transactions. More recently the scope of stamp duty has been widened to cover situations where transactions are entered into without bringing into existence a written document.

Although stamp duty is prepaid in some cases most legal documentation subject to stamp duty must be submitted to the Stamp Duties Office for assessment and subsequent payment of duty.

A taxpayer's liability to stamp duty will vary in accordance with the type of transaction and instrument entered into. In some cases a flat rate is applied, whereas in others duty may be applied on an ad valorem basis. Duty payable on a transfer of premium property in New South Wales for instance, where the value of the property is in excess of AUD 3.194 million will be AUD 160,237 plus 7% of the excess over AUD 3 million.

8.5 Payroll Tax

Payroll tax is levied by State and Territory governments upon employers with a yearly payroll in excess of the specified amount ($1.2 million in New South Wales). No tax is payable where the payroll is below this specified amount. Payroll tax is imposed as a percentage of salaries, wages and benefits paid by the employer in excess of the jurisdiction threshold (in New South Wales, the current rate is 4.85%).

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