


***CR 2005/54 - Income tax: assessable income:
Australian Federal Police employees - International
Deployment Group deployed to Nauru as Assisting
Australian Police***

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Class Ruling

Income tax: assessable income: Australian Federal Police employees – International Deployment Group deployed to Nauru as Assisting Australian Police

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Preamble

*The number, subject heading, **What this Class Ruling is about** (including **Tax law(s)**, **Class of persons** and **Qualifications** sections), **Date of effect**, **Arrangement** and **Ruling** parts of this document are a 'public ruling' in terms of Part IVA of the **Taxation Administration Act 1953**. CR 2001/1 explains Class Rulings and Taxation Rulings TR 92/1 and TR 97/16 together explain when a Ruling is a 'public ruling' and how it is binding on the Commissioner.*

What this Class Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax law(s)' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates.

Tax law(s)

2. The tax laws dealt with in this Ruling are section 23AG of the *Income Tax Assessment Act 1936* (ITAA 1936) and section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997).

Class of persons

3. The class of persons to which this Ruling applies are those persons deployed to Nauru as part of the International Deployment Group (IDG). They are:

- Australian Federal Police (AFP) officers;
- persons seconded to the AFP under section 69D of the *Australian Federal Police Act 1979* (AFP Act 1979) for the purposes of deployment as part of the IDG, for the period of their deployment; and
- persons appointed to the AFP as special members of the AFP under section 40E of the AFP Act 1979 for the purposes of deployment as part of the IDG, for the period of their deployment,

who are deployed to Nauru under the Agreement between Australia and Nauru Concerning Additional Police and Other Assistance to Nauru (the Agreement) and who remain Australian residents throughout the period of deployment.

4. The class of persons in paragraph 3 to whom this Ruling applies will be collectively referred to in this Ruling as AFP employees.

5. The class of persons includes AFP employees who while on deployment to Nauru return to Australia for a period during which they utilise leave that has wholly accrued from their service in Nauru.

6. The class of person does not include AFP employees who while on deployment to Nauru return to Australia for a period during which they utilise leave that has wholly or partly accrued from service in Australia or AFP employees whose term of deployment to Nauru is suspended before completing a continuous period of foreign service of not less than 91 days.

Qualifications

7. The Commissioner makes this Ruling based on the precise arrangement identified in this Ruling.

8. The class of persons defined in this Ruling may rely on its contents provided the arrangement actually carried out is carried out in accordance with the arrangement described in paragraphs 12 to 35.

9. If the arrangement actually carried out is materially different from the arrangement that is described in this Ruling, then:

- this Ruling has no binding effect on the Commissioner because the arrangement entered into is not the arrangement on which the Commissioner has ruled; and
- this Ruling may be withdrawn or modified.

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Date of effect

11. This Ruling applies from 1 July 2004. However, the Ruling does not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of the Ruling (see paragraphs 21 and 22 of Taxation Ruling TR 92/20). Furthermore, the Ruling only applies to the extent that:

- it is not later withdrawn by notice in the *Gazette*;
- it is not taken to be withdrawn by an inconsistent later Public Ruling; or
- the relevant tax laws are not amended.

Arrangement

12. The arrangement that is the subject of the Ruling is described below. This description is based on the following documents which are attached to the file record maintained by the Australian Taxation Office for this Ruling. These documents, or relevant parts of them, as the case may be, form part of and are to be read with this description. The relevant documents or parts of documents incorporated into this description of the arrangement are:

- Application for Class Ruling (dated January 2005) received 20 January 2005;
- Guide to Conditions of Employment – Determination 8 of 2004 (dated 29 October 2004 and provided by email dated 2 March 2005 and received on 2 March 2005);
- information provided by telephone by the applicant (dated 2 March 2005); and
- Copy of the Agreement between Australia and Nauru Concerning Additional Police and Other Assistance to Nauru (provided in a facsimile sent by the applicant received 20 January 2005).

