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Australia:
Legislation introduced to exclude foreign residents from CGT exemption for the sale of a main residence

Overview

Further to our Newsflash issued on August 3, 2017 in relation to the 2017-18 Australian Federal Budget (the "Budget") announcements, below is a summary of recent developments related to the removal of the Capital Gains Tax (CGT) exemption for the sale of a main residence by foreign residents.

Background

In the Budget, the Australian Government announced its intention to restrict the CGT exemption for sale of a main residence, so it would not apply to foreign residents or temporary residents (mainly, foreign nationals in Australia holding temporary visas).

Exposure Draft (ED) legislation to implement this change was released for public consultation on July 21, 2017. It only removed the CGT exemption for foreign tax residents (so temporary residents who reside in Australia may continue to qualify for the CGT exemption).

On February 8, 2018, the Treasury Laws Amendment (Reducing Pressure on Housing Affordability Measures No. 2) Bill 2018 (the "Bill") was introduced into Parliament, which contained the measures to enact the proposed amendments (substantially in line with the ED legislation released last year).

Impact of measures in Bill

When enacted, the measures in the Bill will remove the CGT exemption for the sale of a main residence if the owner is a foreign resident when the sales contract is entered into. The changes will apply to:

- All sales occurring after June 30, 2019
- Any sales before this date if the residence was purchased after 7:30pm AEDT on May 9, 2017

The legislation proposes to amend section 118 – 110 of the Income Tax Assessment Act 1997 (ITAA 1997), with effect for CGT events occurring after 7:30pm AEDT on May 9, 2017. Although most CGT events will be straightforward disposals of property, the amendments will apply to all CGT events affecting dwellings, including compulsory acquisitions and deceased estates.

The legislative amendments will entirely remove the entitlement of foreign residents to full or partial CGT exemptions related to CGT events occurring to dwellings that would otherwise qualify as their main residence. The other requirements for the CGT exemption (including the temporary absence concession, whereby a home can be rented out for up to six years without losing the CGT exemption) are unchanged.

Notably, despite consultation, this proposal continues to be an all-or-nothing exclusion. Unlike many other CGT exemptions, the Bill allows no scope to apportion the CGT main residence exemption between periods of residence and non-residence during the ownership period.

For example, the Explanatory Memorandum to the Bill makes it clear that previously occupying the dwelling as a main residence during any period of Australian residence would not affect the outcome.

Conversely, if an individual becomes a foreign resident, but reestablishes Australian residency for taxation purposes before the relevant CGT event occurs, the full CGT exemption for the sale of a main residence would apply (subject to existing rules for a full or partial exemption).

The amendments in the Bill also ensure the removal of the exemption extends to situations in which dwellings are acquired from deceased estates of foreign residents, and the rules affecting special disability trusts.

Transitional provisions are included to grandfather the exemption for dwellings acquired before 7:30pm AEDT on May 9, 2017, and sold on or before June 30, 2019.

Notably, to obtain the exemption under the transitional rules, the CGT event must occur on or before June 30, 2019, so it is critical to enter into a contract for the sale of a main residence on or before June 30, 2019 (not settlement).

After June 30, 2019, all capital gains or losses arising upon disposal of a foreign resident's main residence will need to be recognized for tax purposes, and the CGT exemption for the sale of a main residence will not apply.

Deloitte's view

The proposed removal of the CGT exemption for the sale of a main residence by foreign residents for Australian tax purposes is likely to have a significant impact on individuals who relocate overseas for work purposes.

The change, once enacted, will in particular come as a shock to those Australian citizens and permanent residents who already work overseas and want to take advantage of rising property values to sell their main residence while residing outside of Australia as foreign tax residents.

Under the rules now before Parliament, individuals who owned a main residence in Australia at 7:30 AEDT on May 9, 2017, and who fall into this category, will only have until June 30, 2019, to sell their homes and apply the CGT exemption for the sale of a main residence.

Aside from this transitional rule, once enacted, the CGT exemption for the sale of a main residence will be completely lost if the individual is a foreign resident on the date of sale of the property. This means that Australian citizens and permanent residents who currently reside overseas will not be able to access any part of the CGT exemption if their property is sold while they are living abroad as foreign residents (for existing properties, sales after June 30, 2019).

However, if they were to return to Australia, recommence Australian tax residency, and then sell their property, all or part of the CGT exemption would be available to the extent that the other conditions for the exemption are met.

It is disappointing that the consultation process did not result in additional modifications to the ED legislation, such as allowing a partial exemption for former Australian citizens and permanent residents with respect to periods in which they actually resided in their main residence.

These new rules will need to be considered carefully by foreign resident owners of Australian residential property.

The CGT liabilities at stake in these circumstances could be material given the significant increases in housing prices in Australia over recent years, especially in Sydney and Melbourne.

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Czech Republic:
Proposed changes to the taxation of individuals

Overview

The Ministry of Finance of the Czech Republic has published for consideration an amendment to Act No. 586/1992 Coll., Income Taxes Act, which could come into force as of January 1, 2019.

The main change introduced by the draft amendment relates to the cancellation of the “super-gross” tax base for employees. Additionally, the amendment also transposes the Anti-Tax Avoidance Directive of the European Union (EU) into Czech law.

New rules for taxation of employment income

If the amendment is approved, the tax base for employees will be gross remuneration (incl. taxable benefits). Neither the employee’s nor the employer’s social security or health insurance contributions will be taken into account any longer.

Deloitte's view

The "super-gross" tax base for employees caused several issues in the case of individuals with cross-border activities. Its cancellation is a part of the Government's Program; however, we do not see a major impact to the simplification of the Czech tax system, which they state as their goal.

New tax rates

In order to maintain a similar level of taxation, the amendment changes the personal income tax rate to 19% and introduces another tax bracket for income over CZK 1,500,000 per year with a rate of 24%.

At the same time, the solidarity surcharge, which is currently applied to income from employment and self-employment activities exceeding 48 times the national average wage, would be cancelled.

Several types of non-employment income are being transferred to a separate tax base, subject to the withholding tax of 15%. This includes dividends and interest income among others.

Deloitte's view

The effective tax rate for employees with income under CZK 1,500,000 p.a. will be lower by 1.1%; employees with higher income will pay approximately the same tax.

Cancellation of the solidarity surcharge will simplify the calculation of tax; however, its replacement by a second tax bracket will increase the tax burden for individuals with types of income other than employment and self-employment income.

Income from self-employment

Self-employed individuals will also be subject to the 19% (or 24%) tax rates. However, their tax burden should not change due to the possibility to deduct ¾ of their social security and health insurance contributions from the tax base as additional expenses. This would apply also to individuals using the lump-sum expenses to calculate their taxable income.

Deloitte's view

The draft amendment does not explain sufficiently whether only final contributions or also pre-payments for the contributions might be deducted. Potentially, self-employed individuals may easily influence their tax base by increasing or decreasing the pre-payments.

Other types of income

For individuals with rental and other types of income, the increase in the tax rates will result in a significantly higher taxation. This income is not subject to any social security or health insurance contributions and thus, only standard expenses will be deductible.

Deloitte's view

For example, this increase may result in significantly higher tax burden for individuals with large income from the sale of shares.

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