


CR 2008/71 - Income tax: assessable income: Australian Federal Police deployed to Timor-Leste

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Class Ruling

Income tax: assessable income: Australian Federal Police deployed to Timor-Leste

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1 This publication provides you with the following level of protection:

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provisions 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 entities

3. The class of entities to which this Ruling applies are:
- employees of the Australian Federal Police (AFP);

- 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 International Deployment Group (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 purpose of deployment as part of the IDG, for the period of their deployment,

who are deployed to Timor-Leste in accordance with the scheme described at paragraphs 11 to 59 of this Ruling. In this Ruling, these entities are referred to as AFP employees.

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

Qualifications

5. The Commissioner makes this Ruling based on the precise scheme identified in this Ruling.
6. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 11 to 59 of this Ruling.
7. If the scheme actually carried out is materially different from the scheme that is described in this Ruling, then:
- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled; and
 - this Ruling may be withdrawn or modified.
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Date of effect

9. This Ruling applies from 13 September 2007. However, this Ruling will 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 this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Previous Rulings

10. This Ruling replaces Class Rulings CR 2006/89 and CR 2006/108.

Scheme

11. The scheme 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 Tax 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 scheme are:

- Class Ruling applications dated 10 October 2005, 27 June 2006 and 12 December 2007;
- AFP Certified Agreement 2003-2006 (Certified Agreement);
- AFP International Deployment Group (IDG) – Determination No. 19 of 2005;
- AFP IDG – Determination No. 20 of 2005;
- AFP IDG – Determination No. 2 of 2006;
- Documentation supporting an arrangement dated 26 May 2006 between the Government of Timor-Leste and the Australian Government for visiting personnel (the Visiting Forces Arrangement);
- AFP Collective Agreement 2007-2011 (Collective Agreement);
- AFP IDG – Determination No. 16 of 2007;
- The Timor-Leste Police Development Program – Project Design Framework;

- Memorandum of Understanding between Government of Australia and the Government of the Republic de Timor Leste on technical cooperation for development (the TLPDP Arrangement);
- Agreement between United Nations and the Democratic Republic of Timor-Leste on the Status of the United Nations Integrated Mission in Timor-Leste (UNMIT Status Agreement); and
- Agreement between the Democratic Republic of East Timor and the United Nations concerning the Status of the United Nations Mission of Support in East Timor (SOMA) (UNMISSET Status Agreement).

Timor-Leste Police Development Program (TLPDP)

12. On 25 August 2003, the Australian Government announced a program of capacity building assistance for the law and justice sector of East Timor. This program is delivered jointly through the Australian Government's aid program (AusAID) and the Australian Federal Police is known as 'The Timor-Leste Police Development Program' (the program).

13. AFP employees posted to East Timor under the program are not afforded diplomatic status and will not be attached to a diplomatic mission.

14. Paragraph XI of the TLPDP Arrangement exempts Australian Project Personnel (including AFP employees deployed under the program) from taxation in East Timor on their emoluments.

Operation Serene

15. Under the Visiting Forces Arrangement, the Australian Government agreed to send AFP employees to provide assistance to Timor-Leste in the restoration of security, evacuation of foreign nationals as required, protect and support the United Nations Mission in Timor-Leste on request, and facilitate humanitarian assistance operations.

16. Clause 2 of Annex A to the Visiting Forces Arrangement grants visiting personnel, including AFP employees, status equivalent to that of administrative and technical staff under the *Vienna Convention on Diplomatic Relations of 18 April 1961* (the Convention). Clause 34 of the Convention provides an exemption from all dues and taxes, personal or real, national, regional or municipal, except certain taxes including dues and taxes on private income having its source in the receiving State (Timor-Leste) and capital taxes on investments made in commercial undertakings in the receiving State (Timor-Leste).

