# *Australia and New Zealand approach to dual resident entities*

*06 June 2019*

*Explore more insights* 365

## *In brief*

Australia and New Zealand have given effect to the Organisation for Economic Cooperation and Development (OECD) Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BEPS) (the Multilateral Instrument). The Multilateral Instrument, which has now been in effect from as early as 1 January 2019 for Australia and New Zealand, will impact the operation of the Australia-New Zealand double tax treaty.

On 27 May 2019, the Australian Taxation Office (ATO) and the New Zealand (NZ) Inland Revenue (IR) released their joint administrative approach to interpreting the 'dual resident' provisions in the Multilateral Instrument. This is a significant development because an entity that is a tax resident of both Australia and New Zealand - i.e. a 'dual resident' in the absence of competent authority agreement - is not entitled to any relief or exemption from tax provided by the Australian-New Zealand treaty. The administrative approach will be particularly beneficial in reducing taxpayer compliance costs and potential uncertainty, particularly for smaller groups.

## *In detail*

Under Article 4(1) of the Multilateral Instrument, dual resident entities cannot access treaty benefits unless the competent authorities agree to which jurisdiction the entity is tie-broken. This means that the taxpayer will need to apply to either competent authority for a determination of their residency for the purposes of applying the relevant treaty.

In recognition of the close economic ties and similarities between the respective tax systems and administrations of Australia and New Zealand, the ATO and NZ IR have developed a joint administrative approach to applying the 'dual resident' provisions in the Australia-New Zealand treaty as modified by Article 4(1) of the Multilateral Instrument.

Under this administrative approach, an ordinary company that is a resident of both Australia and New Zealand, and that meets strict eligibility criteria, can reasonably self-assess 'its place of effective management' and therefore access treaty benefits without needing to apply for competent authority approval. This should promote taxpayer certainty and reduce tax compliance costs for those taxpayers who are eligible.

For example, under the administrative approach, where an eligible taxpayer reasonably self-determines its place of effective management to be located in New Zealand, it is deemed to be a resident of New Zealand for the purposes of the Australia-New Zealand treaty and the taxpayer will also be a prescribed dual resident under the definition in subsection 6(1) of the Income Tax Assessment Act 1936.

One of the **key gateway criteria** to access this concession is that the taxpayer's group annual accounting income must be **less than AUD 250 million (or NZD 260 million)** based on prepared financial statements for the most recent reporting period. This unfortunately narrows the application of the concession to small and medium size business groups.

Furthermore, the following conditions must also be met:

- the taxpayer's gross 'passive income' must be less than 20 per cent of its total assessable income for the most recent income tax year

- the total value of intangible assets (other than goodwill) held by the taxpayer must be less than 20 per cent of the value of its total assets based on prepared financial statements for the most recent reporting period

- the taxpayer or any member of the group must not currently, or in the last five years, be subject to any compliance activity (including any risk review, audit or any other compliance activity) undertaken by either the ATO or IR which relates to the determination of residency for taxation purposes, and

- the taxpayer or any member of the group must not currently be engaged in any objection, challenge, settlement procedure or litigation in either Australia or New Zealand in relation to a dispute with either the ATO or IR - this is very broad and the matter under dispute need not be in relation to matters concerning residency.

There are also additional criteria which must be satisfied on an ongoing basis in order for the concession to continue to apply, including an obligation to notify any new compliance activity undertaken by either of the competent authorities and a requirement that the taxpayer or any member of the taxpayer group not enter into, or carry out any tax avoidance scheme relating to residency.

As noted earlier, the criteria for accessing the concession is quite strict. For example, if a group has consolidated income above AUD 250 million it will not be able to benefit from this administrative approach. Instead such an entity will be required to apply to the competent authority for approval to access the benefits of the Australia-New Zealand treaty.

Once an eligible taxpayer has self-assessed its place of effective management, this is not the end of it. Affected taxpayers are strongly encouraged to document their assessment and are also required to re-assess eligibility where there is a material change to their circumstances. The ATO and IR will not generally seek to review the conclusion as long as all material facts and circumstances remain the same. However, they reserve the right to review the outcome particularly where the ATO or IR is of the opinion that any anti-avoidance rules may apply.

## *The takeaway*

It remains important for all taxpayers with cross border dealings to continue to monitor the impact of the Multilateral Instrument, if any, on any specific tax treaty before seeking to access any treaty relief. In addition, taxpayers should note that the administrative approach taken between Australia and New Zealand in relation to dual residency cannot be applied to any other jurisdiction, and it appears that there is no plan for similar relief to be afforded in relation to any other treaties.

Since the criteria for accessing the administrative concession is quite strict, affected dual resident entities that are seeking to access the Australia-New Zealand approach should carefully document their self-assessment of the place of effective management. In order to access the administrative approach, taxpayers are still required to meet the general record-keeping requirements under domestic law.

It is also important to note that even though the residency of a taxpayer might be able to be tie-broken for tax treaty purposes, this will not resolve the broader issues associated with having foreign incorporation, central management and control in Australia, and therefore being an Australian resident for domestic tax purposes.

## *Let's talk*

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


Jonathan Malone, Sydney
+61 (2) 8266 4770
jonathan.r.malone@pwc.com

Tamika Cullen, Sydney
+61 (2) 8266 0397
tamika.cullen@pwc.com

Peter Collins, Melbourne
+61 (3) 8603 6247
peter.collins@pwc.com

Rebecca Cohen, Sydney
+61 (2) 8266 8476
rebecca.cohen@pwc.com

Jonathan Fraser, Melbourne
+61 (3) 8603 2447
jonathan.fraser@pwc.com