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TAX CONSIDERATIONS FOR INBOUND EMPLOYEES - NOVEMBER 2008

Many companies, particularly in the mining, engineering, construction and IT related industries source skilled employees from overseas

The Australian taxation implications for such inbound employees are an important consideration for Australian employers who will often be expected to meet any additional tax costs of the employee's employment in Australia. On the other hand, employers are able to utilise Australian tax laws to their advantage in providing attractive employment remuneration proposals to potential staff.

The How are Expatriate Employees Taxed?

Employment income is taxed in the individual's country of residence provided the following conditions are met:

- The employee is not physically present in the country where services rendered for more than 183 days in a 12 month period; and
- The remuneration paid by (or on behalf of) an employer who is not in the country of service; and
- The remuneration is not deductible in determining the taxable profits of a permanent establishment or a fixed base which the employer has in the service country.

Where the above conditions are not satisfied, individuals are taxed on employment income in the country in which the services are rendered subject to the Double taxation Agreement ("DTA") between the country of residence and the country of service.

Residency

Expatriates employed by Australian employers are classified as either a resident, non-resident or temporary resident for Australian tax purposes. This classification along with the DTA between Australia and their country of origin will determine how employment income paid by Australian employers is taxed. In general, residents are taxed on worldwide income and non-residents and temporary residents are taxed only on Australian income.

The question of whether an individual is a resident for Australian tax purposes must be determined in consideration of whether an individual resides in or is domiciled in Australia within the normal understanding of the concepts. Factors to be considered include: the location of their home or main dwelling; location of other assets; where his/her family resides; and time spent in the country etc.

Where an individual permanently relocates to Australia, they will be treated as an Australian resident for tax purposes. In general, the non-Australian assets held by these individuals will be allocated a deemed market value at the date they become a permanent resident and all other income will be taxed under the general rules. Such employees should be treated as per other Australian employees.

Where an individual is both a resident of Australia and of their original country, the relevant DTA will determine taxing rights.

Temporary Residents

In light of the current globally mobile workforce and the desire of Australian businesses attract skilled workers into Australia, a new residency category – temporary residents – has been introduced.

A “temporary resident” is defined as someone:

- Who is presently the holder of a temporary visa; and
- Who themselves, and whose spouse, is not an Australian resident within the meaning of the Social Security Act 1991 (“SSA”).

A resident under the SSA is a person who resides in Australia and is either an Australian citizen, and Australian Permanent Resident or a Protected Special Category Visa Holder.

There are no time limits on how long an individual can remain a temporary resident.

Taxation for Temporary Residents

Foreign Sourced Income:

- Exempt from Australian tax;
- Includes dividends, interest and rental income; and
- Does not include foreign sourced employment income.

► Capital Gains

- Exempt from Australian tax where asset is not: an interest in Australian Real Property; an interest in an Australian company; or an Australian Unit Trust.
- Exemption does not include gains derived as a result of Australian employment (including Employee Share/Option Schemes).

► Employee Share/Options Schemes

- Generally the receipt of shares and options in relation to Australian employment will be taxed in Australia. However, the timing of Australian taxation will depend on whether the shares/options are qualifying or non-qualifying under the Employee Share Scheme (“ESS”) rules.
- Where temporary resident have been subject to tax upon granting of share/options, any subsequent capital gain will be taxable in Australia where it relates to employment in Australia.
- There are special provisions dealing with situations where the grant of shares or options is only partially attributable to Australian employment.

► Interest Withholding Tax

- No withholding applies to payments made by temporary resident to foreign lender.

Generally, employment income earned by temporary residents will be taxed in Australia and will be subject to Pay As You Go Withholding, Superannuation Guarantee, Payroll Tax etc. Other Australian income such as dividends, interest, rent etc will be taxed in Australia under the general rules.

Tax Effective Remuneration Packaging

There are opportunities for Australian employers to present tax effective remuneration packages that take advantage of the temporary resident and non-resident taxation laws. This will ensure that employment costs to the company are minimised while employees receive the most advantageous compensation. In this regard, salary packaging can be very beneficial.

Salary packaging is an approach to remuneration whereby non-salary benefits are provided in place of cash salary or wages. A portion of the salary is effectively ‘sacrificed’ by the employee for non-salary ‘fringe’ benefits such as additional superannuation, living away from home allowances or car benefits etc.

It is vital that the non-cash benefits are correctly calculated, documented and implemented in order to minimise Fringe Benefits Tax (“FBT”) and income tax implications. Where this is the case, the result can be increased cash in hand for the employee while maintaining the total cost to the employer.

The most beneficially packaged items are those that are exempt or concessional taxed for FBT purposes.

Living Away from Home Allowances (“LAFHA’s”)

Where employees are temporary or non-residents and have the intention of returning to their original home after the employment term is completed, they will be living away from home and accordingly, may be eligible for a LAFHA. A LAFHA is paid to reimburse employees for additional costs incurred as a result of having to live away from their usual place of residence and includes two components – additional food and additional accommodation costs.

LAFHA’s are particularly favourable as a remuneration method in that when calculated correctly, they are generally exempt from both FBT and income tax.

In order that any LAFHA paid be exempt from FBT to the employer, it is imperative that the employee intends to return to his/her original place of residence and also that it can be clearly demonstrated that the employee was required to temporarily change residences specifically as a result of the employment engagement in question.

Certain relocation costs incurred by temporary residents can also be packaged without incurring FBT as can school fees for children of temporary residents.

Relocating Employees

Where expatriate employees are permanently relocating to Australia for employment purposes, they will not be eligible for a LAFHA but can package a wider range of relocation costs.

Exempt relocation costs can include: the engagement of a relocation consultant; removal and storage of household effects; costs associated with the sale or purchase of a dwelling; utility connection costs; and relocation transport.

FBT Exempt Benefits

Other benefits that can be exempt from FBT and therefore provide maximum advantage when packaged include: laptop computers and mobile phones used primarily for work-related purposes; on-site recreational and childcare facilities; trade/professional journals and subscriptions; airport lounge memberships, credit card schemes and certain taxi travel.

Other Considerations

When employing non-residents or temporary residents, employers need to be mindful of a number of other considerations:

- Medicare Levy: Exemption certificates can be applied for where employees are not eligible for Medicare benefits in Australia. Where an exemption certificate is issued, the individual will be exempt from the Medicare levy and the Medicare Levy surcharge. If the employee is not eligible for the exemption, they will need to obtain appropriate Australian or International private hospital insurance in order to avoid the surcharge.
- Superannuation – in general, superannuation guarantee at 9% of base wages is payable by Australian employees regardless of the residency status of the employee and this should be factored in when presenting packaged remuneration. There are exceptions where the employee’s overseas employer is required to pay superannuation to a foreign fund for the term of the Australian employment. We also note that certain employees, such as some senior foreign executives may be exempt from superannuation guarantee in certain circumstances.
- Other tax requirements such as payroll tax and FBT implications.
- Sponsorship – some visas have strict employment and remuneration conditions that must be complied with.

Cooper Partners provide taxation related services to employers. For more information on any aspect of your human capital taxation related requirements please contact Michelle Saunders on (08) 6311 6911 or Marissa Behta on (08) 6311 6933.

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