# *IT 2222 - Income tax : exempt income : whether contributions under the United States Federal Insurance Contribution Act are an income tax*

# TAXATION RULING NO. IT 2222

INCOME TAX : EXEMPT INCOME : WHETHER CONTRIBUTIONS UNDER THE UNITED STATES FEDERAL INSURANCE CONTRIBUTION ACT ARE AN INCOME TAX

F.O.I. EMBARGO: May be released

REF
H.O. REF: 83/13532 DATE OF EFFECT: Immediate

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F.O.I. INDEX DETAIL

| REFERENCE NO: | SUBJECT REFS: | LEGISLAT. REFS: |
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| I 1194252 | | |
| | EXEMPT INCOME | 23(q) |
| | CONTRIBUTIONS UNDER THE UNITED STATES FEDERAL INSURANCE CONTRIBUTION ACT | INCOME TAX (INTERNATIONAL AGREEMENTS) ACT SCHEDULE 2 ARTICLE XIII OF 1953 CONVENTION |

PREAMBLE

In a recent decision handed down by Taxation Board of Review No. 3, the issue was whether teaching income derived by a university lecturer from sources in the United States of America and subject to U.S. federal insurance contributions was exempt from income tax under paragraph 23(q) of the Income Tax Assessment Act. The decision has been reported as Case S52 85 ATC 388 and Case 58 28 CTBR(NS) 414.

FACTS

2. During the period 1 September 1975 to 30 June 1976 the taxpayer, a resident of Australia, was engaged as a visiting professor at two American universities deriving income from research and teaching activities. The research component of the taxpayer's salary was subject to U.S. federal income tax while the teaching component was exempt from federal income tax by virtue of Article XIII of the Australia/U.S.A. Double Taxation Convention (1953)(the "1953 Convention"). Article XIII of the 1953 Convention only exempted from U.S. federal income tax, income derived from teaching by professors and teachers who were residents of Australia and temporarily present in the United States for a period not exceeding two years for the purpose of teaching at a university, college, school or other educational institution.

3. The taxpayer also had deducted from his whole salary amounts charged under the Federal Insurance Contributions Act (FICA). It was adduced in evidence before the Board that the FICA, which is legislated as part of the U.S. Internal Revenue Code, is a means of financing social security benefits. FICA contributions are deducted from salary and calculated according to the statutory formula provided by the Code. For the calendar

year ended 31 December 1975, the contribution was 5.85% of salary up to $US 14,000, and for 1976, 5.85% of salary up to $US 15,300. The prescribed amount is deducted by the employer from each instalment of salary. An equivalent amount is levied on the employer and may be claimed as a business expense by the employer.

4. The question for decision by the Board was whether the FICA contribution was an income tax for the purposes of paragraph 23(q). Dr Gerber, who delivered the principal reasons for the Board's decision, first considered whether the FICA was an income tax according to U.S. revenue law. Accepting the technical evidence adduced on behalf of the taxpayer, Dr Gerber concluded that it was not an income tax for the purposes of the internal laws of the United States. As a consequence, it was held that the taxpayer was not exempt under the 1953 Convention from having to make FICA contributions.

5. Having determined that the FICA was not an income tax under American law, Dr Gerber then considered whether it was an income tax for Australian law purposes. In so doing, Dr Gerber referred to the judgment of Fullagar J., in Mutual Life and Citizens Assurance Company Limited v FCT (1959) 100 CLR 537 at p. 553, and said that it was possible for an impost not called an income tax in the United States to nonetheless be regarded as an income tax for the purposes of paragraph 23(q).

6. Dr Gerber observed that schemes similar to the FICA were known in Australia and drew an analogy with the Social Services Contribution Assessment Act (No. 39 of 1945) and the Social Services Contribution Act (No. 40 of 1945), which were later repealed and became the Income Tax and Social Services Contribution Assessment Act (No. 48 of 1950) and the Income Tax and Social Services Contribution Act (No. 49 of 1950). Although referred to as "Social Services Contribution" Dr Gerber considered that it constituted an income tax for the purposes of paragraph 23(q).

7. Applied to the present case, and having regard to those factors referred to at paragraph 3 (above), Dr Gerber concluded that contributions under the FICA constituted an income tax for Australian law purposes. Even though the FICA is limited to only part of salary, Dr Gerber considered that it was deemed to be a tax on the whole of the amount. ("If you impose tax on a proportion a/b of x, you are taxing x"; per Fullagar J., Mutual Life and Citizens Assurance Co. Case (supra) at p. 550). Accordingly, because the taxpayer was liable for payment of income tax in the United States the teaching income derived by him was exempt from Australian tax under paragraph 23(q).

RULING

8. The decision of the Board has been accepted and is to be applied in similar cases where, prior to 31 October 1983, taxpayers have derived income from sources in the United States and part of that income has been subjected to contributions under the FICA.

9. With the replacement of the 1953 Convention, by a new United States convention which entered into force on 31 October 1983, there is no longer any provision in the Convention comparable with Article XIII of the 1953 Convention.

COMMISSIONER OF TAXATION
28 November 1985