United Nations Integrated Mission in Timor-Leste (UNMIT)

17. AFP employees are also deployed to Timor-Leste under UNMIT. UNMIT was established in 2006 by United Nations Security Council resolution 1704. Its mission is to support the Government of Timor-Leste in its reconciliation efforts, to support the Timor-Leste electoral process, to assist with the restoration and maintenance of public security and to assist in further strengthening the Timorese national capacity for the monitoring, promotion and protection of human rights.

18. The UNMIT Status Agreement provides that the conditions of the UNMISSET Status Agreement (SOMA) will apply equally to members of the UNMIT mission. Paragraph 31 of the UNMISSET Status Agreement provides that the pay and emoluments received by UNMISSET members are exempt from taxation. As such members of UNMIT are also exempt from taxation in Timor-Leste under this arrangement.

19. Other persons may be seconded or appointed to the AFP for the purpose of deployment.

20. The remuneration for AFP employees takes the form of an annual salary entitlement and the payment of various allowances. Salary and allowances will continue to be paid into the employee's nominated account on a fortnightly basis.

21. AFP employees may be deployed in Timor-Leste under AFP – IDG Determination No. 19 of 2005, AFP – IDG Determination No. 20 of 2005, AFP – IDG Determination No. 2 of 2006 or AFP – IDG Determination No. 16 of 2007.

Determination No. 19 of 2005

22. For those AFP employees deployed under AFP – IDG Determination No. 19 of 2005, the period of deployment will be 40, 60, 80 or 100 weeks.

23. For terms of deployment of 40 weeks the period of overseas duty will be two x 16 weeks of overseas service. For terms of deployment of 60 weeks the period of overseas duty will be three x 16 weeks of overseas service. For terms of deployment of 80 weeks the period of overseas duty will be four x 16 weeks of overseas service. For terms of deployment of 100 weeks the period of overseas duty will be five x 16 weeks of overseas service.

24. AFP employees deployed to Timor-Leste will be entitled to some or all of the following allowances:

- composite allowance (paid during pre-deployment training);
- composite allowance (paid during posting and deployment accrued recreation leave);
- transfer allowance (to and from deployment);

- extended unaccompanied overseas service allowance;
- mission allowance;
- telephone/communications allowance;
- field accommodation allowance; and
- meals and accommodation allowances (if applicable) and incidental allowance.

25. Only the composite allowance will be paid while an AFP employee is on leave accrued during the deployment period.

26. During the period of deployment, AFP employees will accrue recreation leave as outlined in paragraphs 27 to 30 of this Ruling. Miscellaneous leave may also be granted for special circumstances (for example, death of a close family member).

27. For terms of deployment of 40 weeks, eight weeks recreation leave will be accrued less six days for additional training, briefing, debriefing and travel.

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

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

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

31. 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 27 to 30 of this Ruling.

32. Leave accrued by AFP employees prior to their deployment will be held over until their term of deployment ceases.

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

34. During the term of deployment, the leave entitlements referred to in paragraphs 27 to 30 of this Ruling replace the AFP employees entitlement to recreation leave and other leave prescribed under the relevant AFP Agreement.

35. However, where the 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 27 to 30 of this Ruling. The employee will then be entitled to recreation leave under the relevant AFP Agreement.

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

37. The AFP employee is entitled to no other leave whilst deployed. 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 on miscellaneous leave. In so doing, the deployment is suspended.

Determination No. 20 of 2005

38. For those AFP employees deployed under AFP – IDG Determination No. 20 of 2005, the period of deployment will be 12 months or more.

39. AFP employees posted to Timor-Leste will be entitled to some or all of the following allowances:

- composite overseas loading (paid during posting);
- transfer allowances (pre-departure);
- location allowance;
- extended overseas unaccompanied allowance;
- communication allowance;
- boarding allowance (if applicable);
- transfer allowance (repatriation); and
- travel allowance (if applicable).

40. Allowances will be paid while the AFP employee is on leave accrued during the deployment period.

41. The AFP employees posted to Timor-Leste under Determination No. 20 are entitled to the following types of leave as specified in the relevant AFP Agreement:

- standard recreation leave;
- mandatory rest days;
- personal leave;
- miscellaneous leave with/without pay;
- purchased recreation leave;
- maternity leave;
- adoption leave;
- compassionate leave;
- defence reserve service leave; and
- public service holidays / Christmas leave stand-down.

