AUSTCHAM
HONG KONG
A MEMBER OF AUSTCHAM GREATER CHINA

Tax Treaties Branch
Corporate and International Tax Division
Treasury
Email: TaxTreatiesBranch@treasury.gov.au

15 April 2024

Dear Sir or Madam,

Submission on Australia's Tax Treaty Network Expansion

The Australian Chamber of Commerce in Hong Kong (AustCham) represents more than 800 members from 245+ companies. We are one of the largest international chambers in Hong Kong and one of the largest Australian chambers abroad. AustCham's membership includes Australian businesses operating offshore, Hong Kong companies with significant investments in Australia, international companies with operations in Australia and Hong Kong, and individuals leading Small and Medium Sized businesses and working for global business in Hong Kong. AustCham has been in Hong Kong since 1987 supporting our members, their business and the Australia-Hong Kong bi-lateral relationship.

The Treasury's consultation seeking views on issues related to Australia's tax treaty network provides an opportunity to once again share AustCham's support for expanding Australia's tax treaty network by considering a comprehensive Double Tax Agreement (DTA) between Australia and Hong Kong.

Hong Kong is home to over 100,000 Australian nationals, with the largest number of Australian businesses based outside Australia and our second largest expatriate community globally. As of 2023, there were 27 regional headquarters, 52 regional offices and 80 local offices in Hong Kong with parent companies located in Australia – the 10th largest international representation of international regional headquarters in Hong Kong.

Hong Kong is a global financial centre and Asia's leading finance hub. It is a major logistics and transportation hub and remains the gateway to and from China and the wider North Asia region (including Japan, Korea and Taiwan) for investment and capital flows. North Asia accounts for the largest proportion of Asian trade with the rest of the world. Hong Kong is a key trade partner to Australia and is the country's 11th largest source of direct foreign investment. A DTA with Hong Kong will allow alignment and consistency with how Australia treats its major trading and investment partners.

Hong Kong has 48 DTAs in place with jurisdictions that include Australian tax treaty partners such as the United Kingdom, Singapore, New Zealand, Japan, Indonesia and Malaysia. As an example, Hong Kong and New Zealand signed a tax treaty in December 2010, which entered into force in November 2011. Hong Kong is also currently in DTA negotiations with 17 other jurisdictions, including Germany, Israel and Norway. We understand the Hong Kong government is very receptive to entering into DTA negotiations with Australia.

A DTA between Australia and Hong Kong is critical for Australian business and important in strengthening the relationship between Australia and Hong Kong. Such an agreement fosters increased cross-border trade and investment between the two jurisdictions and secure economic growth into the future, whilst demonstrating a shared commitment to addressing international tax avoidance practices.

In 2017 AustCham provided a detailed submission (enclosed) on the benefits of an Australia-Hong Kong Double Taxation Agreement. The issues discussed in this submission remain significant and relevant today. There are real and tangible advantages to Australia in terms of greater information and transparency in entering into a DTA with Hong Kong, including:

- providing complementarity and support to the Australia-Hong Kong Free Trade Agreement
- strengthening investment into Australia, particularly given large infrastructure projects requiring capital such as green energy and decarbonisation projects
- providing greater access to information in Hong Kong for the ATO
- protecting Australian tax residents temporarily based in Hong Kong, from Australian tax on their foreign source income (assuming they are allocated to Hong Kong under the tie-breaker provisions)
- Increasing the attractiveness of Australia for leading global talent, especially international executives, identified as a solution to addressing Australia's skills deficit and accelerating economic growth.

These last two points are particularly critical given the proposed reform of Australia's individual tax residency tests and proposed adoption of the Board of Taxation's recommendations in its 2019 report[1]. AustCham has actively engaged with Treasury on the proposed recommendations, and I enclose a copy of our submission to the Australian Government Consultation on Modernising the Individual Tax Residency Rules (dated 22 September 2023).

Recent developments with the implementation of the OECD/G20 Base Erosion and Profit Shifting (BEPS) Inclusive Framework also underscore the need for greater certainty a DTA can provide for Australian businesses in Hong Kong.

If you have any queries about this submission, contact myself on austcham@austcham.com.hk or by phone +852 6398 6105.

Yours sincerely,

S. Evennett

Stefanie Evennett
Chief Executive

Encl.: March 2017, AustCham Hong Kong Submission, Australia - Hong Kong Comprehensive Double Taxation Agreement: Securing economic growth into the future (Confidential)
September 2023, AustCham Hong Kong Submission to Australian Government Consultation on Modernising the Individual Tax Residency Rules

CC Gareth Williams, Australian Consul-General in Hong Kong

[1] The previous Federal Government in the 2021/2022 Federal Budget proposed to consider the recommendations of the Board of Taxation in reforming Australia's tax residency rules as contained in its report released in 2019 'Reforming Individual Tax Residency Rules – a model for modernisation'.

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AUSTCHAM HONG KONG & MACAU
A MEMBER OF AUSTCHAM GREATER CHINA

Connecting Australian Businesses for 30 years in Hong Kong & Macau

Australia - Hong Kong Comprehensive Double Taxation Agreement

Securing economic growth into the future

AustCham Hong Kong

March 2017

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1 Executive summary

Political uncertainties in many parts of the world are impacting the global economic outlook. At the same time, Governments around the world are also faced with the challenge of globalisation, which is exacerbating opportunities for tax avoidance.

The idea of a double taxation agreement ("DTA") between Australia and Hong Kong is not new, and now is the time for action. This is the time for Australia and Hong Kong to enter into a DTA to foster increased cross-border trade and investment in the region and secure economic growth into the future, whilst demonstrating Australia's and Hong Kong's commitment to addressing international tax avoidance practices.

Hong Kong is one of Australia's top 15 partners in terms of trade in goods and services[1]. Hong Kong is also the 6th highest source of investment in Australia; this is followed by China at the 7th position, which also makes a large proportion of its outbound investments through Hong Kong[2]. Although Australia has an established network of DTAs with its main trading and investment partners such as China (the DTA does not extend to cover Hong Kong) and Singapore (which has a similar tax system to Hong Kong), Hong Kong is a notable absence from Australia's DTA network.

A DTA between Australia and Hong Kong would provide benefits to both signatories. Hong Kong has a longstanding economic policy of free enterprise and free trade, and is strategically located in the heart of Asia and a key financial center in the region.

Geographically and commercially, Hong Kong is an attractive entry point for other countries looking to do business in the region; in particular, Hong Kong is proven gateway to China's high growth markets (which we understand is increasingly important for Australia).

A DTA between Australia and Hong Kong would foster increased cross-border trade and investment between the two jurisdictions as well as enhanced access to other parts of Asia for Australian businesses. Specifically, with regard to Australia's aspirations to deliver new sources of growth through innovation[3], a DTA between Australia and Hong Kong would support Australian businesses that are seeking to commercialise good ideas with realising the potential of Asian markets, and in turn, Australia's shift from the mining boom to the "ideas booms". The DTA would provide greater certainty and simplicity for businesses operating in the region with respect to the taxation of cross-border investment and transfer of human capital (which is particularly relevant for businesses built on innovation).

In line with international efforts, the DTA can also be used by Australia and Hong Kong to jointly respond to the challenge of effective tax administration in today's global environment through anti-treaty abuse safeguards, mutual assistance in tax collection, exchange of tax information and improved dispute resolution, which are common features in modern DTAs.

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[1] Australian Government Department of Foreign Affairs and Trade ("DFAT"), *Australia's trade in goods and services by top 15 partners*, 2015-16, http://dfat.gov.au/about-us/publications/trade-investment/australias-trade-in-goods-and-services/Pages/australias-trade-in-goods-and-services-2015-16.aspx#partners

[2] Australian Government DFAT, *Which countries invest in Australia?,* 2015, http://dfat.gov.au/trade/topics/investment/Pages/which-countries-invest-in-australia.aspx

[3] Australian Government, *National Innovation and Science Agenda: Welcome to the Ideas Boom*, 7 December 2015, http://www.innovation.gov.au/page/national-innovation-and-science-agenda-report

We understand that there have been a number of discussions between the Hong Kong Financial Services and Treasury Bureau, and the Australian Treasury in the past to discuss a DTA. The Australian Treasury is, as we understand it, receptive to the idea of a DTA, subject to an evaluation of the implications of concluding a DTA with Hong Kong.

Specifically, we understand that Australia's primary concern has related to a potential loss of revenue as result of entering into a DTA. We note that there should be little impact, if any, on revenue collection for dividend and interest withholding tax; the only potential impact is in respect of royalty withholding tax if the DTA were to provide for reduced royalty withholding tax on royalties paid from Australia to Hong Kong. Given that Hong Kong has re-affirmed its commitment to expanding its DTA networks[4], and has demonstrated willingness to be flexible in treaty negotiations in the past, a DTA between Australia and Hong Kong could presumably involve a carve-out in respect of the royalty article, if this is considered necessary.

In any event, it is unlikely that the Australian Taxation Office ("ATO") would collect any meaningful amounts of royalty withholding tax on payments to Hong Kong. For Australian businesses selling technology intensive goods and services into Asian markets, it is more likely that there would be royalties paid to Australia for the use of intellectual property developed and located in Australia.

