

It's back: Removal of the main residence CGT exemption for foreign residents

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In brief

On 23 October 2019, the Federal Government introduced the [*Treasury Laws Amendment \(Reducing Pressure on Housing Affordability Measures\) Bill 2019*](#), which proposes amendments to deny the Capital Gains Tax (CGT) main residence exemption for foreign residents with effect from 7:30pm (AEST) on 9 May 2017.

This measure is substantially the same as that which was previously announced as part of the 2017-18 Federal Budget and the previous Bill that lapsed with the Federal election in May 2019. However, there are some changes including an extension of the transitional period for dwellings owned before 9 May 2017 which can be sold on or before 30 June 2020 and continue to be eligible for the CGT exemption.

Additionally, foreign residents can now continue to access the main residence exemption where the individual is a foreign resident for six continuous years or less and where certain “life events” occur during the period of foreign residency. These life events include a terminal medical condition, death of the spouse or minor child, or divorce or separation.

Who is impacted by these changes? For the most part, the changes impact Australians going overseas who sell their main residence at the time they are a foreign resident:

- where a “life event” does not occur;
- after six continuous years, even where a life event occurs; or
- do not qualify for the transitional relief (because they acquired their main residence after 9 May 2017 or sold it after 30 June 2020).

Under the proposals, a “foreign resident” means someone who is not a tax resident of Australia and includes Australian citizens and permanent residents who are foreign residents. Individuals who are Australian tax residents at the time of sale of a main residence will not be affected by this measure.

All expatriates who own residential property should consider how these changes will impact their circumstances.

In detail

Current CGT main residence exemption

A taxpayer's main residence is exempt from CGT where a gain (or loss) is made on the disposal of the dwelling that is an individual's main residence throughout their ownership period.

There is also a partial exemption if the dwelling was the individual's main residence for only a part of their ownership period or if it was also used to produce assessable income (e.g. rental income) during their ownership period.

Furthermore, under the "absence rule", an individual who does not treat any other dwelling as their main residence can treat a dwelling as their main residence for CGT purposes for up to six years even if it is rented out, or for an unlimited period where it is not rented out.

Finally, the main residence exemption may also apply to individuals who are beneficiaries of an estate of a deceased person who used the dwelling as their main residence.

CGT main residence exemption to be removed for foreign residents

The [Treasury Laws Amendment \(Reducing Pressure on Housing Affordability Measures\) Bill 2019](#) proposes amendments to remove access to the CGT main residence exemption for "foreign residents" in relation to CGT events happening from 7:30pm (AEST) on 9 May 2017.

A foreign resident is an individual who is not a resident of Australia for taxation purposes.

As a result, an individual who sells their Australian main residence and who is a foreign resident at the time of disposal (referred to as a "CGT event") will no longer be entitled to the main residence exemption, subject to two limited exceptions:

1. where the individual is a foreign resident for six continuous years or less and for certain disposals as a result of a "life event", or
2. the disposal qualifies under the transitional period.

Importance of Australian tax residency status at the time of disposal

For individuals having an ownership interest in a dwelling, for CGT purposes, the date of disposal of their interest in the dwelling will be the time a contract for sale is entered into. This is the relevant time to determine whether the individual is an Australian resident or a foreign resident subject to the new law.

If, at the disposal time, the individual is a foreign resident, the main residence exemption will not apply and the capital gain or loss on the disposal will not be exempt for Australian tax purposes.

There is no ability to apportion the main residence exemption, having regard to the number of days of ownership as an Australian resident or as a foreign resident.

Interaction with the "absence rule"

The amending law makes no consideration of the Australian "absence rule" which can allow an individual to continue to treat a dwelling as their main residence (subject to meeting the conditions noted earlier) for CGT purposes.

Accordingly, if an individual is a foreign resident at the time they sell their residence and one of the two exceptions does not apply, they would be subject to CGT on the full amount of any capital gain.