13. AFP employees who are employees under the AFP Act 1979 seconded under section 69D or special members under section 40E will be deployed to Nauru under the Agreement between Australia and Nauru which was signed on 10 May 2004. As part of the Agreement, the Australian Government has decided to deploy AFP employees to Nauru. The deployment is integral to the Australian Government's effort to address core issues in Nauru in the areas of governance, law and order and justice and financial management.

14. Under the Agreement the Australian Government is providing AFP employees to the Nauru Police Service.

15. The periods of deployment of AFP employees in Nauru will be at least 91 days and usually for 60, 80 or 100 weeks.

16. For terms of deployment of 60 weeks the period of overseas duty will be three × 16 weeks of overseas service. For terms of deployment of 80 weeks the period of overseas duty will be four × 16 weeks of overseas service. For terms of deployment of 100 weeks the period of overseas duty will be five × 16 weeks of overseas service.

17. Deployments could also be extended for the period of the current Agreement.

18. Additional AFP employees may replace current deployed members under rotational arrangements.

19. Salary and other allowances will continue to be paid into the employee's nominated bank account on a fortnightly basis.

20. AFP employees will be a member of either the Commonwealth Superannuation Scheme or the Public Sector Superannuation Scheme or other approved superannuation scheme.

21. AFP employees will be entitled to the following allowances:

- Pre-deployment composite allowance;
- Deployment composite allowance paid during overseas posting and recreation leave periods taken during the term of overseas posting;
- Transfer allowance;
- Motor vehicle allowance during deployment;
- Extended unaccompanied overseas service allowance;
- Mission allowance;
- Telephone/communications allowance during the overseas posting; and
- Meals, accommodation and incidentals allowance.

22. During the period of deployment, AFP employees will accrue recreation leave entitlements as outlined in paragraphs 23 to 26.

23. For terms of deployment of 60 weeks, 12 weeks recreation leave will be accrued less nine days for additional training, briefing, debriefing and travel.

24. For terms of deployment of 80 weeks, 16 weeks recreation leave will be accrued less 12 days for additional training, briefing, debriefing and travel.

25. For terms of deployment of 100 weeks, 20 weeks recreation leave will be accrued less 15 days for additional training, briefing, debriefing and travel.

26. The general expectation is that AFP employees will be required to take recreation leave in blocks of four weeks, each block following a 16 week deployment. This may vary due to mission-specific requirements, however, employees will be provided with leave as outlined in paragraphs 23 to 25.

27. Recreation leave and mandatory recreation leave already accrued by an AFP employee prior to their deployment will be held over until their term of deployment ceases.

28. During the periods of leave following each posting, AFP employees will make themselves available for additional training, briefing and debriefing at the discretion of the National Manager of the IDG.

29. During the term of deployment, the leave entitlements referred to in paragraphs 23 to 26 replace the AFP employees entitlement to recreation leave and mandatory recreation leave prescribed under the AFP Certified Agreement 2003-2006 (Certified Agreement) except for AFP employees who do not complete six months of their deployment and terminate services voluntarily.

30. Where an AFP employee voluntarily terminates their term of deployment prior to the completion of six months, the employee is not entitled to the recreation leave referred to in paragraphs 23 to 26. The employee will then be entitled to recreation leave under the Certified Agreement.

31. The AFP employees are not allowed to take recreation leave and mandatory recreation leave accrued prior to the deployment until their term of deployment is completed.

32. Training, briefing and debriefing may be conducted in person, by telephone or any other communication method determined by the National Manager of the IDG.

33. The National Manager of the IDG may, upon request from an AFP employee, consider any special circumstances in respect of the employee (for example the death of a close family member) to determine whether to return the employee to their home base.

34. Employees may seek approval from the National Manager of the IDG to change, in blocks of 20 weeks only, a period of engagement provided they provide at least 24 weeks notice of their intention. However, employees on terms of deployment of 60, 80 or 100 weeks may not reduce their term of deployment below 60 weeks.

35. Article 11.4 of the Agreement provides that Designated Persons such as AFP employees deployed to Nauru, shall be exempt from taxation by the Government of Nauru on their pay and other emoluments.