Tax as a "growth friendly" strategy and strengthening cooperation to close the gaps in international tax rules have never been higher on the agenda for world leaders. By entering into a DTA with Hong Kong, Australia would be sending the message that it is looking ahead and committed to supporting the Australian economy's shift to broader-based growth by making the most of opportunities offered in Hong Kong and other parts of the region. This is the time for Australia and Hong Kong to partner up to secure economic growth into the future.

[4] Hong Kong Financial Secretary's 2017/18 Budget Speech, released on 22 February 2017

2 Background

2.1 The challenge of economic growth

The World Bank is projecting a growth of 2.7 percent in 2017 for the global economy after a post-crisis low last year[5]. The shifting political landscape in many parts of the world – for example, the United Kingdom's ("UK") decision to leave the European Union ("Brexit"), the United States ("US") Presidential Election in 2016 and political uncertainty ahead of crucial elections in the eurozone[6] – is impacting the global economic outlook. A need for action to manage the associated uncertainties is high on the agenda for world leaders.

In Australia, the economy continues to transition from the investment phase to the production phase of the mining boom and the challenge is achieving broader-based growth.[7] As the International Monetary Fund ("IMF") noted in its annual assessment of the Australian economy, although economic growth in Australia has been relatively robust despite the unwinding of the mining boom, "Australia has not been immune to the new mediocre"[8]. We understand that the Australian Federal Government is focused on securing Australia's economic growth in light of the significant risks and uncertainties ahead such as weaker than expected domestic consumption and rise of protectionist measures in G20 economies [9]. Indeed, the IMF has endorsed the Australian Government's reform agenda given the focus on strengthening competition and fostering innovation, and Australia's commitment to "an open economy in trade, foreign investment and immigration"[10].

2.2 The BEPS challenge

At the same time, there have been significant changes in the international tax landscape in recent years to address the risk of tax base erosion and profit shifting by multinationals. In the aftermath of the global financial crisis, the G20 and OECD have partnered to establish a modern international tax framework that is focused on:

— Ensuring that profits are taxed where the value is created; and

— Tax transparency as a means of enabling improved accountability and cooperation between taxpayers and tax administrations.

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[5] World Bank Group Flagship Report, *Global Economic Prospects: Weak Investment in Uncertain Times*, January 2017, https://openknowledge.worldbank.org/bitstream/handle/10986/25823/9781464810169.pdf
[6] The Netherland's General Election was held on 15 March 2017 and is the first in series of elections across Europe this year, which includes France's Presidential Election (first round on 23 April 2017, second round on 7 May 2017) and Germany's Federal Election on 22 October 2017
[7] The Australian Federal Government's Mid-Year Economic and Fiscal Outlook 2016-17, December 2016, http://www.budget.gov.au/2016-17/content/myefo/html/
[8] International Monetary Fund ("IMF"), *IMF Executive Board Concludes 2016 Article IV Consultation with Australia*, 9 February 2017, https://www.imf.org/en/News/Articles/2017/02/09/PR1741-Australia-IMF-Executive-Board-Concludes-2016-Article-IV-Consultation
[9] OECD/ World Trade Organisation ("WTO")/ United Nations Conference on Trade and Development ("UNCTAD"), Reports on G20 Trade and Investment Measures (Mid May to Mid-October 2016), 10 November 2016, https://www.wto.org/english/news_e/news16_e/g20_joint_summary_november16_e.pdf
[10] Refer Note 7

Since the G20/OECD first embarked on this project (referred to as the Base Erosion and Profit Shifting ("BEPS") Project), more than 60 jurisdictions have been involved in delivering the 15 Action Plans under the BEPS Project (released in November 2015)[11].

There are now more than 90 jurisdictions (including Australia and Hong Kong) who are working together to set standards for the implementation of the BEPS Action Plans in their domestic tax laws[12]. Specifically, these jurisdictions have committed to four minimum standards:

— Countering harmful tax practices more effectively;

— Preventing treaty abuse;

— Imposing country-by-country reporting requirements; and

— Improving the cross-border dispute resolution regime[13].

For instance, as part of its commitment to implement a model that meets international standards, Hong Kong has recently announced the introduction of specific transfer pricing rules that are aimed at ensuring that taxpayers earn an arm's length profit for the activities they are performing, and which include mandatory transfer pricing documentation requirements[14].

In connection with the BEPS Project, Australia and Hong Kong, together with more than other 100 jurisdictions, have also participated in developing the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting ("the Multilateral Instrument") (released on 31 December 2016 with signature by the relevant countries planned for June 2017)[15]. The Multilateral Instrument implements standards for countering treaty abuse, improve dispute resolution mechanisms and strengthen the tax treaty related measures developed under the BEPS Project.

2.3 Hong Kong's commitment to expanding its DTA network

Hong Kong is the leading financial services centre in Asia, as well as the preferred regional or head office jurisdiction for many multinational and Asian corporations. Hong Kong is looking to further capitalise on its status as a head office and financial services centre, and to promote cross-border trade and investment between China and the rest of the world. Hong Kong's proximity to China and other parts of Asia, and its international business environment, makes it a preferred jurisdiction for investors to establish business operations and to hold their investments in Asia. In support of this, Hong Kong has been actively seeking to expand its DTA network. DTAs have already been signed with China, the UK, France, Switzerland, Malaysia and Indonesia (37 jurisdictions in total

[11] OECD/G20 Base Erosion and Profit Shifting Project, 2015 Final Reports, http://www.oecd.org/ctp/beps-2015-final-reports.htm
[12] OECD Inclusive Framework on BEPS Composition as at 5 January 2017, https://www.oecd.org/tax/beps/inclusive-framework-on-beps-composition.pdf
[13] OECD, *BEPS: About BEPS and the inclusive framework*, http://www.oecd.org/tax/beps/beps-about.htm
[14] On 26 October 2016, the Hong Kong Government issued a consultation paper on a range of measures including a proposal to introduce specific transfer pricing rules for Hong Kong. Draft legislation is expected to be introduced by mid-2017
[15] OECD's Information Brochure on the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting, http://www.oecd.org/tax/treaties/multilateral-instrument-BEPS-tax-treaty-information-brochure.pdf

as of 28 February 2017).[16] Hong Kong has also signed a DTA with New Zealand and Canada, and is currently negotiating a DTA with Germany, jurisdictions with similar taxation regimes to that of Australia.

More recently, Hong Kong has signed DTAs with Russia (18 January 2016), Latvia (13 April 2016) and Belarus (16 January 2017) and Pakistan (17 February 2017), major developing economies along the "One Belt One Road". Hong Kong is continuing its efforts to expand its network of DTAs with other trading and investment partners. In addition to current negotiations with Australia, Hong Kong is also in negotiations with a further 14 jurisdictions (including India and Germany).

[16] Refer Appendix A: Hong Kong's DTA network

3 Treaty benefits

Australia is currently a party to 44 DTAs (as at 28 February 2017), including the revised DTA with Germany that was signed on 12 November 2015.[17] While Australia has treaties with many trading partners (including some neighbouring Asian jurisdictions), most of them are relatively old and the existing DTA between Australia and China does not extend to cover Hong Kong.

There is an opportunity here for Australia and Hong Kong to enter into a DTA to minimise barriers to key drivers of economic growth such as investment, innovation and entrepreneurship. A DTA between Australia and Hong Kong helps ensure that Australia is in a competitive position for trade and investment with Hong Kong as well as other parts of Asia, which would provide benefits to both jurisdictions. The mutual benefit of increased cross-border trade and investment supports innovation, job creation and future economic growth for Australia and Hong Kong.

3.1 Enhance cross-border trade and investment between Australia and Hong Kong

Australia and Hong Kong have a longstanding and significant trading relationship. Hong Kong is Australia's 12th largest two-way trading partner (2015-16)[18], including being Australia's 6th largest destination for merchandise exports (A$8.8 billion) and 7th largest destination for service exports (A$2.3 billion)[19].

Hong Kong is also the 6th largest source of foreign investment for Australia (A$85.4 billion in 2015). This outranks direct investment from China into Australia (A$74.5 billion in 2015)[20], noting that many Chinese enterprises prefer to manage their outbound investments through Hong Kong. Hong Kong's investment in Australia ranges from infrastructure and telecommunications to banking, property development, transport, hospitality and agriculture[21].

Importantly, there is room for growth. Based on Australia's International Business Survey 2016 ("AIBS 2016"), which captures responses from more than 900 Australian businesses undertaking international activities, Hong Kong is expected to be a key new market for the "Information, Communications and Technology" ("ICT") (ranked 7th) and "professional, scientific and technical services" (ranked 8th) sector, in terms of additional revenue expected over the next two years. This suggests that Australian business are seeing opportunities for increased technology intensive goods and service exports to Hong Kong. This is also consistent with a recent report on *"Australia's jobs future: The rise of Asia and the services opportunity"*[22], which noted that service exports from Australia to Asia are underperforming relative to Australia's traditional partners and

[17] Refer Appendix B: Australia's DTA network
[18] Refer Note 1
[19] Australian Government Department of Foreign Affairs and Trade ("DFAT"), Trade and economic factsheet for Hong Kong, December 2016, http://dfat.gov.au/trade/resources/Documents/hong.pdf
[20] Refer Note 2
[21] Hong Kong Financial Secretary, Australian Consulate-General Australia Day Reception Address on 24 January 2017, http://www.news.gov.hk/en/record/html/2017/01/20170124_204510.shtml
[22] ANZ/ PwC/ Asialink Business Services Report, *Australia's jobs future: the rise of Asia and the services opportunity"*, April 2015, https://www.pwc.com.au/asia-practice/assets/anz-pwc-asialink-apr15.pdf

concluded that by employing the right strategies, services can become Australia's number one export to Asia in terms of total value added, creating jobs in the process[23].

