



CR 2004/37 - Income Tax: Assessability of income: Bougainville Transition Team

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Class Ruling

Income Tax: Assessability of income: Bougainville Transition Team

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Preamble

*The number, subject heading, and the **What this Class Ruling is about** (including **Tax law(s)**, **Class of persons** and **Qualifications** sections), **Date of effect**, **Withdrawal**, **Arrangement** and **Ruling** parts of this document are a ‘public ruling’ in terms of Part IVAAA 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 sections 6-5, 6-10, 6-15 and 11-15 of the *Income Tax Assessment Act 1997* (ITAA 1997) and section 23AG of the *Income Tax Assessment Act 1936* (ITAA 1936).

Class of persons

3. The class of persons to which this Ruling applies is the Australian Government employees who were deployed to the Bougainville Transition Team (BTT) and are Australian residents for income tax purposes.

Qualifications

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

5. 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 below at paragraphs 10 to 20 in this Ruling.

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

- 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- this Ruling may be withdrawn or modified.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

8. This Ruling applies from 1 July 2003. However, the Ruling does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Ruling (see paragraphs 21 to 22 of Taxation Ruling TR 92/20). Furthermore, the Ruling only applies to the extent that:

- It is not later withdrawn by Gazette;
- It is not taken to be withdrawn by an inconsistent later public ruling; or
- The relevant tax laws are not amended.

Withdrawal

9. This Class Ruling is withdrawn and ceases to have effect after 30 June 2004. The Ruling continues to apply, in respect of the tax law ruled upon, to all persons within the specified arrangement during the term of the Ruling. Thus, the Ruling continues to apply to those

persons, even following its withdrawal, for arrangements entered into prior to the withdrawal of the Ruling. This is subject to there being no change in the arrangement or in the persons' involvement in the arrangement.

Arrangement

10. The arrangement that is the subject of the Ruling is described below. This description is based on the following documents. 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 3 October 2003;
- National Interest Analysis: Category B Treaty, Summary Page;
- Protocol, signed at Sydney on 30 June 2003, ((2003) ATNIF 13); and
- Further information provided by the applicant.

Mission

11. BTT was a small civilian team created to continue the work undertaken by the Peace Monitoring Group and its predecessor, the Truce Monitoring Group, in promoting, facilitating and instilling confidence in the peace process on Bougainville Province and in the transition towards autonomous government.

12. Members of BTT included Australians who are employees of the Australian Public Service, seconded to and paid by the Australian Agency for International Development (AusAID).

13. The persons referred to in paragraph 12 are Australian residents for income tax purposes.

Period of deployment

14. The first BTT members entered Bougainville on 1 July 2003 and worked for a period greater than 91 days.

15. The last of the employees returned to Australia early in January 2004.

Allowances and Conditions

16. Salary and other remuneration entitlements were paid to the deployed employees on a fortnightly basis.
17. BTT members were also entitled to a 'per diem' allowance of \$145 per day, paid in accordance with the AusAID Determination 1999/2 Overseas Conditions of Service Manual – Determination 2003 (the Determination) subclauses 6.1.15(1) and 6.1.15(2).
18. BTT members on a six month assignment received 5 days Hardship Leave that could not be accrued.
19. The Hardship Leave had to be taken along with 5 days recreation leave, approximately 3 months into their assignment.
20. This leave was in accordance with the Determination in subclauses 6.1.15(3), 6.1.15(4) and 6.1.15(5).

Taxation

21. Foreign earnings are exempt from taxation in Papua New Guinea because of the *Agreement between Australia, Papua New Guinea, New Zealand, Fiji and Vanuatu concerning the Neutral Truce Monitoring Group for Bougainville (Bougainville Agreement)*.

Ruling

22. Section 23AG of the ITAA 1936 provides an exemption from Australian Income Tax on the foreign earnings derived by an Australian resident who has been engaged in foreign service for a continuous period of not less than 91 days.
23. The exempt income from that foreign service is, however taken into account when calculating the Australian tax payable on the assessable income of the taxpayer.
24. The salary and allowances referred to in paragraph 16 and 17 of this ruling, derived by the class of persons referred to in paragraph 3 of this ruling from their foreign service in Bougainville are exempt from tax under section 23AG where:
 - Those employees were engaged in service in Bougainville for a continuous period of not less than 91 days; and
 - None of the conditions set out in subsection 23AG(2) are satisfied.