42. AFP employees accrue recreation leave on a monthly pro rata basis as per the relevant AFP Agreement. Recreation leave is credited to the employee on the first day of each month.

43. The employee's team leader may approve leave subject to operational requirements and the employee's leave balance. However, this would generally be restricted to leave accrued during deployment.

44. In addition to standard recreation leave AFP employees will accrue mandatory rest days as per the relevant AFP Agreement. Mandatory rest days must be taken in accordance with arrangements made with the employee's team leader, and must be taken during that quarter prior to the crediting of subsequent days.

Determination No. 2 of 2006

45. For those AFP employees deployed under AFP – IDG Determination No. 2 of 2006, the period of deployment will be short term between one day and six months.

46. AFP employees may receive some or all of the following allowances:

- composite allowance (paid during deployment);
- transfer allowance (to and from deployments of more than one month);
- mission allowance;
- meals and accommodation allowances (if applicable) and incidental allowance;
- communication allowance (if applicable); and
- field accommodation allowance.

47. Leave entitlements are in accordance with the relevant AFP Agreement described in paragraphs 41 to 44 of this Ruling, excluding purchased recreation leave, maternity leave and adoption leave.

48. Leave would generally not be approved during the Timor-Leste posting and additional rest periods may be granted to compensate for additional time worked.

Determination No. 16 of 2007

49. The length of each individual's deployment period is dependent on overseas operational requirements of individual missions. No standard period of deployment has been set and no standard pattern of duty applies.

50. No period of deployment may exceed 20 weeks without leave accrued in mission being applied and taken.

51. The Police Commissioner or his delegate may at any time terminate an appointee's period of deployment, and Mission Component service period. Once the appointee's period of deployment and or Mission Component service period is terminated, the Police Commissioner or his delegate may:

- direct that appointee to return to Australia;
- assign that appointee other IDG duties in Australia; or
- direct that the appointee may not perform Mission Component duties for a specified period.

52. Where an AFP appointee is deployed for more than 28 days, leave will accrue at the rate of seven days (one week) leave per 28 days (four weeks) overseas deployment.

53. Mission Component leave will not be granted in advance of accrual and must be utilised prior to other accrued recreation leave being applied and taken.

54. Determination No.16 of 2007 16 also allows the National Manager IDG (NMIDG) to approve miscellaneous or other personal leave, resulting in a suspension of the appointee's service period. Where an AFP appointee is granted a suspension, they cease to be deployed under Determination No. 16 of 2007 and revert to the relevant AFP Agreement (currently the AFP Collective Agreement).

55. An appointee may also be directed to stand down by NMIDG, the Mission Commander or the appointee's supervisor at any time during their deployment. If an appointee is stood down they must remain in mission and will still be entitled to their base salary, composite and other allowances payable under Determination No. 16 of 2007.

56. AFP employees are paid a salary according to the role undertaken while deployed.

57. AFP employees deployed under Determination No. 16 of 2007 will be entitled to some or all of the following allowances:

- composite allowance;
- notice to move (NTM) allowance;
- extended unaccompanied overseas service allowance (EUOSA);
- mission allowance;
- transfer allowance;
- telephone/communications allowance;
- meal and accommodation allowances (if applicable); and
- field accommodation allowance (if applicable).

58. Where an appointee's period of deployment is suspended for any of the following reasons (listed in section 16.1 of Determination No. 16 of 2007) their employment conditions will cease to be determined by that determination:

- operational or organisational reasons;
- health or welfare reasons;
- miscellaneous or other leave;
- professional standards reasons; or
- IDG management initiated disciplinary reasons.

59. Once repatriated, the appointee's conditions will be governed by the relevant AFP Agreement (currently the AFP Collective Agreement).

