TAX TALKS

Australia's Tax News Podcast - The Podcast for Australian Tax Professionals

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What happens to your tax position when you expand overseas?

Expand Overseas

Business is going well in Australia and so you want to expand overseas. What are the tax implications when you do? This is what Clint Harding of Arnold Bloch Leibler in Sydney will discuss with you in this episode.

Here is what we learned but please listen in as Clint Harding explains all this much better than we ever could.

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Expand Overseas

Australia's policy is to give you a system that taxes your overseas activities no more harshly than your overseas competitors are taxed. Australia needs exports and hence treats lightly when it comes to charging taxes on your overseas income.

Tax should not be the reason why you don't expand overseas. So we have s768A ITAA97 that allows you to pay dividends from your overseas company back to your Australian company without any further tax (by treating those dividends as NANE).

On the same hand Australia doesn't want you to transfer taxable profits overseas avoiding Australian tax altogether. So we have the CFC rules, the Controlled Foreign Company rules. We have the CGT-free disposal of overseas shares where you have an interest of greater than 10%. And so on. All this is designed to give you a level playing field.

New Zealand

The world is a big place and the double tax treaty with one country is very different to the one with another. So let's use New Zealand as an example.

No Tax Unless a Permanent Establishment

It starts with the tax treaty between Australia and New Zealand that talks about PEs. Per Article 7 of this DTA (double tax agreement) profits of an Australia enterprise shall be taxed only in Australia unless that enterprise carries on business in New Zealand through a permanent establishment.

So no tax in New Zealand unless you have a permanent establishment (or entity) there.

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PE Triggers

What triggers a permanent establishment (‘PE’)? Usually a fixed place of business and dependent contractors or employees on the ground will trigger a permanent establishment in any country. Same in NZ.

The rules generally distinguish between employees and contractors. And then also between independent and dependent contractors. So the questions are: Do they work for other people? Do they have authority to sign contracts? Do they follow instructions like an employee would?

Look at paragraph 9 Article 5 of the tax treaty for an in depth analysis of what makes a contractor independent or dependent.

But, “An enterprise shall not be deemed to have a permanent establishment if it just carries on business in New Zealand through a broker / general commission agent or any other agent of an independent status provided that such persons are acting in the ordinary course of their business as a broker.”

So as long as you just employ independent agents – no PE.

Attribution

So if you have a PE, which portion of your profits is subject to tax in New Zealand?

The tax treaty again, “Profits may be taxed in New Zealand but only so much of them is attributable to that in PE.”

So this is all about transfer pricing. The question of how much of the net profit belongs to Australia or New Zealand.

Withholding Tax

But once you have paid income tax in New Zealand through your PE or company, you are not done yet. There is also a 5% or 15% withholding tax on any profits you pass on from New Zealand to Australia. It is 5% on dividends, if the beneficial owner of those dividends is a company which holds directly 10% of the New Zealand company.

So if John has a holding company in Australia that holds 100% shares in a New Zealand company, the withholding tax is 5%, otherwise 15%.

Franking Credits

Australia and New Zealand are two of only four countries in the world that have an amputation system. Mutual recognition of franking credits – so Australians can claim NZ franking credits and vice versa – has been a discussion point between the two countr but without any results yet.

So Australian tax residents can’t claim NZ imputation credits. And New Zealand tax residents can’t claim Australian franking credits.

s768A ITAA 1997

Non-portfolio dividends are any dividends you receive from a company where you hold more than 10%. Those dividends arrive in Australia as NANE. NANE stands for non-assessable non-exempt income. So NANE is good. It means no further tax.

However, once you distribute those dividends to Australian shareholders, they arrive without franking credits, so result in tax leakage.

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