Explanation

25. 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.
26. Salary and wages are ordinary income for the purposes of subsection 6-5(2) of the ITAA 1997.
27. Subsection 6-15(2) of the ITAA 1997 provides that if an amount is exempt income then it is not assessable income.
28. 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 overseas employment income.
29. Section 23AG of the ITAA 1936 provides an exemption from Australian tax on the foreign earnings derived an Australian resident who has been engaged in foreign service continuously for 91 days or more.
30. Subsection 23AG(1) 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.
31. The basic test for the exemption of foreign employment income in subsection 23AG(1) are, the taxpayer must:
- be a ‘resident of Australia’;
 - be engaged in ‘foreign service’;
 - be engaged for a continuous period of not less than 91 days; and
 - derive ‘foreign earnings’ from that ‘foreign service’.

Resident of Australia

32. 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 Income Tax Ruling IT 2650. It is expected that persons who were deployed to Bougainville as a member of BTT remained residents of Australia throughout the period of their deployment.

Engaged in Foreign Service

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

34. Service in Bougainville is considered to have its source in Papua New Guinea; therefore BTT members were undertaking *'service in a foreign country'*.

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

36. Employees of the BTT are considered to meet the above definition of *'employee'*.

For a continuous period of not less than 91 days

37. Each BTT member in Bougainville was expected to serve continuously for a period of at least 91 days. Therefore, these periods of 'foreign service' meet the test that Australian residents working overseas must be engaged *'for a continuous period of not less than 91 days'*. If a BTT member departed Bougainville prior to the completion of 91 days of continuous service, that person would normally be ineligible for the exemption.

38. However, in certain instances, a BTT member who departed Bougainville 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).

Derived foreign earnings

39. The definition of 'foreign earnings' is contained in subsection 23AG(7), 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.

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

41. The remuneration of posted BTT members takes the form of a continuation of an annual salary entitlement and the payment of a daily 'per diem' allowance.

42. Salary and allowances are specifically included in the subsection 23AG(7) definition of 'foreign earnings'.

43. Whilst the salaries of BTT members were paid into Australian financial institutions in Australia, those 'earnings' were still considered 'foreign earnings'. Subsection 23AG(1) provides an implicit connection between 'foreign earnings' and 'foreign service', that is, '*any foreign earnings derived by the person from that foreign service is exempt from tax*' (emphasis added). The direct linkage of earnings to service negates the need to consider any potential 'source' issues, even though the source of remuneration under a normal contract of employment is generally regarded as the place where the duties are performed (*FC of T v. French* (1957) 98 CLR 398).

From that foreign service

44. 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.

45. In the case of allowances paid after the person 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.

Certain foreign earnings not exempt

46. Subsection 23AG(2) provides that no exemption is available under subsection 23AG(1) 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)).

47. The Papua New Guinea income tax status of members of the BTT is covered by the Bougainville Agreement. Paragraph 1 of Article 17 of the Bougainville Agreement provides that Australian residents are exempt from tax in Papua New Guinea on pay and emoluments received from Australia. As such, the taxpayer's salary and wages income is exempt from tax in Papua New Guinea.

48. The Agreement is not one which falls within paragraph 23AG(2)(f) of the ITAA 1936 as an international agreement dealing with privileges and immunities of diplomatic or consuls or of persons connected with international organisations. BTT is not considered an 'international organisation', nor was it set up under an international organisation, such as the United Nations. The Agreement is not caught by any of the other reasons listed in subsection 23AG(2) of the ITAA 1936.

Double Tax Agreement between Papua New Guinea (PNG) and Australia

49. Under paragraph 23AG(2)(b) of the ITAA 1936 where income is exempt in the foreign country as a result of the operation of a double tax agreement, that income is not exempt.

50. In determining liability to Australian tax on foreign sourced income it is necessary to consider not only the income tax laws but also any applicable double tax agreement contained in the *International Tax Agreements Act 1953* (the Agreements Act).

51. Section 4 of the Agreements Act incorporates that Act with the ITAA 1936 and ITAA 1997 so that those Acts are read as one. The Agreements Act effectively overrides the ITAA 1936 and ITAA 1997 where there are inconsistent provisions (except for some limited provisions).