Examples

The Explanatory Memorandum (EM) accompanying the Bill provides the following example:

Vicki acquired a dwelling on 10 September 2010 moving into it and establishing it as her main residence. On 1 July 2018 Vicki vacated the dwelling and moved to New York. On 15 October 2020 Vicki signs a contract to sell the dwelling. As Vicki is a foreign resident on 15 October 2020, she is not entitled to the main residence exemption.

The EM further confirms that this outcome is not affected by Vicki previously using the dwelling as her main residence and the absence rule that could otherwise have applied to treat the dwelling as Vicki's main residence from 1 July 2018 to 15 October 2020.

This means that foreign residents will no longer benefit from the "absence rule" rule if the property is sold when they are a foreign resident.

However, where an individual returns to Australia and resumes Australian tax residency before entering into a contract of sale, they may still be able to claim the main residence exemption and also benefit from the "absence rule". The example below from the EM demonstrates this outcome.

Amita acquired a dwelling in Australia on 20 February 2003. On 15 August 2021 Amita signs a contract to sell the dwelling. Amita used the dwelling as follows:

- residing in the dwelling from when she acquired it until 1 October 2007;
- renting it out from 2 October 2007 until 5 March 2011 while she lived in a rented home in Paris as a foreign resident (i.e. the absence rule applies to treat her Australian dwelling as her main residence);
- residing in the dwelling and using it as a main residence from 6 March 2011 until 15 April 2012;
- renting it out from 16 April 2012 until 10 June 2017 while she lived in a rented home in Hong Kong as a foreign resident (i.e. the absence rule applies to treat her Australian dwelling as her main residence); and
- residing in the dwelling from 11 June 2017 until it was sold on 15 August 2021.

As Amita is an Australian resident for taxation purposes at the time the contract for sale is signed on 15 August 2021, she is entitled to the full main residence exemption.

An exception for certain life events

There is an exception available to a foreign resident who may be able to access the CGT main residence exemption if they satisfy the "life events test".

To satisfy the first part of this test, the individual must have been a foreign resident for a period of six years or less.

The second element of the life events test is that one of the following specified circumstances has occurred:

- Terminal medical condition of the individual, their spouse or their minor children;
- Death of the individual's spouse or the individual's minor children; or
- Divorce or separation of spouse (or former spouse).

Accordingly, an individual, who has been a foreign resident for six years or less when disposing of an Australian dwelling, may still be able to access the CGT main residence exemption if one of the above life events occurs.

Transitional provisions

The removal of the main residence exemption for foreign residents applies to CGT events happening from 7:30pm (AEST) on 9 May 2017.

However for properties held as at 7:30pm (AEST) on 9 May 2017, the proposed rules will not apply to a disposal of the property until after 30 June 2020.

This means that affected individuals who owned a dwelling before 9 May 2017 that they use as their main residence - or where the absence rule will apply to treat this dwelling as their main residence - will still be able to benefit from the main residence exemption for a disposal on or prior to 30 June 2020.

Potential impact for individuals seconded to Australia

The proposed changes will also apply to individuals who come to Australia and either have a main residence in their home country or purchase a main residence in Australia.

The takeaway

If the proposed Bill is legislated in its current form, the removal of the main residence exemption for foreign residents will have implications for both employers and individuals.

Employers of expatriates

1. Employees may be more reluctant to accept an assignment outside Australia if they will be negatively impacted by the tax consequences of potentially losing their main residence exemption should they wish to sell their home while on assignment.
2. Employers who have tax equalisation arrangements for their expatriate employees and who tax equalise personal income, should consider whether they will tax equalise any CGT imposed on the sale of an employee's Australian home while they are a foreign resident.

Individuals

1. If a main residence was held as at 9 May 2017, current and future foreign residents may consider selling their main residence before 30 June 2020 to obtain the CGT main residence exemption under the transitional rules.
2. Comparative calculations and tax residency analysis may be required before accepting any assignment overseas.
3. Individuals who are currently foreign residents or who will become foreign residents need to be aware of the potential tax implications should they sell their Australian dwelling while they are foreign residents. Any capital gain or loss arising upon such disposal will need to be recognised.

In any case, impacted individuals should seek specific taxation advice in order to evaluate the impact of this measure on their personal tax situation and to take relevant actions where appropriate.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

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