At the same time, innovation and technology development is high on the Hong Kong Government's policy agenda, and Hong Kong's Financial Secretary has expressed a desire to partner with Australia in this area[24].

Against this backdrop, a DTA between Australia and Hong Kong would foster bilateral economic activity, and in particular, the commercialisation of technology intensive goods and services in Asia by Australian businesses.

Based on a study conducted by the Australian Government's Productivity Commission, one of the barriers to growth in Australian service exports relates to investment in Australian service providers[25]. Australia has always relied on foreign investment to drive economic growth (and with it, growth in employment)[26]. However, tax laws in Australia are often seen as very complex and can change suddenly. As tax certainty and simplicity are some of the factors to consider in deciding whether to invest in Australia or elsewhere, a DTA between Australia and Hong Kong would support increased investment from Hong Kong into Australia by specifying the maximum rates of withholding taxes that can be applied to dividends, interest and/or royalties. This allows investors to make investment decisions with greater confidence and reduces compliance costs for investors by making it easier to determine potential returns on investments.

Barriers to attracting skilled employees and impediments to the movement of services have also been identified in the Productivity Commission's study as barriers to growth in Australian service exports. These could have a substantial effect on the supply of service exports by increasing the ongoing costs of export operations and/or limiting the supply of exports[27]. The services sector is particularly reliant on the availability of skilled employees and in the case of service exports, entails a greater degree of cross-border movement of employees than the export of goods. A DTA between Australia and Hong Kong would reduce potential impediments in these areas by supporting the movement of employees between these jurisdictions. For employees engaged in certain short-term income-earning activities in Hong Kong, it could reduce compliance costs and provide cash flow advantages by eliminating the need to pay tax in that jurisdiction (i.e. Hong Kong) and then claim that tax against the tax liability in their home jurisdiction (i.e. Australia). It would also support Australian businesses with the exchange of ideas for innovation, developing an "Asia capable" workforce and competing on an international level by leveraging from the experience of those in Hong Kong.

[23] Commissioned by the Export Council of Australia ("ECA") with the support of Austrade and Export Finance and Insurance Corporation ("Efic"), http://www.austrade.gov.au/ArticleDocuments/1358/AIBS-2016-full-report.pdf.aspx
[24] Refer Note 20
[25] Australian Government, *Productivity Commission Research Report on Barriers to Growth in Service Export*, November 2015, http://www.pc.gov.au/inquiries/completed/service-exports/report/service-exports.pdf
[26] Australian Government DFAT, Australia and Foreign Investment, http://dfat.gov.au/trade/topics/investment/Pages/frequently-asked-questions.aspx
[27] Refer Note 24

3.2 Gateway to Asian markets

For Australian businesses looking to do business in Asia, Hong Kong is an attractive entry point. Hong Kong is the top ranking jurisdiction on the Heritage Foundation's Index of Economic Freedom, which takes into account 12 quantitative and qualitative factors (including government integrity, fiscal health, business freedom, trade freedom and investment freedom), and has held this position for the last 22 years[28]. Hong Kong also ranks 4th out of 190 economies on the World Bank's "ease of doing business" rankings[29].

Geographically, Hong Kong is located at the heart of Asia. Key Asian cities such as Beijing, Shanghai, Singapore, Taipei, Manila and Kuala Lumpur are in the same time zone as Hong Kong; Bangkok, Jakarta, Seoul and Tokyo are all within an hour's difference. Hong Kong's success as a gateway to other Asian markets is underpinned by peerless transport connections in the region. All of Asia's key markets are less than four hours' flight time from Hong Kong; half of the world's population is within five hours' flight time from Hong Kong[30].

Figure 3.1 Hong Kong's strategic location[31]

[28] Heritage Foundation, 2017 Index of Economic Freedom, http://www.heritage.org/index/country/hongkong; The Government of the Hong Kong Special Administrative Region InvestHK, *Why Hong Kong*, http://www.investhk.gov.hk/why-hong-kong/international-transparent-and-efficient.html (last modified on 25 October 2016)
[29] The World Bank, "Ease of Doing Business" Economy Rankings (2017), http://www.doingbusiness.org/rankings
[30] The Government of the Hong Kong Special Administrative Region InvestHK, *Why Hong Kong*, http://www.investhk.gov.hk/why-hong-kong/strategic-location.html (last modified on 25 October 2016)
[31] Source: refer Note 29

In particular, Hong Kong is a proven gateway into the Chinese high growth market and has been used as an entry point by Australian exporters seeking to enter the Chinese market. China remains a mainstay in supporting the global economic growth. The World Bank is projecting a growth of 6.5 percent in 2017 for China and a medium-high growth looking further ahead[32]. The growth in China and other parts of Asia represents an opportunity for Australian businesses looking to increase market share (in particular, through increased service exports to the region). Australian companies looking to do business in Asia would benefit from the conclusion of a DTA between Australia and Hong Kong. By fostering increased trade and investment between Australia and Hong Kong, a DTA between the two jurisdictions is also supporting enhanced access to Asian markets (through Hong Kong) for Australian businesses.

3.3 Australia as a major financial centre in Asia

We understand that Australia is seeking to establish closer economic ties with Asia and to further its status as a major financial centre in the region. In this area, Hong Kong is widely seen as one of the leading international and regional financial centres in Asia, and the head or regional office location to some of Asia's largest corporate groups and many multinational corporations.

By entering into a DTA with Hong Kong, Australia would be taking a step towards fostering closer economic ties with Asia because of the role that Hong Kong has in international financial and capital markets, and achieving improved interoperability between Australia and Hong Kong as two of the key financial centres in the region.

Australia and Hong Kong have already sought to foster closer collaboration on renminbi ("RMB") trade settlement, the development of RMB-denominated products and closer RMB banking and financial links, with regard to the increasing importance of the RMB as a trade and investment currency in the region. Hong Kong was the first offshore market to launch the RMB business in 2004, and remains the largest offshore RMB hub[33]. In 2012, Australia and Hong Kong established a high-level dialogue between respective senior business leaders to identify new opportunities arising from RMB use in trade and investment in the region. The first Australia-Hong Kong RMB Trade and Investment Dialogue was held in Sydney (April 2013); the second in Hong Kong (May 2014); and the third was again held in Sydney (July 2015). Based on SWIFT's latest RMB tracker (February 2017), Australia currently ranks as the 8th largest offshore RMB clearing centre[34].

3.4 Co-operation on international tax integrity

An important feature of the Hong Kong DTA is the inclusion of a standard OECD information exchange article, which will give Australia the ability to request and exchange

[32] Refer Note 5
[33] Hong Kong Monetary Authority ("HKMA"), *Hong Kong: The Global Offshore Renminbi Business Hub*, January 2016, http://www.hkma.gov.hk/media/eng/doc/key-functions/monetary-stability/rmb-business-in-hong-kong/hkma-rmb-booklet.pdf
[34] SWIFT, RMB Tracker: Monthly reporting and statistics on renminbi ("RMB") progress towards becoming an international currency, February 2017, retrieved from https://www.swift.com/our-solutions/compliance-and-shared-services/business-intelligence/renminbi/rmb-tracker/document-centre

information with the tax authorities in Hong Kong. Hong Kong, as a leading financial centre, has now adopted the Common Reporting Standard ("CRS"). Under the CRS framework, financial institutions in Hong Kong are required to collect and report the financial account information relating to tax residents of "reportable jurisdictions" to the Hong Kong Inland Revenue Department ("IRD"), commencing 2018 with respect to 2017 account information. Subject to entering into the relevant bilateral agreements, Hong Kong can then also exchange the CRS information automatically with other jurisdictions.

Hong Kong's list of reportable jurisdictions currently comprise Japan and the UK, and there are plans to add a further 72 jurisdictions to this list (which includes Australia) with effective from 1 July 2017[35]. For these new reportable jurisdictions, the IRD can only exchange the CRS information with the other relevant jurisdiction after it has signed a Competent Authority Agreement with that jurisdiction.

A DTA between Australia and Hong Kong in these circumstances would therefore enable tax officials to detect and prevent tax avoidance and evasion in both jurisdictions. Specifically, a DTA would enable Hong Kong to conclude a Competent Authority Agreement with Australia, which will allow it to exchange information on an automatic basis with Australia.

