

Tax residence and implications



Tax residency can cost your clients money and time if documents are not filed correctly, warns JEFF OWENS.

In an increasingly global business and employment environment, New Zealanders often move to other countries, sometimes never to return, and sometimes returning to NZ after a few years.

The country where income is sourced typically has the first right to tax that income – employment, interest and dividends, rental income. The country where they are tax resident then typically has the ability to tax the person's worldwide income, generally with a credit for tax paid at source. Sometimes, but not always, there is an exclusion for employment income taxed at source.

The person's tax residence therefore has a crucial

impact on the total tax they pay and to which tax authority.

If a NZ resident is working outside NZ then they will generally want to cease their NZ tax residence to:

- avoid the administrative cost of filing NZ tax returns
- avoid the cost of a potential top up to NZ tax rates – which can be very expensive where their income is taxed at a low rate in the country of source.

The NZ IR of course has an interest in capturing such taxpayers to make them pay a top up of income tax.

DETERMINING TAX RESIDENCE

Like most OECD countries there are two tests of NZ tax residence – personal presence, and permanent place of abode.

Under the personal presence test an individual will prima facie retain their NZ residence until such time as they have been physically absent for at least 325 days in any 12-month period.

Also under that test an individual will trigger NZ tax residence from the first day of any 12-month period in which they are personally present in NZ for 183 days in total.

In applying these tests:

- the 12-month period does not have to be a calendar year
- a part day of presence eg day of departure and day of arrival are both treated as personally present in NZ
- once they satisfy such a test the residence (or non residence) is backdated until the first date in such 12-month period.

These tests are simply a matter of determining facts, although being forewarned a taxpayer may be able to adjust their travel plans to get a favourable result.

The personal presence test is over ridden by having a permanent place of abode in NZ.

Permanent place of abode is not a defined test, but rather comes out of developing case law and commentary. It encompasses such factors as availability of long-term accommodation (not necessarily owned), employment, family, sports clubs, church etc.

Thus a person who appears to have ceased residence by virtue of physical absence from NZ may still be NZ resident because they have a permanent place of abode.

DOUBLE TAX TREATIES

Where a person is deemed tax resident in two countries, an applicable tax treaty will determine them (for purposes of the Treaty, for example imposition of income tax) to be tax resident in just one of those countries. Such tests can be complex to administer, and

further, there are many countries (especially low tax jurisdictions) with which we don't have a tax treaty.

IR886

Taxpayers can express their intentions by completing an IR886 New Zealand tax residence questionnaire. IR will use this as an indication as to whether or not the taxpayer has ceased (or regained) NZ tax residence.

Unfortunately some taxpayers complete these themselves and give responses that may be factually incorrect and incorrectly indicate they retain NZ tax residence.

IR RESPONSE

In the past three months we have had three taxpayers referred to us where upon departing (or returning) to NZ they had incorrectly completed IR886 forms, and IR has determined that they had retained NZ tax residence. In each case they were deriving income in a low tax jurisdiction and IR was seeking to collect NZ tax on that income. In the most recent example IR wanted to collect tax on eight years of foreign sourced income.

IR issued its conclusion by way of a "disputable decision" and told the taxpayer that if they disagreed they had to complete a Notice of Proposed Adjustment.

This is quite inappropriate – if the IR disagrees with a taxpayer's position then its own public standards require IR to prepare such a document, not impose the cost on the taxpayer. We have taken this matter up with senior IR personnel.

In each case fortunately we were able to get IR's position overridden and protect the taxpayer's position.

CONCLUSIONS

Never let your client file a document with IR without having it carefully checked by an expert.

Ensure you understand tax residence issues – or refer to an external expert.

If IR disagrees with a taxpayer's position but tries to force you into lodging a NOPA, object in strong terms and advise NZICA. ■

Jeff Owens CA is the Director of Owens Tax Advisors Ltd, a specialist tax advisory firm.

If the IR disagrees with a taxpayer's position then its own public standards require IR to prepare such a document, not impose the cost on the taxpayer