Ruling

36. Subject to paragraph 37, the salary and allowances referred to in paragraphs 19 and 21 of this Ruling, derived by AFP employees described in paragraphs 3 to 6 of this Ruling deployed to Nauru are exempt from tax under section 23AG of the ITAA 1936 where:

- the employee has been engaged, or is taken to have been engaged, in service in Nauru for a continuous period of not less than 91 days; and
- the salary and allowances are derived from that foreign service, including payments for recreation leave that has wholly accrued from the period of service in Nauru.

37. The pre-deployment composite allowance and transfer allowance referred to in paragraph 21 are not exempt from tax under subsection 23AG(1) of the ITAA 1936.

Explanation

38. Subsection 6-5(2) of the ITAA 1997 provides that the assessable income of a resident taxpayer includes ordinary income derived directly or indirectly from all sources, whether in or out of Australia, during the income year.

39. Salary and wages are ordinary income for the purposes of subsection 6-5(2) of the ITAA 1997.

40. Subsection 6-15(2) of the ITAA 1997 provides that if an amount is exempt income then it is not assessable income.

41. Section 11-15 of the ITAA 1997 lists those provisions dealing with income which may be exempt. Included in this list is section 23AG of the ITAA 1936 which deals with exempt foreign employment income.

42. Section 23AG of the ITAA 1936 provides an exemption from Australian tax on the foreign earnings derived by an Australian resident who has been engaged in foreign service continuously for 91 days or more.

43. Subsection 23AG(1) of the ITAA 1936 states:

Where a resident, being a natural person, has been engaged in foreign service for a continuous period of not less than 91 days, any foreign earnings derived by the person from that foreign service is exempt from tax.

44. The basic tests for the exemption of foreign employment income in subsection 23AG(1) of the ITAA 1936 are:

- the taxpayer must be a 'resident of Australia';
- the taxpayer must be engaged in 'foreign service';

- the foreign service must be for a continuous period of not less than 91 days; and
- the taxpayer must derive 'foreign earnings' from that 'foreign service'.

However, certain foreign earnings that meet these tests may not be exempt from tax (see paragraphs 77 to 83).

Resident of Australia

45. The determination of a person's residency status depends on that person's circumstances and is a determination made in relation to each year of income. For further information see Taxation Ruling IT 2650. This Class Ruling only applies to the class of persons described in paragraph 3 of this Ruling who remain Australian residents for tax purposes during their deployment to Nauru.

46. This Ruling is based on the assumption that AFP employees deployed to Nauru will remain Australian residents for tax purposes throughout the period of their deployment.

Engaged in foreign service

47. 'Foreign service' is defined as 'service in a foreign country as the holder of an office or in the capacity of an employee' (subsection 23AG(7) of the ITAA 1936).

48. The term 'employee' is defined within subsection 23AG(7) of the ITAA 1936 to include 'a person employed by a government or an authority of a government or by an international organisation'.

49. AFP employees referred to in paragraph 3 of this Ruling are considered to meet the above definition of an 'employee'.

50. Deployment of AFP employees to Nauru constitutes 'foreign service' as each employee is undertaking 'service in a foreign country as a holder of an office or in the capacity of an employee'.

For a continuous period of not less than 91 days

51. Each AFP employee based in Nauru is expected to serve continuously in Nauru for a period of at least 91 days. These periods of 'foreign service', if met, satisfy the test that Australian residents working overseas must be engaged 'for a continuous period of not less than 91 days'.

52. Should an AFP employee depart Nauru prior to the completion of 91 days of continuous service, that employee will normally be ineligible for the exemption.

53. However, in certain instances, an employee who departs Nauru prior to serving the necessary number of days, may still qualify for exemption if they return to continue their posting at a later date (refer paragraphs 9 to 16 of Taxation Ruling TR 96/15).

Temporary absences

54. Subsection 23AG(6) of the ITAA 1936 and paragraph 11 of TR 96/15 treat certain temporary absences from foreign service as forming part of the period of foreign service.