As signatories to the Inclusive Framework on BEPS and the Multilateral Instrument (which implements standards for countering treaty abuse, improving dispute resolution mechanisms and strengthening the tax treaty related measures developed under the BEPS Project), a DTA between Australia and Hong Kong would provide the two jurisdictions with the opportunity to coordinate their approach and to give effect to the G20/OECD's recommendations for addressing the risk of tax base erosion and profit shifting by multinationals using artificial or contrived arrangements. For example, features between the DTA between Australia and Hong Kong could include provisions for revenue agencies in the two jurisdictions to assist each other in the collection of any outstanding tax debts, and to clarify the circumstances in which a taxable "permanent establishment" will arise.

A DTA between Australia and Hong Kong would demonstrate that both jurisdictions remain committed to maintaining a fair tax environment and aligning with international standards on tax modernisation.

[35] Hong Kong Legislative Council Panel on Financial Affairs, *Update on Implementation of Automatic Exchange of Financial Information in Tax Matters ("AEOI")*, LC Paper No. CB(1)660/16-17(09) for discussion on 16 March 2017, http://www.legco.gov.hk/yr16-17/english/panels/fa/papers/fa20170316cb1-660-9-e.pdf

4 Comparison: Singapore DTA

It is relevant to note that Australia concluded a DTA with Singapore in 1969, a jurisdiction with a similar taxation system to Hong Kong. Both Singapore and Hong Kong have a "territorial" system of taxation such that it is only income sourced in that country which is subject to tax there.[36] Further, Singapore does not impose tax on capital gains or dividends. Singapore also has a comparable corporate tax rate to Hong Kong, being 17%. In addition, Singaporean withholding tax rates for recipients resident in a non-tax treaty jurisdiction are 10% for royalties, and 15% for interest.

Under the Australian DTA with Singapore, the withholding tax rates are;

— 15% for interest; and

— 10% for royalties.

As noted above, Singapore does not impose withholding tax on dividends.

Similar to a DTA between Hong Kong and Australia, under the Singapore treaty, Singapore has not forgone any withholding tax as result of entering in to the DTA. Yet, this is as we understand, is one of the key reservations that Australia may have when considering a DTA with Hong Kong. The Australia – Singapore DTA may therefore serve as a useful reference point in negotiations between Hong Kong and Australia. As Australia has had such a long standing DTA with Singapore, Australia should be able to reach an agreement on a DTA with Hong Kong, which has a similar tax system to Singapore.

[36] However, Singapore also taxes companies on foreign source income remitted into Singapore, which has been taxed at a rate less than 15%

5 Perceived loss of revenue

As outlined above, a DTA between Australia and Hong Kong would bring clear benefits to both jurisdictions. However, for Australia, we understand that there had been concerns in the past on the potential loss of revenue that may occur under a DTA.

Ordinarily, both parties entering into a DTA would make reciprocal withholding tax rate reductions. However, Hong Kong generally does not levy withholding taxes (it does impose a low rate of withholding tax on royalties, however this is likely to be the same rate specified in a DTA) and therefore, Hong Kong should not actually forego any withholding tax.

By way of reference, Australian withholding tax rates for recipients resident in a non-tax treaty jurisdiction are;

— 30% for unfranked dividends;

— 30% for royalties; and

— 10% for interest.

We understand that the principal concern in Australia if it were to enter into a DTA with Hong Kong, would be the impact this may have on revenue collection. However, expectations of a loss of revenue may be more illusory than real. In an article that discussed the impact that a DTA with Hong Kong would have for Australia[37], in the context of employment income and business profits, the conclusion was that a DTA should only have a minimal impact from a revenue perspective. More particularly, the article also concluded that an agreement would provide taxpayers from both jurisdictions with increased certainty about their exposure to tax in the jurisdictions.

One of the main benefits of a DTA is that the reduction in withholding taxes that apply to dividends and interest. However, a DTA between Hong Kong and Australia is likely to have little impact in this regard. In the case of dividends, the impact is likely to be negligible because only unfranked dividends are subject to withholding tax in Australia. An unfranked dividend refers to, broadly, dividends paid by companies out of profits which were not subject to Australian tax. Accordingly, any reduction in the dividend withholding tax rate is likely to have immaterial impact on the current revenue collection in Australia in respect of dividends paid to Hong Kong residents.

In respect of interest, Australia's DTAs typically do not offer a lower withholding tax rate. As such, there would be no impact on the revenue collection for Australia in respect of interest withholding tax.

However, the article acknowledged that a DTA was likely to negatively impact the withholding tax revenues collected by Australia from royalties paid to residents of Hong Kong. Ordinarily, we would expect the royalty withholding tax in a DTA to be reduced to 10% (resulting in a reduction of 20% for Australia). It is acknowledged that the most significant impact that the signing of a DTA would have is on taxation of royalties by Australia. However, international corporations with potential royalty cross-border payments are likely to structure contract terms to ensure the payments are made in the most tax efficient manner. Although we have not sighted any applicable data, we would

[37] Nolan Cormac Sharkey and Kathrin Bain, eJournal of Tax Research Volume 9 Number 3, December 2011, *An Australia-Hong Kong double tax agreement: Assessing the costs and benefits*

not expect significant royalty payments being made from Australia to Hong Kong. Accordingly, we would question the significance of a reduction on royalty withholding tax on revenue collection in Australia. In any event, if this were a concern to the Australian Government, this issue could be dealt with in the DTA. That is, the DTA would be agreed with no reduction in withholding taxes for royalties.

It is important to note however, that to the extent Australia has concerns on the possible loss of revenue from any part of a DTA, the Hong Kong Government would, we believe, be prepared to be flexible and address any such concerns in the course of the DTA negotiations. As noted, royalty withholding tax is an article Hong Kong could carve out of a potential DTA for the purposes of negotiations with Australia.

Further, Hong Kong's existing DTA network covers most of Europe and Asia (including many advanced economies such as the UK, Canada, Japan and France). We understand that Hong Kong's existing treaty partners have benefited from entering into a DTA with Hong Kong in that the DTA has made treaty partner jurisdictions a more attractive destination for investment from Hong Kong (including investment from Chinese investors that structure their investments through Hong Kong) and have supported their growing presence in Asia, without significant loss in revenue from entering into the DTA.

For comparison, we note that New Zealand (which has a comparative tax system to Australia) signed a DTA with Hong Kong on 1 December 2010. The revenue cost to New Zealand as a result of the reduction in withholding rates afforded in the DTA was expected to be relatively small, at approximately NZ$0.5 million per year.[38] In this case, the New Zealand Parliament was satisfied that the advantages of the entering a DTA with Hong Kong outweigh the potential disadvantages. From an Australian perspective, a DTA would almost certainly result in increased trade and investment flows between Australia and Hong Kong, which should, in our opinion, outweigh any potential loss of revenue from, for example, reduced withholding taxes on profit flows offshore. Should this issue continue to be a concern of Australia, Australia should consider engaging in a similar exercise in attempt to quantify, if any, the loss of revenue as a result of entering into a DTA with Hong Kong.

[38] Parliament *of New* Zealand, Dr Craig Latham, *National Interest Analysis: Double Tax Agreement with the Hong Kong Special Administrative Region of the People's Republic of China*

6 A more internationally competitive Australia

According to the World Economic Forum's Global Competitiveness Index (2016-17) ("Index"), which assesses the competitiveness of 138 economies in a global context, Australia ranks 22nd overall[39]. In comparison, Hong Kong has ranked in the top 10 for the fifth consecutive year[40]. The Index highlights that "tax rates" and "tax regulations" are two of the top five most problematic factors for doing business in Australia.

This is consistent with the Governor of the Reserve Bank of Australia's ("RBA") recent comments that there is a need to ensure that Australia's tax system is internationally competitive given the impact on Australia's attractiveness as a destination for trade and investment, which plays a critical role in Australia's future prosperity[41]. The RBA Governor noted that from a government revenue perspective, this may be supported through reducing spending or rebuilding revenue in other areas.

We understand that the Australian Government recognises the risk of Australia falling further behind international competitors and the role of reducing the tax burden on Australian employers in managing this challenge[42]. In particular, the Government has responded with a fully funded "Ten Year Enterprise Tax Plan", which is aimed at reducing the Australian corporate tax rate to help Australian businesses compete, noting that 15 years ago, Australia enjoyed the 9th lowest corporate tax rate amongst advanced economies whereas today, Australia (corporate tax rate of 30%) has the 6th highest corporate tax rate amongst 35 OECD countries[43].