52. Schedule 29 to the Agreements Act contains the double tax agreement between Australia and PNG (the PNG Agreement). The PNG Agreement operates to avoid the double taxation of income received by Australian and PNG residents.

53. Article 15(1) of the PNG Agreement provides that salary and wages income of an Australian resident will be taxable only in Australia unless the employment is exercised in PNG. If the employment is exercised in PNG then PNG may also tax the income unless the taxpayer is present in PNG on a temporary visit.

54. Temporary visits are dealt with in Article 15(2) of the PNG Agreement which provides that remuneration derived by a resident of Australia in respect of employment exercised in PNG shall be taxable only in Australia if:

- the taxpayer is present in PNG for a period or periods not exceeding in the aggregate 90 days in the PNG year of income;
- the remuneration is paid by, or on behalf of, an employer who is not a resident of PNG;
- the remuneration is not deductible in determining the taxable profits of a permanent establishment or fixed base that the employer has in PNG; and
- the remuneration is subject to tax in Australia.

55. However, where a BTT member has been present in PNG for a period in excess of 90 days in the PNG year of income, Article 15(2) of the PNG Agreement will not apply. Therefore, although the BTT member's income is subject to tax in Australia, it may also be subject to tax in the PNG under Article 15 of the PNG Agreement.

56. The BTT member's income is however exempt from tax in PNG under the 'Bougainville Agreement' between Australia and PNG. The exemption provided by the Agreement does not fit within any of the other categories excluding exemption under subsection 23AG(2) of the ITAA 1936.

Other relevant information

57. The 'foreign earnings' of members of BTT that are exempt from Australian tax under section 23AG are nevertheless taken into account in calculating the Australian tax on other assessable income derived by the employee.

58. Tax on other assessable income is calculated by applying to the non-exempt income (e.g. Australian salary, investment income), the notional average rate of tax payable on the sum of exempt income and non-exempt income.

Example

59. In the 2003 – 2004 income year a BTT member derived the following types of income:

- Australian employment income after deductions of \$45,000; and
- Overseas employment income after deductions of \$15,000.

The total amount of Australian tax payable on the member's income is calculated with reference to the following formula:

$(\text{Notional gross tax} / \text{Notional gross taxable income}) \times \text{Other taxable income}$

Step 1

The member's notional gross taxable income is \$60,000
(\$45,000 + \$15,000)

Step 2

The notional gross tax is \$16,032 (the normal Australian income tax and Medicare levy payable on a taxable income of \$60,000 - this does not include Medicare levy surcharge as the member has appropriate private patient hospital cover).

Step 3

The other taxable income is \$45,000 (Australian employment income)

Step 4

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

$(\$16,032 / \$60,000) \times \$45,000 = \$12,024.00$

Detailed contents list

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Commissioner of Taxation

7 April 2004

<i>Previous draft:</i>	- ITAA 1936 23AG
Not previously issued as a draft	- ITAA 1936 23AG(1)
	- ITAA 1936 23AG(2)
<i>Related Rulings/Determinations:</i>	- ITAA 1936 23AG(2)(a)
CR 2001/1; TR 97/16; TR 96/15;	- ITAA 1936 23AG(2)(b)
TR 92/20; TR 92/1; IT 2650	- ITAA 1936 23AG(2)(c)
	- ITAA 1936 23AG(2)(d)
	- ITAA 1936 23AG(2)(e)
<i>Subject references:</i>	- ITAA 1936 23AG(2)(f)
- exempt foreign income	- ITAA 1936 23AG(2)(g)
	- ITAA 1936 23AG(7)
<i>Legislative references:</i>	- ITAA 1936 Subdiv AA Div 2
- ITAA 1997 6-5	- ITAA 1936 27A(1)
- ITAA 1997 6-5(2)	- TAA 1953 Pt IVAAA
- ITAA 1997 6-10	- Copyright Act 1968
- ITAA 1997 6-15	- International Tax Agreements Act 1953
- ITAA 1997 6-15(2)	- International Tax Agreements Act 1953 4
- ITAA 1997 11-15	

- International Tax Agreements Act
1953 Sch 29

Case references:

- *FC of T v. French* (1957) 98 CLR
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Other references:

- Agreement between Australia,
Papua New Guinea, New Zealand,
Fiji and Vanuatu concerning the
Neutral Truce Monitoring Group for
Bougainville

ATO references

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