55. This includes absences on recreation leave, other than:

- a. leave wholly or partly attributable to a period of service or employment other than the foreign service;
- b. long service leave, furlough, extended leave or leave of a similar kind (however described); or
- c. leave without pay or on reduced pay.

56. Where an AFP employee is temporarily absent from foreign service due to an absence on recreation leave defined in the previous paragraph, these absences will be taken to form part of the period of foreign service.

57. Where the overseas employment is performed under a cyclical arrangement, the whole of the work cycle (times on and off) are regarded as a continuous period of employment (Taxation Ruling IT 2441 and TR 96/15).

58. IT 2441 states that where a resident is employed in a foreign country, leave taken in circumstances similar to those mentioned in Taxation Ruling IT 2015 is treated as recreation leave that forms part of a period of foreign service under subsection 23AG(6) of the ITAA 1936. Subsection 23AG(6) states that the period of foreign service will include recreation leave other than long service leave or leave without pay or reduced pay and will not constitute a break in a period of foreign service.

59. IT 2015 refers to employees who are engaged in uninterrupted cycles of five weeks on site and five weeks leave in Australia, without any entitlement for additional annual leave and who are not required to attend company offices in Australia during leave periods.

60. TR 96/15 in referring to the recreation leave under subsection 23AG(6) of the ITAA 1936 considers extended leave not be part of the recreation leave. However, additional recreation leave entitlements granted to employees posted overseas are not extended leave where the additional leave is reasonable for example where it is granted due to the hardship involved in the postings resulting in the need for more rest and recreation.

61. The period of taking recreation leave in blocks of four weeks, each block following a 16 week deployment is granted to AFP employees replacing the recreation leave and mandatory recreation leave entitlements under the Certified Agreement and having regard to the arduous conditions under which they are deployed to Nauru. These include:

- exposed to personal risk;
- extreme hardship conditions; and
- inherent dangers and risks associated whilst performing duties in overseas jurisdictions.

Therefore, it is considered that the recreation leave granted is reasonable and is considered to be recreation leave under subsection 23AG(6) of the ITAA 1936 and would not be considered as extended leave as described under subparagraph 23AG(6)(a)(ii) of the ITAA 1936.

62. In respect of periods spent by AFP employees on visits to Australia as described in paragraphs 23 to 26 of this Ruling, these periods are temporary absences from duty authorised by the terms and conditions of the employee's foreign service and it is considered that the work arrangement is a cyclical arrangement as defined in IT 2441 and TR 96/15. Therefore, the entire period of the cyclical arrangement forms part of a continuous period of foreign service and is taken to form part of the employee's foreign service period. These absences will not break the continuity of eligible foreign service.

63. If an AFP employee who is in Australia as described in paragraphs 23 to 26 of this Ruling, extends their stay to take further recreational leave, that further recreation leave will not be taken to form part of the foreign service. As the normal leave accruals are replaced with the leave entitlements referred to in paragraphs 23 to 26 while on deployment, any further leave taken will not have accrued wholly from foreign service in Nauru.

64. It is considered that during the periods of leave following each posting, when AFP employees make themselves available for additional training, briefing and debriefing at the discretion of the National Manager of the IDG, should be treated as part of the person's continuous period of foreign service provided they are not excessive.

Temporary absences utilising leave entitlements from employment in Australia

65. As advised in paragraph 6 of this Ruling, AFP employees who take leave that accrued wholly or partly from employment in Australia are not part of the class of person to whom this Ruling applies.

66. In certain limited circumstances, an employee who is temporarily absent from Nauru while taking a period of leave that had accrued wholly or partly from employment in Australia may still meet the requirements of continuous service for exemption under section 23AG of the ITAA 1936. AFP employees who have or are planning to take leave using an entitlement that wholly or partially accrued from employment in Australia should seek professional advice from their taxation adviser or the Australian Taxation Office about the application of subsection 23AG(6D) of the ITAA 1936 to their circumstances.