According to the OECD's report on tax developments across OECD countries, the average corporate tax rate declined from 32% in 2000 to 25% in 2015 with five OECD countries having implemented rate reductions in that year[44]. Looking ahead, many countries such as the US, UK, France, Japan and Italy announced plans to lower their corporate tax rates. In particular, the UK has announced a reduction of its headline corporate tax rate down to 17% by 2020 to provide "the right conditions for business investment and growth", following government analysis showing that the reduction in tax rates could increase gross domestic product ("GDP") by between 0.6% and 1.1% longer term[45]. In the US, which has one of the highest statutory corporate tax rates in the world (35%), President Trump has indicated in his first joint address to Congress on 28 February 2017 that his economic team "is developing historic tax reform that will reduce

[39] World Economic Forum, Global Competitiveness Index (2016-17), Australia, http://sjm.ministers.treasury.gov.au/media-release/011-2017/
[40] World Economic Forum, Global Competitiveness Index (2016-17), Hong Kong, http://reports.weforum.org/global-competitiveness-index/country-profiles/#economy=HKG
[41] Reserve Bank of Australia ("RBA") Governor Philip Lowe's Speech at the A50 Australian Economic Forum Dinner on 9 February 2017, https://www.rba.gov.au/speeches/2017/sp-gov-2017-02-09.html
[42] The Honourable Scott Morrison MP, Treasurer of the Commonwealth of Australia, Media Release, "Labor has run out of excuses on business tax cuts as RBA governor exposes their threat to jobs", 10 February 2017, http://sjm.ministers.treasury.gov.au/media-release/011-2017/
[43] The Honourable Scott Morrison MP, Treasurer of the Commonwealth of Australia, Media Release, "Turnbull Government's Enterprise Tax Plan to drive investment, jobs and wages", 1 February 2017, http://sjm.ministers.treasury.gov.au/media-release/005-2017/
[44] OECD, Tax Policy Reforms in the OECD 2016, 22 September 2016, http://www.oecd-ilibrary.org/taxation/tax-policy-reform-in-the-oecd-2016_9789264260399-en
[45] HM Revenue & Customs, Policy Paper: Corporate Tax to 17% in 2020, 16 March 2016, https://www.gov.uk/government/publications/corporation-tax-to-17-in-2020/corporation-tax-to-17-in-2020

the tax rate on our companies so that they can compete and thrive anywhere and with anyone. It will be a big, big cut"[46].

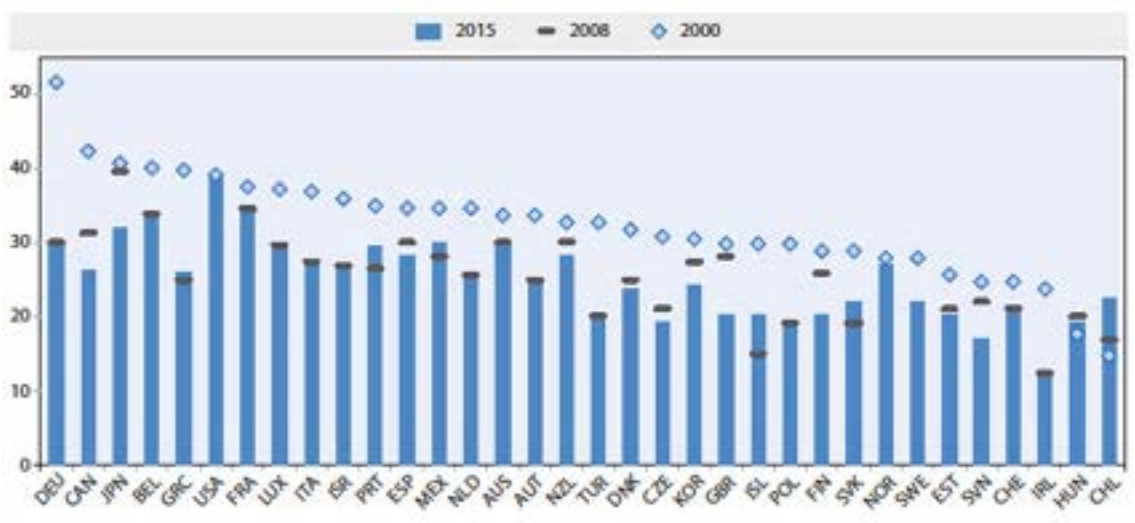

Figure 6.1 Downward trend in corporate tax rates[47]

The OECD predicts that the downward trend on corporate tax rates is accelerating as the focus of tax reforms have shifted towards the pursuit of economic growth by reducing taxes on labour and corporate income[48].

In light of these trends in other parts of the world, a DTA between Australia and Hong Kong would help Australia to remain internationally competitive. Currently, more than 500 Australian businesses are headquartered in Hong Kong, and more than 1,000 Australian businesses have representative offices in Hong Kong[49]. As outlined above, there is also an opportunity for Australian businesses that do not currently have a presence in Hong Kong to expand into the region to realise the potential of Asian markets.

Businesses have always wanted the right people in the right places. However, the level of investment required to implement international assignments are often an issue from a planning, cost and time perspective.

International short term assignments can lead to additional tax and administrative costs on employees and employers. A DTA between Australia and Hong Kong facilitates the mobilisation of employees between these jurisdictions by removing tax related impediments for short term assignments. In particular, the DTA can provide a level of protection for both employees operating cross-border under short term assignments and the relevant employers by providing greater certainty and simplicity when it comes to assessing and complying with the tax requirements on both sides (e.g. whether the

[46] The White House, Office of the Press Secretary, Remarks by President Trump in Joint Address to Congress, 28 February 2017, https://www.whitehouse.gov/the-press-office/2017/02/28/remarks-president-trump-joint-address-congress
[47] Source: refer Note 43
[48] Refer Note 43
[49] Refer Note 20

employee is satisfying their tax obligations in the relevant jurisdictions and whether employee movements are triggering any tax reporting and withholding obligations for the business. In the absence of a DTA, there could be potential cash flow issues for employees, an additional layer of cost for employers and employees as well as increased administrative burden for both employees and employers[50].

By removing impediments to short term assignments, a DTA between Australia and Hong Kong supports Australian businesses with achieving overall business goals and objectives such as expansion into new markets (e.g. China's high growth markets), regional business management and global leadership development. For example, Australian businesses with regional operations may require the skills and experience of a particular Australian based employee in their Hong Kong office (e.g. an employee with a regional Asia-Pacific role); Australian business with Hong Kong headquarters may require a particular Hong Kong based employee (e.g. senior level management from the Hong Kong head office) in Australia to develop particular set of skills for staff in Australia (i.e. build the talent pool) or to grow a part of the business in Australia. The mobilisation of employees between Australia and Hong Kong could also be desirous for designated projects that require closer collaboration and connectivity between participating employees in Australia and Hong Kong.

[50] Individuals operating between Australia and Hong Kong may be subject to tax on the same employment income under the tax rules of both Australia and Hong Kong. Although it is possible to avoid double taxation by the individual claiming credits in their individual income tax return for the tax already paid in the other jurisdiction ('foreign tax credits") as an offset against the tax liability in their home jurisdiction, the mechanism for claiming foreign tax credits can result in cash flow issues for the individual. For Hong Kong employees operating in Australia, there could also be an additional layer of tax as the applicable tax rate in Australia is higher than in Hong Kong. In practice, employers may seek to manage this issue by providing a loan to the relevant individual(s). However, this results in additional costs for employers seeking to use such short term assignments to maintain competitiveness and/or expand into new markets. Further, in the absence of a DTA between Australia and Hong Kong, there could also be employer reporting obligations in both jurisdictions in respect of the salary and benefits paid to the individual operating cross-border.

7 The way forward

We understand that the general consensus in the business community in Australia is in favour of Hong Kong and Australia concluding a DTA.

Hong Kong and Australia have extensive business and social ties, and a DTA would further promote cross-border trade, investment and employment between the two jurisdictions.

It is important to raise the debate on the potential advantages to Australia from concluding a DTA with Hong Kong, rather than focusing on any possible loss of revenue from a reduction in Australian withholding tax rates. As outlined above, the potential advantages from entering into a DTA, for both jurisdictions, far outweigh any potential disadvantages (if any).

Against a backdrop of global political and economic uncertainties, and given what is at stake as the world becomes smaller and the Australian economy continues to transition away from the mining boom, now is the time to prioritise entering into a DTA between Australia and Hong Kong to foster increased cross-border trade and investment in the region and secure economic growth into the future.

A Hong Kong's DTA network

The table below lists those jurisdictions (37) that, as of 28 February 2017, have signed a comprehensive tax treaty with Hong Kong.

Austria	Japan	Portugal
Belarus	Jersey	Qatar
Belgium	Korea	Romania
Brunei	Kuwait	Russia
Canada	Latvia	South Africa
China (Mainland)	Liechtenstein	Spain
Czech Republic	Luxembourg	Switzerland
France	Malaysia	Thailand
Guernsey	Malta	United Arab Emirates
Hungary	Mexico	United Kingdom
Indonesia	Netherlands	Vietnam
Ireland	New Zealand	
Italy	Pakistan	

The table below lists those jurisdictions that, as of 28 February 2017, Hong Kong is engaged in negotiations with for a comprehensive tax treaty.

Bahrain	India	Nigeria
Bangladesh	Israel	Pakistan
Cyprus	Macao SAR	Saudi Arabia
Finland	Macedonia	Turkey
Germany	Mauritius	

B Australia's DTA network

The table below lists those jurisdictions (44) that, as of 28 February 2017, have a comprehensive tax treaty with Australia. This includes 25 jurisdictions that have separately signed a comprehensive tax treaty with Hong Kong.