Ruling

60. The salary and allowances referred to in paragraphs 20, 24, 39, 46, 56 and 57 of this Ruling derived by the AFP employees described in paragraph 3 of this Ruling are ordinary income under section 6-5 of the ITAA 1997.

Exempt income

61. Subject to paragraph 67 of this Ruling, the salary and allowances referred to in paragraphs 20, 24, 39, 46, 56 and 57 of this Ruling, derived by AFP employees described in paragraph 3 of this Ruling deployed to Timor-Leste 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 Timor-Leste 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 Timor-Leste.

62. The Notice to Move allowance referred to in paragraph 57 of this Ruling is payable before, during and after deployment overseas. The Notice to Move allowance is exempt from tax under subsection 23AG(1) of the ITAA 1936 to the extent it is derived from foreign service. To the extent it is derived prior to engaging in foreign service, or following the completion of foreign service, it is not exempt from tax.

Assessable income

63. The salary and allowances derived by an AFP employee are included in their assessable income and are not exempt from tax under subsection 23AG(1) of the ITAA 1936 where:

- the employee has not been engaged in a continuous period of foreign service of not less than 91 days;
- it is not foreign earnings derived from that foreign service, as defined in subsection 23AG(7) of the ITAA 1936; or
- the employee had a change in circumstances and no longer satisfies the exemption conditions. The exemption will still apply for the period that the employee satisfied the exemption conditions.

64. The salary and composite allowance paid during pre-deployment training and transfer allowances referred to in paragraphs 20, 24, 39, 46, 56 and 57 of this Ruling are not exempt from tax under subsection 23AG(1) of the ITAA 1936.

Temporary absences form part of foreign service

65. An AFP employee is considered to be engaged in a continuous period of foreign service where:

- the AFP employee has a temporary absence from foreign service taken in accordance with the terms and conditions of that service because of accident or illness, or recreation leave wholly attributable to the period of foreign service (but not absences for long service leave, leave without pay or at reduced pay, furlough or extended leave, however described) (subsection 23AG(6) of the ITAA 1936 and paragraphs 9 to 11 of Taxation Ruling TR 96/15); or
- the AFP employee has two or more periods of foreign service that constitute a continuous period of foreign service (subsection 23AG(6A) of the ITAA 1936).

66. An AFP employee who takes leave other than that outlined at paragraph 65 of this Ruling will break their continuous period of foreign service.

Exemption with progression

67. The salary and allowances that are exempt from tax under paragraph 61 of this Ruling are still taken into account in calculating the Australian tax on other assessable income derived by the employee (subsection 23AG(3) of the ITAA 1936).

Example

68. In the 2007-2008 income year, Daniel, an 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 exempt foreign employment income of \$100.

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 \$24,450 (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:

$$(\$24,450/\$90,000) \times \$60,000 = \$16,300$$

Note: this calculation is based on the 2007-2008 income tax rates. If the income tax rates for future years change, you should refer to the tax rates for that current income year.

Appendix 1 – Explanation

❶ *This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.*

69. 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.

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

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

72. 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.

73. 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.

74. 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.

75. 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 114 to 121 of this Ruling).

Resident of Australia

76. 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 2650.¹ This Ruling only applies to the class of entities described in paragraph 3 of this Ruling who remain Australian residents for tax purposes during their deployment to Timor-Leste.

77. This Ruling is based on the assumption that AFP employees deployed to Timor-Leste are Australian residents for tax purposes throughout the period of their deployment.

Engaged in foreign service

78. '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).

79. 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'.

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

81. Deployment of AFP employees to Timor-Leste 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

82. Generally AFP employees based in Timor-Leste are expected to serve continuously 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 in foreign service 'for a continuous period of not less than 91 days'.

83. Should an AFP employee depart Timor-Leste prior to the completion of 91 days of continuous service, that employee will normally be ineligible for the exemption.

84. However, in certain instances, an AFP employee who departs Timor-Leste 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 96/15²).

¹ Income tax: residency – permanent place of abode outside Australia.

² Income tax: foreign tax credit system: issues relating to the practical application of section 23AG.