Foreign earnings

67. The definition of 'foreign earnings' is contained in subsection 23AG(7) of the ITAA 1936, which provides that:

'foreign earnings' means income consisting of earnings, salary, wages, commission, bonuses or allowances but does not include any payment, consideration or amount that:

- (a) is included in assessable income under Subdivision AA of Division 2; or
- (b) is excluded from the definition of 'eligible termination payment' in subsection 27A(1) because of paragraph (ja), (k), (ka), (m), (ma), (n) or (p) of that definition.

68. The exclusions to the definition of 'foreign earnings' in paragraph 67 are not, however, relevant to this arrangement as they relate to pensions, annuities, eligible termination payments and other similar amounts.

69. The remuneration of posted AFP employees takes the form of an annual salary entitlement and the payment of various allowances (see paragraphs 19 and 21).

70. These salary and allowances are specifically included in the subsection 23AG(7) of the ITAA 1936 definition of 'foreign earnings'.

71. Whilst the salary of AFP employees may be paid into financial institutions in Australia, those 'earnings' are still considered 'foreign earnings'.

From that foreign service

72. To qualify for the exemption the 'foreign earnings' must be derived from the 'foreign service'. That does not mean that the foreign earnings need to be derived at the time of engaging in foreign service. The important test is that the foreign earnings, when derived, need to be derived as a result of the undertaking of that foreign service.

73. In the case of allowances paid after the taxpayer returns to Australia that relate to the period of foreign service, such allowances are treated as foreign earnings derived from that foreign service. Also, any advances paid to the taxpayer prior to the undertaking of foreign service against salary arising from the undertaking of that foreign service would be treated as foreign earnings from foreign service.

74. The salary that is paid when taking recreational leave that accrued during the period of foreign service is also considered to be foreign earnings from that service, even though the recreational leave may be taken after the completion of the foreign service.

75. An AFP employee is entitled to a composite allowance while undertaking pre-deployment training prior to engaging in foreign service. The composite allowance payable during the pre-deployment period is not derived from foreign service. It is derived as a result of the training taken prior to leaving Australia and does not, therefore, qualify for exemption under section 23AG of the ITAA 1936.

76. An AFP employee is also entitled to a transfer allowance prior to engaging in foreign service and after the completion of foreign service. The transfer allowance payable prior to the deployment period and after the end of the foreign service is not derived from that foreign service. It is paid as a compensation for non-reimbursed expenditure incurred by the AFP employee prior to engaging in foreign service and after completion of foreign service and does not, therefore, qualify for exemption under section 23AG of the ITAA 1936.

Certain foreign earnings not exempt

77. Subsection 23AG(2) of the ITAA 1936 provides that no exemption is available under subsection 23AG(1) of the ITAA 1936 in circumstances where an amount of foreign earnings derived in a foreign country is exempt from tax in the foreign country solely because of:

- a double tax agreement or a law of a country that gives effect to such an agreement (paragraphs 23AG(2)(a) and (b));
- a law of that foreign country which generally exempts from, or does not provide for, the imposition of income tax on income derived in the capacity of an employee, income from personal services or any other similar income (paragraphs 23AG(2)(c) and (d)); and
- a law or international agreement dealing with privileges and immunities of diplomats or consuls or of persons connected with international organisations (paragraphs 23AG(2)(e), (f) and (g)).

78. There is currently no double tax agreement between Australia and Nauru.

79. The privileges and immunities of persons connected with an international organisation do not apply to AFP employees working in Nauru.

80. The foreign earnings derived by AFP employees in Nauru are not subject to income tax as the law of Nauru does not provide for the imposition of income tax on any of the categories of income listed in paragraphs 19 and 21. Therefore, the income would not be exempt from tax under subsection 23AG(1) of the ITAA 1936 because paragraph 23AG(2)(d) of the ITAA 1936 applies.

81. Consequently, unless the income is also exempt from taxation in Nauru for another reason that is not listed in subsection 23AG(2) of the ITAA 1936, the income will not be exempt in Australia under the provisions of subsection 23AG(1) of the ITAA 1936.