Argentina	Ireland	Singapore
Austria	Italy	Slovakia
Belgium	Japan	South Africa
Canada	Kiribati	South Korea
Chile	Malaysia	Spain
China (Mainland)	Malta	Sri Lanka
Czech Republic	Mexico	Sweden
Denmark	Netherlands	Switzerland
Fiji	New Zealand	Taipei
Finland	Norway	Thailand
France	Papua New Guinea	Turkey
Germany	Philippines	United Kingdom
Hungary	Poland	United States
India	Romania	Vietnam
Indonesia	Russia	

Assistant Secretary, Personal and Small Business
Tax Branch
Personal and Indirect Tax and Charities Division,
The Treasury
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By email: individualtaxresidency@treasury.gov.au

22 September 2023

Dear Sir / Madam,

Consultation on modernising individual tax residency

We write on behalf of the Australian Chamber of Commerce in Hong Kong ("**AustCham**"), in respect of the July 2023 consultation on the proposed changes to the Australian individual tax residency rules (the "**New Residency Rules**"). The consultation relates to changes that were first announced by the then Government in the FY20/21 Budget following a review of the Australian tax residency rules by the Board of Taxation in August 2019.

Our submission is focussed on ensuring that Hong Kong based Australians and Australian businesses operating in Hong Kong are on a similar footing (or at least no worse off) than Australians residing in jurisdictions that have concluded a double tax agreement with Australia.

The Consultation outlines the background to the review that was undertaken by the Board and their recommendations to modernise and simplify the current residency rules. The proposed changes are designed to ensure that the tax residency framework is consistent with the principles of adhesive residency, certainty, simplicity, and integrity.

When the proposed changes were first outlined back in 2019, we had the opportunity to engage with various arms of government, including Treasury, outlining our views as well as highlighting several areas of concern that the changes could have for many expatriates, but especially for Hong Kong residents.

At that time, we expressed our support for the stated aims of achieving simplicity in determining tax residency and greater certainty for globally mobile individuals and their employers. However,

there were several real concerns over the harsh adverse impact that the proposed changes could have on Australian businesses and individuals living in Hong Kong and elsewhere in Asia.

In particular, we highlighted how adverse the amendments will be for Hong Kong based Australians and Australian businesses operating in Hong Kong. Hong Kong plays an important role as a global financial centre as well as regional headquarters and trading hub for many Australian businesses. There are approximately over 100,000 Australian nationals living in Hong Kong, many of whom would travel frequently to Australia for work and leisure,

This number of businesses and Australian individuals demonstrates that Hong Kong tax residents will be uniquely impacted by these new residency rules more so than perhaps any other jurisdiction given that there is no double tax agreement in force between the two jurisdictions (unlike the other jurisdictions with high number of Australia businesses and individuals being Singapore, the United Kingdom, and the United States). Australian citizens and permanent residents living and working in Hong Kong (irrespective of the duration that they have lived outside Australia) are likely to be severely impacted under the proposed changes.

The new residency rules, as currently proposed, will result in an inequitable outcome for Hong Kong based employees. This will be adverse to Australian businesses as it will materially impact their ability to attract staff and executives to Hong Kong. It follows that this will have a significant adverse impact on the role and influence of Australians in the region at a critical time, when continued deep engagement on the ground is required.

The consultation outlines the proposed framework for the updated tax residency rules as well as requesting feedback on a number of specific aspects of the proposed changes. Encouragingly, many of the questions for comments relate to the issues we have raised with various members of the Government during the consultation that occurred back in 2021. However, despite the concerns that were highlighted back in 2021, the proposed tax residency framework outlined in the consultation remains unchanged from what was first proposed. This is disappointing.

Summary of substantive change requested

It is AustCham's submission that the inequitable outcomes, based merely on whether there is a double tax agreement with that jurisdiction, should be addressed through the introduction of a tie breaker test, similar to OECD Model Tax Convention on Income and Capital, where the Secondary Test applies.

The tie breaker provision ensures that individuals that are genuinely tax resident in another jurisdiction are not discriminated against and unfairly treated resulting in double tax based merely on their home jurisdiction. This discrimination and inequity will be experienced by those individuals that live and work in Hong Kong as it does not have a double tax agreement with Australia and is not expected to finalise one with Australia in the immediate future.

It is acknowledged that the introduction of such a tie breaker would, in part, be contrary to the Government's current position on the implementation of residency not being aligned with outcomes under a double tax agreement[1]. However, the tie breaker test is well understood by the ATO and tax advisers and would not, as asserted, make it more complicated for taxpayers. Indeed, it would allow for clarity on a taxpayer's residency if that individual were a genuine tax resident of Hong Kong (or another jurisdiction).

The Secondary Test, if adopted with or without amendments (which may increase the complexity) such as the exclusion of days, even an increased number of days, or different or additional factors, will distort how an individual will conduct themselves and their affairs if they move from or to Australia.

Key features of the changes

The consultation outlines the key features of the changes to the residency rules, which remain the same as the proposals announced back in 2021 as recommended by the Board. The New Residency Rules framework has the following features:

- Physical presence in Australia being the primary measure of residency, on the grounds that this would be aligned with international practice.
- The rules will focus on a connection with Australia; and
- The rules will apply additional factors to be determined objectively whether a person would be considered a tax resident or not.

Based on these features, the proposed changes will involve Primary and Secondary tests.

- The Primary Test

  The Primary test being that if a person was physically present for 183 days or more in Australia in any income year, that person would be considered to be a tax resident of Australia. In addition, if a person is physically present in Australia for less than 45 days in any income year, they will be deemed to not be tax resident.

- The Secondary Test

  The Secondary Test gives rise to the greatest number of concerns. The Secondary Test will apply where a person is in Australia for between 45 and 182 days for whatever reason. Under that test, if 2 out of the 4 secondary tests were satisfied, then such persons will be considered tax resident in Australia – subject to the application of any applicable comprehensive double tax agreement that may be in force with Australia.

[1] Paragraph 62 of the Consultation Paper

Our concerns therefore remain, for many Australians living and working in Hong Kong, the test will ultimately become a '45-day rule' as persons are likely to easily satisfy 2 out of the 4 tests. As such, Australian nationals living and working in Hong Kong will be at risk of being Australian tax resident if they spend more than 45 days in Australia. This is why we are of the view that Hong Kong will be uniquely adversely affected by the proposed changes given Hong Kong does not have a double tax agreement with Australia.

Further, given Hong Kong's role as a global financial centre, a trading hub for the region and the gateway for capital flows to and from mainland China, many businesses require their Hong Kong based employees to travel extensively, including to Australia. Hong Kong is an attractive base for Australian businesses wishing to take advantage of the gateway to China. It is unique in that Australian Business can second or relocate their Australian based individuals to Hong Kong because the infrastructure (e.g. schools, language, legal system, banking system, Australian teachers and curriculum) to support Australians living in Hong Kong is not readily replicated in China or other Asian jurisdictions.

This could therefore seriously disrupt the way in which Australians and Australian businesses in Hong Kong conduct their business dealings with China and Australia. It would particularly impact businesses in the Education, Aviation, Tourism and Financial Services Sectors, amongst many others.

Consultation questions 1 and 2. How many days in an income year should an individual with strong connections to Australia be able to spend in Australia before they are considered tax resident?

This is a particularly important issue for Australians in Hong Kong given the absence of a comprehensive double tax agreement with Australia.

We acknowledge the comment in paragraph 62 of the consultation paper that the Government is not planning to align the domestic residency rules with outcomes under the double tax agreements, despite the Board of Tax's recommendation, on the basis that it would make it more complicated for taxpayers. We do not agree that such an adoption of the tie breaker would make it more complicated for taxpayers. Indeed, we are of the view that the adoption of the double tax agreement position makes the new test equitable and simplifies the potential application of these new provisions.

We are of the view that for Australian nationals that are tax resident in Hong Kong, the rules should apply a tie breaker test for such persons. That is, Hong Kong tax residents should be able to spend up to 182 days in Australia before they are able to be considered tax resident, provided they satisfy a tie breaker test. The purpose of the tie breaker test is to align Hong Kong tax residents with Singapore tax residents, who will benefit from the double tax agreement with Australia (and residents of other jurisdictions with a double tax agreement with Australia). This

would allow Australian businesses to allow their employees to travel to and from Australia for work purposes, whilst allowing Australians to continue to visit family and friends in Australia.

The tie breaker test could be introduced as part of the legislative amendments to the residency rules and would effectively operate, if the Secondary Test applies, to test if that individual is a genuine tax resident of another jurisdiction, We believe that this would be a simpler, and equitable solution to what would otherwise be a significant problem for Australian businesses (as an Australian business or individual should not be treated differently merely because of the jurisdiction within which they reside. We would recommend that the tie breaker be consistent with the OECD Model Tax Convention on Income and Capital[2], which is widely adopted, and it would provide an objective and well understood test for those individuals with legitimate claims of tax residency elsewhere, such as in Hong Kong.

Consultation question 2. Should some days spent in Australia under circumstances be disregarded for the purposes of the 45-day count?

We firmly are of the view that the 45-day count is unworkable as it would easily result in many foreign tax residents becoming Australian tax residents merely from carrying out their regional employment duties as well as visiting family and friends. As explained above, for persons that have established a genuine tax residence outside of Australia, the threshold must therefore be increased to a more reasonable limit – say,182 days.

In the absence of a tie breaker provision, the proposed day count would somehow need to take into account the nature of the visits, and therefore some visits would need to be disregarded for the purposes of the count. However, we acknowledge that having a rule that excludes some days, will involve an element of subjectivity (requiring supporting materials), that could lead to uncertainty and perhaps even challenge. This would not be in line with the purported objectives of simplicity and certainty.