Temporary absences forming part of a period of foreign service

85. Subsection 23AG(6) of the ITAA 1936 treats certain temporary absences from foreign service as forming part of the period of foreign service. The Commissioner's view on the application of that subsection is reflected in paragraphs 9 to 11 of TR 96/15.

86. Absences which form part of the period of foreign service include absences taken in accordance with the terms and conditions of that service because of accident or illness, or recreation leave.

87. 'Recreation leave' is leave in the nature of paid holidays to which an employee has accrued an entitlement. Most usually it is the employee's accrued annual leave. Leave which fits this description is 'recreation leave', even if it is not called this.

88. However, 'recreation leave' does not include:

- leave that is not in the nature of paid holidays, such as weekends, rostered days off, flexidays, and days off in lieu;
- public holidays;
- leave wholly or partly attributable to a period of employment other than foreign service;
- long service leave, furlough, extended leave or similar leave; and
- leave without pay or on reduced pay.

89. During the period of deployment, AFP employees deployed under Determination No. 19 of 2005 will accrue four weeks recreation leave (less days for additional training, briefing, debriefing and travel) after each 16 week deployment block.

90. During the period of deployment, AFP employees deployed under Determination No. 2 of 2006 will accrue:

- 240 hours standard recreation leave per annum on a monthly pro-rata basis. Recreation leave is credited to the employee on the first day of each month; and
- mandatory recreation leave of a further five days per annum on the basis of one day for two months worked.

91. During the period of deployment, AFP employees deployed under Determination No. 20 of 2005 will accrue:

- 228 hours standard recreation leave per annum monthly on a pro-rata basis; and
- Four mandatory rest days per year (one per quarter).

92. Where an AFP employee is deployed for more than 28 days under Determination No. 16 of 2007 leave will accrue at the rate of seven days (one week) leave for 28 days (four weeks) overseas deployment.

93. Given the nature of the overseas deployment, it is considered that the recreation leave in paragraphs 89 to 92 of this Ruling granted to AFP employees deployed to Timor-Leste is reasonable. This recreation leave is wholly attributable to the period of foreign service and forms part of a continuous period of foreign service for the purposes of subsection 23AG(1) of the ITAA 1936.

94. Where an AFP employee purchases recreation leave, the employee's base salary is adjusted by the amount of the leave purchased and they will receive a reduced fortnightly salary. This leave is not recreation leave as it is not in the nature of paid holidays to which an employee has accrued an entitlement, but rather is leave on reduced pay (see paragraphs 87 and 88 of this Ruling). The AFP employee needs to consider the discussion at paragraph 98 of this Ruling to determine whether the continuity of foreign service can be maintained.

95. An AFP employee's period of continuous foreign service will be maintained where the AFP employee is granted:

- personal leave relating to their sickness or accident; or
- miscellaneous leave with pay or personal leave because of the accident, illness or death of another person where the leave is for a short period.

Temporary absences not breaking the period of foreign service: the one-sixth administrative test

96. In certain limited circumstances, breaks other than those specified in paragraph 86 of this Ruling are also taken to form part of a period of foreign service. Such breaks include weekends, public holidays, rostered days off, and days off in lieu, where such breaks are authorised by the terms and conditions of the deployment. However, where such breaks are used to return to Australia they must not be excessive. Where the break is excessive the period of foreign service will still not be broken if continuity of the foreign service period can be maintained by application of the rules outlined in paragraph 98 of this Ruling.

97. Breaks taken to visit or return to Australia are considered excessive when the total of such breaks are more than one-sixth of the period of scheduled foreign service or, if the period of foreign service is ongoing, more than one-sixth of the income year. This one-sixth administrative test is different to the 1/6 legislative rule covered in paragraphs 100 to 102 of this Ruling.

Temporary absences not breaking foreign service period: the legislative rule

98. Where an AFP employee takes leave other than the leave outlined at:

- paragraphs at 89 to 92 and 95 of this Ruling; or

- paragraph 96 of this Ruling that is not excessive, they need to determine whether the continuity of foreign service can be maintained (subsection 23AG(6A) of the ITAA 1936).

