



CR 2004/75 - Income tax: exempt foreign employment income: section 23AG: New South Wales Department of Education and Training employees deployed to the Democratic Republic of Timor-Leste (East Timor)

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 This document has changed over time. This is a consolidated version of the ruling which was published on *1 January 2003*



Class Ruling

Income tax: exempt foreign employment income: section 23AG: New South Wales Department of Education and Training employees deployed to the Democratic Republic of Timor–Leste (East Timor)

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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**, **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 law dealt with in this Ruling is section 23AG of the *Income Tax Assessment Act 1936* (ITAA 1936).

Class of persons

3. The class of persons to which this Ruling applies are employees of the New South Wales Department of Education and Training (DET employees) who are residents of Australia for tax purposes and are deployed to the Democratic Republic of Timor-Leste (referred to in this Ruling as Timor-Leste, also known as East Timor).

4. The class of person includes DET employees who while on deployment to Timor-Leste return to Australia for a period during which they utilise leave that has wholly accrued from their service in Timor-Leste.

5. The class of person does not include DET 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.

Qualifications

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

7. 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 11 to 18 in this Ruling.

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

- (a) 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
- (b) this Ruling may be withdrawn or modified.

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Date of effect

10. This Ruling applies from 1 January 2003. 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

11. 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 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 arrangement are:

- application dated 15 January 2004; and
- further information provided by the applicant.

12. As part of the Commonwealth and NSW Governments' commitment to supporting Timor-Leste, DET employees will be deployed to Timor-Leste to assist in the re-building of education and training programs for that country.

13. DET employees deployed to Timor-Leste will be senior managers and suitably qualified experienced teachers who preferably have a fluency in Bahasa Indonesian, standard Portuguese or Tetum.

14. Most DET employees will be deployed for a period of 6 to 12 months. Some employees may extend their period of deployment. In limited circumstances, a shorter period of deployment may be offered. All deployments will be for a period of at least 91 days.

15. Salary entitlements will continue to be paid on a fortnightly basis to DET employees during deployment.

16. DET employees deployed to Timor-Leste will also be entitled to an allowance of up to \$2,500 per month for accommodation and living expenses. The allowance may be increased in line with cost of living increases.

17. Each employee is entitled to return to Australia on 3 occasions during the period of deployment. While DET does not specify the number of days a DET employee may spend in Australia, the duration is based upon the number of days needed to report and perform other employment activities, including the purchase of required supplies. DET will meet the cost of one return fare to Sydney and two return fares to Darwin for this purpose.

18. The visits are also required for recreation purposes, in recognition of the hardships endured in Timor-Leste. It is expected that most DET employees will only utilise recreation leave that has wholly accrued from service in Timor-Leste. Subject to operational needs, DET employees may be able to utilise leave that accrued wholly or partly from employment in Australia.

Ruling

19. The salary and allowances referred to in paragraphs 15 and 16 of this ruling, derived by a DET employee described in paragraphs 3 and 4 of this ruling deployed to Timor-Leste, are exempt from tax under section 23AG 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.

Explanation

20. Subsection 6-5(2) of the *Income Tax Assessment Act* (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.

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

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

23. 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.

24. 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.

25. 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.'

26. The basic tests for the exemption of foreign employment income in subsection 23AG(1) 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 50 to 53).

Resident of Australia

27. 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. This Class Ruling only applies to the class of persons described in paragraphs 3 and 4 of this ruling who remain Australian residents for tax purposes during their deployment to Timor-Leste.

28. This ruling is based on the assumption that DET employees deployed to Timor-Leste will remain residents of Australia for tax purposes throughout the period of their deployment.

Engaged in foreign service

29. '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)).

30. 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'.

31. DET employees referred to in paragraph 3 of this ruling are considered to meet the above definition of an 'employee'.

32. Deployment of a DET employee 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

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

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

35. However, in certain instances, an 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 96/15).

Temporary Absences

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

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

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

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

39. In respect of periods spent by DET employees on visits to Australia as described in paragraph 17 of this ruling, these periods are temporary absences from duty authorised by the terms and conditions of the employee's foreign service and are taken to form part of the employee's foreign service period. As such, these absences will not break the continuity of eligible foreign service.

40. If a DET employee who is in Australia as described in paragraph 17 of this ruling, extends their stay to take recreational leave that accrued wholly from foreign service in Timor-Leste, that period of leave is taken to form part of the employee's foreign service.

Temporary Absences utilising leave entitlements from employment in Australia

41. As advised in paragraph 5 of this ruling, DET 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.

42. In certain limited circumstances, an employee who is temporarily absent from Timor-Leste 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. DET 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 s23AD(6D) to their circumstances.

Foreign earnings

43. 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.'

44. 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.

45. The remuneration of posted DET employees takes the form of an annual salary entitlement and the payment of an accommodation and living expenses allowance.

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

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

From that foreign service

48. 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.

49. 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

50. 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)).

51. There is currently no double tax agreement between Australia and Timor-Leste.

52. The privileges and immunities of persons connected with an international organisation do not apply to DET employees working in Timor-Leste.

53. The foreign earnings derived by DET employees in Timor-Leste are not exempt, under a general provision from income tax in Timor-Leste.

Exemption with progression

54. The 'foreign earnings' of DET employees 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 (subsection 23AG(3)).

55. 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

56. In the 2003 - 2004 income year, Daniel, a DET employee 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 Daniel's income will be calculated with reference to the following formula:

$$\frac{\text{Notional gross tax}}{\text{Notional gross taxable income}} \times \text{Other taxable income}$$

Step 1

Daniel'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 Daniel 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 Daniel's Australian income is:

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

Detailed contents list

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Commissioner of Taxation

21 July 2004

<i>Previous draft:</i>	- ITAA 1936 23AG(2)
Not previously released in draft form	- ITAA 1936 23AG(2)(a)
	- ITAA 1936 23AG(2)(b)
	- ITAA 1936 23AG(2)(c)
<i>Related Rulings/Determinations:</i>	- ITAA 1936 23AG(2)(d)
CR 2001/1; IT 2650; TR 92/1;	- ITAA 1936 23AG(2)(e)
TR 92/20; TR 96/15; TR 97/16;	- ITAA 1936 23AG(2)(f)
	- ITAA 1936 23AG(2)(g)
<i>Subject references:</i>	- ITAA 1936 23AG(3)
- Timor-Leste	- ITAA 1936 23AG(6)
- foreign exempt employment income	- ITAA 1936 23AG(6D)
- foreign income	- ITAA 1936 23AG(7)
- foreign salary & wages	- ITAA 1936 Part III Div 2
- foreign source income	Subdiv AA
- international tax	- ITAA 1936 27A(1)
- overseas countries	- ITAA 1936 27A(1)(ja)
- overseas tax laws	- ITAA 1936 27A(1)(k)
- residence of individuals	- ITAA 1936 27A(1)(ka)
	- ITAA 1936 27A(1)(m)
	- ITAA 1936 27A(1)(ma)
<i>Legislative references:</i>	- ITAA 1936 27A(1)(n)
- ITAA 1936 23AG	- ITAA 1936 27A(1)(p)
- ITAA 1936 23AG(1)	

- ITAA 1997 6-5(2)
 - ITAA 1997 6-15(2)
 - ITAA 1997 11-15
 - TAA 1953 Pt IVAAA
- Copyright Act 1968
-

ATO references

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