Disregarding days could be done in one of two ways, but both of these could result in unwanted complexity. For example, the framework could disregard days for employment related duties where there is no nexus with a permanent establishment in Australia. Alternatively, non-workdays could be excluded so that visits to Australia for holidays or to visit family and friends are not taken into account for the purposes of the 45-day rule test.

As you will appreciate, both alternatives may give rise to some level of judgement and therefore some uncertainty and a blurring of the lines between whether a day in Australia was for one purpose or another, together with how an individual is able to support an assertion that a day is outside the relevant count. Accordingly, consistent with the themes of simplicity, certainty, and integrity we recommend a tie break type provision be introduced into the legislation such that a

[2] See Article 4 of the OECD Model Convention with respect to Taxes on Income and Capital (2017)

person with a genuine tax residence, say in Hong Kong, would have a day limit of 182 days before becoming an Australian tax resident. As mentioned already, the inclusion of the tie breaker provision would be in line with international best practice and provide all individuals equitable treatment in determining their Australian tax residency.

Consultation questions 3, 4, 5 and 6. Could any of the four factors be defined differently? Are there any other factors better suited to identifying individuals with strong connections to Australia in an objective and simple way?

Although the intention of the changes is to simplify the criteria of when an individual will be treated as an Australian tax resident, the effect of the proposals announced is likely to result in Australians living and working in Hong Kong and elsewhere in Asia for many years being Australian tax residents going forward. The concerns stem from the construction of the Secondary Test of the New Residency Rules, which considers not just physical presence in Australia but other factors. Indeed, these other factors are such that most Australian nationals would easily satisfy at least two of the tests.

Under the proposed rules, Australian nationals and permanent residents can be treated as tax resident if they are physically in Australia for 45 days or more in a year if they also satisfy two out of the four additional substantive ties or nexus factors outlined in the framework. Broadly, the four-factor test, for Australian nationals or permanent residents, is, for pragmatic purposes, a one factor test. The other three factors follow themes in the OECD Model Tax Convention on residency for individuals but implement a threshold at a much lower level such that genuine foreign tax residents are likely to satisfy two of the four factors. The other three factors are:

- Australian family connections;
- the ownership of property in Australia and having a legal right to access such accommodation; and
- other Australian economic interests, which include participation in a business or even a bank account with 'significant' cash in the account.

Simply being an Australian national or permanent resident and either having a dependent living in Australia or a property available for use in Australia would satisfy two of the conditions. The ease with which many Australians would therefore satisfy these additional factors means that the Secondary Test is simply a '45 day in Australia' test, i.e., if a person is in Australia for 45 days or more in a year, then they will be treated as a tax resident.

Given Hong Kong's role as a global and regional financial centre and trading hub, many employees are required to travel extensively for business. For many Hong Kong residents, the introduction of the changes would mean that they will need to limit the number of visits each year to less than 45 days so as not to be considered a tax resident. This would especially be the case for someone that needs to travel to Australia frequently for business, which would "eat into" the number of days they could visit family and friends. Business could therefore be impacted by the

changes, as it could either result in less engagement in Australia, a significant adverse impact on the ability to attract Australian staff to Hong Kong or it could increase the cost of doing business as they need to compensate employees for the additional tax burden and compliance. Further, families would certainly reconsider sending their children to Australia for education if it put them at risk of being "inadvertent" Australian tax residents.

As currently drafted, no consideration is given to individual circumstances that may require unplanned and/or extended trips to Australia. Such visits could include for medical reasons, bereavements or visiting unwell members of family.

There are several solutions that should be considered.

As highlighted above, the day count could disregard certain types of visits to Australia - such as business related visits where there is no nexus with a permanent establishment being created in Australia. Alternatively, non-workdays, weekends and public holidays could be excluded so that visits to Australia for holidays or to visit family and friends are not taken into account for the purposes of the 45-day rule test.

As you will appreciate, both alternatives will give rise to some level of judgement and therefore some uncertainty and a blurring of the lines between where a day in Australia was for one purpose or another. Accordingly, we prefer a tie break type provision be introduced into the legislation such that a person with a genuine tax residence in Hong Kong would have a day limit of 182 days.

Satisfying two or even three out of the four tests should not necessarily mean that a person would automatically be treated as a tax resident of Australia. In such circumstances, a person may still not have a connection to Australia that warrants they be treated as a tax resident, especially if they have maintained a home and a genuine tax residence outside of Australia for many years. The inclusion of the tie breaker, if the Secondary Test applies, would ensure that genuine tax residents of other countries would not be unfairly caught.

There are other proposed changes that should be considered include:

- The accommodation test should only apply where a person is maintaining a property for their sole use when in Australia and not the use of a family member;
- The economic interests should only include situations where a person was actively engaged in a trade or business in Australia or where they commonly carried out their employment duties in Australia. It should not cover other investments that a person may have in Australia, including a bank account, or where those investments are managed either by third party investment managers or where they are managed from outside of Australia.
- The family connection should not cover situations where a person may have children at school in Australia, including a boarding school. It should also not cover situations where a person is present in Australia for personal reasons, such as supporting elderly parents or other family members and for medical treatment and convalescing

Consultation questions 9 and 10. Ceasing short term and long-term residency tests.

We have a real concern that the proposed changes will make it more difficult to attract senior executives to Australia if they are likely to continue to be tax resident for a period of time even after leaving Australia permanently. This will ultimately make Australia less attractive as an investment jurisdiction.

There has been a focus by Australia to entice international businesses and talent to Australia with an emphasis on leveraging the lifestyle and proximity to Asia. Following the Covid-19 pandemic and the rise in agile working, Australia should be well placed to attract entrepreneurs and experienced business leaders to relocate to Australia. Hong Kong has been specifically singled out as a source of talent and investment.

However, the proposed new rules will make it harder for senior executives to consider Australia if they are likely to remain Australian tax residents for a period of up to 2 years after they permanently depart Australia. Under the proposals, a person who relocates to Australia and establishes a tax residency for more than 6 years would continue to be tax resident for a period of two years even after they have departed Australia.

The rules clearly make it harder to cease being a tax resident of Australia upon departure from Australia and are viewed as excessively sticky and unreasonable. This would certainly come as a surprise to many senior executives given that in most countries, a person typically ceases being a tax resident at the time they leave the jurisdiction permanently. Senior executives and entrepreneurs are therefore likely to consider this to be a major disincentive to relocating to Australia and taking up permanent residence or Australian citizenship.

In our view, a long-term Australian resident should be considered to cease residency once they depart Australia permanently, with no intention of returning to Australia. This will be an issue that needs to be considered case-by-case. Persons should cease to be tax resident upon their decision to permanently depart from Australia regardless of whether they have an employment contract with an overseas employer. Australians who depart Australia permanently upon retirement or otherwise, should not be considered an Australian tax resident from the date they leave.

Consultation questions 11 and 12. Does the overseas employment rule strike the right balance between facilitating skills development through international experience and integrity of the tax residency rules?

We are firmly of the view that the proposed overseas employment rule will act as a deterrent to Australians that may seek experience overseas if they do not have an offer of employment at the time that they leave Australia.

It has become a rite of passage for many Australians to seek experience living and working overseas. This is a tradition that has benefited Australia and Australian businesses greatly over the years. Currently, an Australian that departs Australia permanently for an extended period of time should be able to establish themselves as a non-resident for tax purposes from the date that they leave. The new rules fundamentally change this position.

The proposed changes, inconsistent with the stated objective of simplicity, will greatly add to the compliance and reporting burden of Australians that leave Australia. For a period of up to 2 years, they could continue to be an Australian tax resident, subject to the application of any applicable double tax agreement. Again, therefore Australians moving to Hong Kong could be uniquely affected by the proposed new rule changes. In the absence of an offer of employment for a period of more than 2 years, such persons will continue to be tax resident in Australia.

Consultation 13. Transitional rules and how should they apply to persons that may already have departed Australia.

A basic principle of taxation should be that any changes should only be prospective and not prospective. As such, any changes that are made should only apply on a going forward basis.

At the very least the transitional rules should allow those persons that have already departed Australia sufficient time to adjust their connection with Australia having regard to the factors in the Secondary Test. This may include rationalising their investments in Australia, relocating family, and establishing alternate support structures for wider family members. All these factors are sensitive and require the person to undertake them in an orderly manner. Accordingly, the transitional provisions should:

- allow at least [2] years for a person to reorganise their affairs before the Secondary Test begin to apply; and
- disregard the activity of a taxpayer prior to the commencement of the proposed residency rules.

Conclusion

We support the stated aim of modernising the Australian tax system particularly where such reform is intended to provide certainty and simplicity for individuals regarding their tax residency status. At the same time, the reforms should seek to accommodate a reasonable level of equity and integrity.

However, the proposed new tax residency framework outlined in the Consultation is likely to adversely impact Hong Kong based residents and businesses more than any other location. This is due to Hong Kong's role as a global financial centre; a home to over 100,000 Australian nationals and importantly, the absence of a comprehensive double tax agreement.