99. Paragraphs 100 to 102 of this Ruling provide an explanation of this tax provision. Alternatively, the AFP employee could seek professional advice from their taxation adviser or the Tax Office.

Continuity of the period of foreign service – 1/6 legislative rule

100. The 1/6 legislative rule allows two or more continuous periods of foreign service to be joined as a total period of foreign service, unless, at any time, the total period of absence (in days) from foreign service between the continuous periods of foreign service exceeds 1/6 of the number of days of the total period of foreign service.

101. If the period of absence exceeds 1/6 of the total period of foreign service at any time, continuity of foreign service is broken. The AFP employee will begin a new period of foreign service when he or she next engages in foreign service and must determine whether that period of foreign service lasts for at least 91 continuous days (subsection 23AG(6A) of the ITAA 1936).

102. The 1/6 legislative rule should not be confused with the one-sixth administrative test outlined at paragraphs 96 and 97 of this Ruling. The 1/6 legislative rule in subsection 23AG(6A) of the ITAA 1936 permits two or more periods of foreign service to constitute a continuous period of foreign service where continuity would be otherwise broken by absence. Absences between the periods of foreign service under the 1/6 legislative rule do not form part of the continuous period of foreign service. In contrast, the one-sixth rule is an administrative test which permits what would otherwise be a break in the foreign service to be included in a continuous period of foreign service.

Foreign earnings

103. 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, or of amounts included in a person's assessable income under Subdivision 13A, but does not include any payment, consideration or amount that:

- (a) is included in assessable income under Division 82 or Subdivision 83-295 or Division 301, 302, 304 or 305 of the *Income Tax Assessment Act 1997*; or
- (b) is included in assessable income under Division 82 of the *Income Tax (Transitional Provisions) Act 1997*; or
- (c) is mentioned in paragraph 82-135(e), (f), (g), (i) or (j) of the *Income Tax Assessment Act 1997*; or

- (d) is an amount transferred to a fund, if the amount is included in the assessable income of the fund under section 295-200 of the *Income Tax Assessment Act 1997*.

104. However, the exclusions to the definition of 'foreign earnings' in paragraph 103 of this Ruling are not relevant to this arrangement as they relate to pensions, annuities, employment termination payments and other similar amounts.

105. The remuneration of deployed AFP employees takes the form of an annual salary entitlement and the payment of various allowances.

106. These salary and allowances which are described in paragraphs 20, 24, 39, 46, 56 and 57 of this Ruling come within the definition of 'foreign earnings' in subsection 23AG(7) of the ITAA 1936.

107. 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

108. 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.

109. 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 against salary or allowances paid to the taxpayer prior to the undertaking of foreign service arising from the undertaking of that foreign service would be treated as foreign earnings from foreign service.

110. 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 recreation leave may be taken after the completion of the foreign service.

111. The receipt of the following allowances by AFP employees:

- composite allowance/composite overseas loading paid during posting and deployment accrued recreation leave;
- extended unaccompanied overseas service allowance/extended overseas unaccompanied allowance;
- mission allowance;
- telephone/communication allowance;

- field accommodation allowance;
- meals and accommodation allowances (if applicable) and incidental allowance;
- notice to move (NTM) allowance (derived during deployment);
- location allowance (if applicable);
- boarding allowance (if applicable); and
- travel allowance (if applicable),

are considered to be exempt as they are derived from that foreign service in Timor-Leste. However, to the extent that the NTM allowance is derived either prior to engaging in foreign service, or following the completion of foreign service, it is not exempt because it is not derived from that foreign service.

112. AFP employees may also be entitled to transfer allowances. Transfer allowances paid are not derived from that foreign service in Timor-Leste. They are paid as compensation for non-reimbursed expenditure incurred by the AFP employee prior to engaging in foreign service or after completion of foreign service and therefore, do not qualify for exemption under section 23AG of the ITAA 1936.