82. The Agreement addresses taxation matters at Article 11.4. The Agreement includes a specific clause exempting income from taxation in Nauru.

83. As the foreign earnings of AFP employees are not exempt from tax in Nauru solely because of any of the reasons listed in subsection 23AG(2) of the ITAA 1936, subsection 23AG(2) will not deny the exemption under subsection 23AG(1) of the ITAA 1936.

Exemption with progression

84. The 'foreign earnings' of AFP employees that are exempt from Australian tax under section 23AG of the ITAA 1936 are nevertheless taken into account in calculating the Australian tax on other assessable income derived by the employee (subsection 23AG(3) of the ITAA 1936).

85. Tax on other assessable income will be calculated by applying to the non-exempt income (for example, Australian salary, investment income), the notional average rate of tax payable on the sum of exempt income and non-exempt income.

Example

86. *In the 2004-2005 income year, Daniel, an AFP employee derives the following types of income:*

- *Australian employment income of \$60,300;*
- *allowable deductions against Australian income of \$300;*
- *foreign exempt employment income of \$30,100; and*
- *expenses directly related to foreign exempt employment income of \$100.*

The foreign exempt employment income was earned from the deployment in Nauru of 16 weeks in mission and four weeks compensating recreational leave taken in Australia.

Assume that Daniel has appropriate private patient hospital cover for Medicare levy surcharge purposes.

The total amount of Australian tax payable will be calculated with reference to the following formula:

(Notional gross tax/Notional gross taxable income) × Other taxable income

Step 1

*Daniel's **notional gross taxable income** is \$90,000 ($[\$60,300 - \$300] + [\$30,100 - \$100]$).*

Step 2

*The **notional gross tax** is \$29,362 (the normal Australian income tax and Medicare levy payable on a taxable income of \$90,000).*

Step 3

*The **other taxable income** is \$60,000 (Australian employment income).*

Step 4

The Australian tax payable (including Medicare levy) on Daniel's Australian income is:

$$(\$29,362/\$90,000) \times \$60,000 = \$19,574.67$$

Detailed contents list

87. Below is a detailed contents list for this Class Ruling:

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Commissioner of Taxation

29 June 2005

<i>Previous draft:</i>	- ITAA 1936 23AG(2)(c)
Not previously issued as a draft	- ITAA 1936 23AG(2)(d)
	- ITAA 1936 23AG(2)(e)
<i>Related Rulings/Determinations:</i>	- ITAA 1936 23AG(2)(f)
CR 2001/1; TR 92/1; TR 92/20;	- ITAA 1936 23AG(2)(g)
TR 96/15; TR 97/16; IT 2015;	- ITAA 1936 23AG(3)
IT 2441; IT 2650	- ITAA 1936 23AG(6)
	- ITAA 1936 23AG(6)(a)(ii)
<i>Subject references:</i>	- ITAA 1936 23AG(6D)
- exempt foreign income	- ITAA 1936 23AG(7)
- exempt income	- ITAA 1936 Subdiv AA Div 2
- foreign exempt employment income	- ITAA 1936 27A(1)
- foreign income	- ITAA 1997 6-5
- foreign salary & wages	- ITAA 1997 6-5(2)
- foreign source income	- ITAA 1997 6-15(2)
- international tax	- ITAA 1997 11-15
- Nauru	- TAA 1953 Pt IVAAA
- overseas countries	- Copyright Act 1968
- overseas tax laws	- AFP Act 1979 40E
- residence of individuals	- AFP Act 1979 69D
	<i>Other references:</i>
<i>Legislative references:</i>	- The Agreement between Australia and Nauru Concerning Additional Police and Other Assistance to Nauru
- ITAA 1936 23AG	
- ITAA 1936 23AG(1)	
- ITAA 1936 23AG(2)	
- ITAA 1936 23AG(2)(a)	
- ITAA 1936 23AG(2)(b)	

ATO references

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