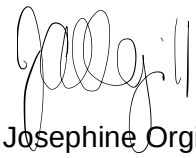
If the rules are implemented as outlined in the framework and there is no amendment to address the genuine concerns of Hong Kong tax residents doing business in the region, including Australia, the rules will have a significant impact on the cost of doing business. It is likely that Hong Kong tax residents would limit their business and personal visits to Australia and for those that must travel for business, it is likely to significantly increase the cost of doing business.

However, the integrity of the new framework can be maintained with some refinements.

For Australian nationals tax resident in Hong Kong, the rules should apply a 182-day test to determine residency. This would align Hong Kong tax residents with Singapore tax residents, which has a double tax agreement with Australia. This would therefore allow Australian businesses to allow their employees to travel to and from Australia for work purposes, whilst allowing Australians to continue to visit family and friends in Australia.

Finally, it is very important that the potential impact on businesses and tax residents of Hong Kong be addressed under the new framework. In the absence of any amendments to the rules as outlined in the consultation, the proposed changes will result in an additional cost to Australian businesses operating in Asia. Hong Kong based employees would be reluctant to travel to Australia either on business or for leisure, and it will also influence where they send their children to school and where they invest their wealth going forward.

Yours faithfully,



Josephine Orgill
Chair
The Australian Chamber of Commerce in Hong Kong

Appendix

Impact on Cost of doing Business

The proposed changes to the tax residency rules could have an additional cost to Australian businesses operating in Asia. For many such businesses, employees are required to travel extensively as part of their duties, which often includes business trips to Australia. This is especially the case for senior executives required to travel to head office in Australia, or for Asian based directors on Australian company boards.

It is quite conceivable that such employees may be reluctant to travel to Australia on business, as such days would count towards the proposed 45-day rule, which would mean less available days for personal travel to visit family and friends, or in a worse case, due to a prolonged illness or a medical emergency either to a family member or them personally in any particular year. This would have an impact on the way in which business could be conducted.

Hong Kong is an attractive base for Australian businesses wishing to take advantage of the gateway to China. It is unique in that Australian Business can second or relocate their Australian based individuals to Hong Kong because the infrastructure (e.g. schools, language, legal system, banking system, Australian teachers and curriculum) to support Australians living in Hong Kong is not readily replicated in China or other Asian jurisdictions. Notwithstanding this unique position Australian businesses could also find it more difficult to second employees from their Australian operations to postings in Hong Kong and Asia if such employees would still be considered tax resident in Australia. In the survey that we conducted of our members, the overwhelming majority indicated a reluctance to an overseas posting if they would continue to be a tax resident of Australia. From an employee perspective, the risk of being tax resident and subject to taxation in both jurisdictions (with a risk of double taxation) would outweigh the perceived benefits of an overseas posting, which would have significant implications for Australian businesses looking to expand into Asia. Of particular note is that with less Australian relocating to Hong Kong the role and influence Australian businesses and Australian individuals will have in the region will diminish.

The effect of the changes would be that Australian businesses may ultimately need to increase the compensation payable to employees to encourage them to move overseas. Employers would also need to schedule and track their employees' whereabouts to ensure they are not unintentionally caught by the rules. The foreseeable increase in costs and administrative burden would obviously conflict with the objective of the New Residency Rules – i.e. greater simplicity and lower compliance costs.

Education Sector

The education sector could be seriously impacted by the New Residency Rules. Australian teachers are highly sought after by international schools in Asia, particularly by the many

Australian international schools operating in the region, including in Hong Kong. Teachers are in a unique position in that they have extended summer holidays during which they would normally return home to spend time with family and friends. The 45-day threshold will make it much more difficult for such teachers to return to Australia for extended vacation periods as they would be at risk of becoming or remaining a tax resident of Australia. This could clearly act as a barrier to recruiting Australian teachers to move to Australian schools in Asia and seriously impact the ability of such schools to attract experienced and suitably qualified teaching staff.

The changes may also have an impact on Australian boarding schools. Australian nationals living overseas often enrol their children in boarding schools in Australia to benefit from the education system in their home country. Parents typically travel to Australia regularly and stay for an extended period during the school holidays to spend time with their children. In their current form, the ease with which Australian nationals could satisfy two of the four factors will undoubtedly discourage parents from sending their children to Australian boarding schools. We anticipate parents will instead opt for other well-regarded locations to send their children for schooling, such as the United Kingdom, given how easily they could be dragged into the Australian tax residency net.

Attracting Foreign Talent to Australia

Attracting senior executives to Australia under the New Residency Rules could be more difficult if it will be harder for them to cease to be a tax resident upon leaving Australia permanently.

We understand a Talent Attraction Taskforce has been established to entice international businesses and talent to Australia with an emphasis on leveraging the lifestyle and proximity to Asia to attract global business and foreign talent. The Government has cited the changing global environment, namely the Covid-19 pandemic and the corresponding rise in agile working, as reasons why employees, entrepreneurs and businesses may decide to relocate to Australia. Hong Kong has been specifically singled out as a source of talent and global business.[3]

Under the proposed changes, the rules could make it harder to cease being a tax resident of Australia upon departure from Australia. In particular, and what is viewed by our members as excessively sticky, a person that leaves Australia permanently after being a tax resident for several years could still find that they remain a tax resident for at least 2 years after they have left Australia. This would certainly come as a surprise to many people given that in most countries, a person typically ceases being a tax resident at the time they leave the jurisdiction permanently. Senior executives and entrepreneurs are therefore likely to consider this to be a major disincentive to relocating to Australia and taking up permanent residence or Australian citizenship.

There could also be unintended consequences for younger Australians who wish to broaden their experience and pursue overseas work experience opportunities. Such persons could also continue to be a tax resident for a couple of years after leaving Australia, which could act as a

[3]

disincentive to them when considering going overseas to explore new opportunities and experiences.

The Aviation Sector

The aviation sector is a prime example of an industry that could be significantly affected by the New Residency Rules. Hong Kong based Australian pilots and crew members who routinely travel between Hong Kong and Australia could find themselves being tax resident in both jurisdictions, even if their permanent home is in Hong Kong. In the absence of a tax treaty, an Australian pilot flying to Australia several times a month could be in Australia for more than 45 days. Landing in Australia at any time before midnight would count as one full day for the purposes of counting the number of days physically present in Australia under the New Residency Rules. The view of Australian members of the airline community in Hong Kong is that they are likely to be severely impacted by the changes given they often fly on the Australian routes. This would be a very unfortunate outcome given the aviation industry is a key enabler of many other economic activities and has already been significantly impacted by the ongoing Covid-19 pandemic.

Absence of a DTA with Hong Kong

Finally, many Australians living offshore, particularly in Hong Kong and Singapore, are concerned about how this rule will impact them. However, unlike Singapore, Hong Kong does not have a double tax agreement ("**DTA**") with Australia which would otherwise give Australians working in Hong Kong some added protection against becoming an Australian tax resident where they are also tax resident in Hong Kong. As such, Hong Kong based Australians would be uniquely impacted by the proposed residency changes given the absence of comprehensive DTA with Australia.

The benefit of having a DTA in force is that they typically contain tie-breaker provisions to determine the residency of an individual when an individual is considered a tax resident in two jurisdictions. Usually, it is the place where they have a permanent home, habitual abode, or strong economic and personal connections that determine which jurisdiction they are resident in. these tests are broadly reflected in some of the factors of the Secondary Test but the threshold to satisfy the factors in the Secondary test are significantly lower than that in a double tax agreement. For example, under the DTA signed with Australia, where a person is resident in both Singapore and Australia, the primary test of the tie breaker provides that an individual would be considered tax resident in Australia only if they have a permanent home available to them in Australia and no permanent home available to them in Singapore.[4]

[4] Article 3 of the Agreement between the Government of the Commonwealth of Australia and the Government of the Republic of Singapore for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income.

The absence of a DTA between Hong Kong and Australia is particularly concerning for the Australian business community in Hong Kong given the important role that Hong Kong plays as a global financial centre in Asia and a regional headquarters for many multi-nationals. An Australian seconded to Hong Kong could therefore be unfairly disadvantaged compared to his counterpart in Singapore.

Hong Kong's investment and trading ties with Australia

Hong Kong's relationship with Australia is somewhat unique. Hong Kong is home to over 100,000 Australian nationals and remains an important market for many Australian businesses operating throughout Asia. It is the leading financial centre in Asia and a key source of capital, being the second largest IPO market globally in 2020.[5] Hong Kong is also the regional headquarters for many multinational companies, including for many Australian businesses.

Australia and Hong Kong have had a longstanding trade and investment relationship. Hong Kong is Australia's seventh largest trading partner and fifth largest source of direct foreign investment.[6] For Australian businesses, Hong Kong's unique selling point is the key role it plays in accessing the mainland Chinese market. Hong Kong remains the gateway for capital to and from China for many Australian businesses and it is uniquely positioned to facilitate trade into mainland China due to its proximity and the stability of Hong Kong's legal and banking systems.

[5] https://www.ft.com/partnercontent/brandhongkong/hong-kong-ipo-market-resilience-and-innovation.html
[6] https://www.dfat.gov.au/geo/hong-kong/Pages/hong-kong-brief