113. 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 undertaken prior to leaving Australia and does not, therefore, qualify for exemption under section 23AG of the ITAA 1936.

Certain foreign earnings not exempt

114. 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)).

115. Australia has not entered into a tax treaty with Timor-Leste and the laws of Timor-Leste provide for the imposition of income tax.

116. Timor-Leste law does not provide a general exemption from income tax.

117. The TLPDP Arrangement between the Government of Australia and the Government of Timor-Leste, which exempts the emoluments of Australian TLPDP personnel from taxation in Timor-Leste, is not an international agreement that is legally binding at international law. Whilst AFP employees deployed under the TLPDP Arrangement receive privileges and immunities, they do not receive diplomatic or consular privileges and immunities under an international agreement.

118. The Visiting Forces Arrangement relating to operation Serene between the Government of Timor-Leste and Government of Australia concerning the status of visiting AFP personnel provides that such personnel will be accorded the status equivalent to that of administrative and technical staff under the *Vienna Convention of Diplomatic Relations of 18 April 1961*. As such the Arrangement provides an exemption from tax in Timor-Leste on the salary and allowances of the deployed AFP employees.

119. However the Visiting Forces Arrangement is not an international agreement that is legally binding at international law. Whilst the AFP employees deployed under the Visiting Forces Arrangement receive privileges and immunities, they do not receive diplomatic or consular privileges and immunities under an international agreement.

120. The UNMISSET Status Agreement governing the status of UNMIT deployees exempts the pay and emoluments of employees deployed as part of UNMIT from taxation in Timor-Leste. Although the agreement provides privileges and immunities to persons connected with the UN, Australia is not a party to the Status agreement and, as such, AFP employees deployed to UNMIT are not provided with privileges and immunities connected with an international organisation through an international agreement to which Australia is a party.

121. As a result, the foreign earnings of the deployed AFP employees are exempt from tax in Timor-Leste for a reason other than those listed in subsection 23AG(2) of the ITAA 1936. Therefore, subsection 23AG(2) of the ITAA 1936 will not operate to deny the 'foreign earnings' exemption under subsection 23AG(1) of the ITAA 1936.

Exemption with progression

122. 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).

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

124. In calculating these amounts, any deductions that relate to the exempt income are allowed as if the exempt income was assessable income. That is, expenses which relate directly to earning income in Timor-Leste are deductible from exempt income.

Appendix 2 – Detailed contents list

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 96/15; IT 2650; TR 2006/10

Previous Rulings/Determinations:

CR 2006/89; CR 2006/108

Subject references:

- exempt income
- foreign income
- foreign salary & wages
- foreign source income
- international tax
- overseas countries
- overseas employees
- overseas tax laws
- residence of individuals
- Timor-Leste

Legislative references:

- ITAA 1936 23AG
- ITAA 1936 23AG(1)
- ITAA 1936 23AG(2)
- ITAA 1936 23AG(2)(a)
- ITAA 1936 23AG(2)(b)
- ITAA 1936 23AG(2)(c)
- ITAA 1936 23AG(2)(d)
- ITAA 1936 23AG(2)(e)
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- Income Tax (Transitional Provisions) Act 1997 Div 82
- TAA 1953
- Copyright Act 1968
- AFP Act 1979 40E
- AFP Act 1979 69D

Other references:

- Vienna Convention of Diplomatic Relations of 18 April 1961
- AFP(IDG) Determination No. 19 of 2005
- AFP (IDG) Determination No. 20 of 2005
- AFP (IDG) Determination No. 2 of 2006
- AFP (IDG) Determination No. 16 of 2007
- Arrangement dated 26 May 2006 between the Democratic Republic of Timor-Leste and the Australian Government for visiting personnel
- Agreement between United Nations and the Democratic Republic of Timor-Leste on the Status of the United Nations Integrated Mission in Timor-Leste
- Agreement between the Democratic Republic of East Timor and the United Nations concerning the Status of the United Nations Mission of Support in East Timor

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