CR 2006/15 - Income tax: assessable income: Australian Agency for International Development employees - deployed to Indonesia as Development Program specialists under the Australia - Indonesia Partnership for Reconstruction and Development

This ruling contains references to repealed provisions, some of which may have been re-enacted or remade. The ruling has effect in relation to the re-enacted or remade provisions. Paragraph 32 in TR 2006/10 provides further guidance on the status and binding effect of public rulings where the law has been repealed or repealed and rewritten.
Australia's tax treaties and other agreements except for the Taipei Agreement are set out in the Australian Treaty Series. The citation for each is in a note to the applicable defined term in sections 3AAA or 3AAB of the International Tax Agreements Act 1953.

Class Ruling

Income tax: assessable income: Australian Agency for International Development employees – deployed to Indonesia as Development Program specialists under the Australia – Indonesia Partnership for Reconstruction and Development

Contents Para

This Ruling provides you with the following level of protection:

This publication (excluding appendices) 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, we must apply the law to you in the way set out in the ruling (or in a way that is more favourable for you if we are satisfied that the ruling is incorrect and disadvantages you, and we are not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any under-paid 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 taxation provision(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant taxation provision(s)

2. The relevant taxation 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). Changes to section 23AG of the ITAA 1936 came into effect on 19 December 2005. The Commissioner's interpretation on the treatment of absences in respect of section 23AG of the ITAA 1936 prior to the latest amendments is contained in Taxation Ruling TR 96/15.

Class of entities

3. The class of entities to which this Ruling applies are Australian Public Service (APS) employees of Australian Agency for International Development (AusAID) deployed to Indonesia as Development Program Specialists as part of the Australia – Indonesia Partnership for Reconstruction and Development program. The deployment is under the General Agreement on Development Co-operation between the Government of Australia and the Government of the Republic of Indonesia.

4. AusAID employees remain Australian residents throughout the period of deployment.

5. AusAID employees include employees who while on deployment to Indonesia return to Australia for a period during which they utilise leave that has wholly accrued from their service in Indonesia.

6. The class of entities does not include AusAID employees who while on deployment to Indonesia return to Australia for a period during which they utilise leave that has wholly or partly accrued from service in Australia.

Qualifications

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

8. 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 12 to 23 of this Ruling.

9. 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.

Date of effect

11. This Ruling applies from 1 April 2005. 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*; or
- the relevant taxation provisions are not amended.

Scheme

12. 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 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 scheme are:

- Application for Class Ruling (dated 14 May 2005) received 21 June 2005;
- Letters of Offer dated 7 June 2005;
- Conditions of Employment;
- AusAID Code of Conduct for Overseas Service; and
- General Agreement on Development Co-operation between the Government of Australia and the Government of the Republic of Indonesia 9 July 1998 (the Government Treaty).

13. AusAID employees will be deployed to Indonesia as Development Program Specialists as part of the Australia – Indonesia Partnership for Reconstruction and Development program under the Government Treaty.

14. The period of deployment is for an initial period of 12 months. However, deployments may be extended beyond the initial 12 month period.

15. It is anticipated that the AusAID employees will return to Australia to reside on a permanent basis on completion of their deployment, after which they will continue to remain employees of AusAID in Australia.

16. AusAID employees will be members of either the Commonwealth Superannuation Scheme or the Public Sector Superannuation scheme.

17. The remuneration for AusAID 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.

18. AusAID employees are entitled to the following allowances:

- transfer allowance paid in two instalments (one prior to deployment and one on completion of deployment);
- cost of living allowance;
- cost of posting allowance;
- hardship allowance;
- child allowances;
- special location allowance;
- household maintenance allowance;
- additional household allowance.

19. Allowances will be paid while an AusAID employee is on leave accrued during the deployment period.

20. AusAID employees will accrue 20 days of recreation leave per year. They will also accrue personal and long service leave while deployed in Indonesia. In addition, AusAID employees will receive 10 days additional recreation leave per annum or pro-rata for part year of deployment.

21. Leave will be approved subject to operational requirements and with approval from line management. The Conditions of Employment require that AusAID employees take recreation leave from the locality at a minimum of every six months.

22. It is expected that only recreation leave accrued while on deployment will be taken by AusAID employees. If an employee chooses to return to Australia on recreation leave they would not be expected or required to perform any work related duties in Australia.

23. Article XI of the Government Treaty provides that the income tax liability of Australian personnel, including AusAID employees deployed to Indonesia, shall be borne by the Government of the Republic of Indonesia.

Ruling

24. Subject to paragraph 25 of this Ruling, the salary and allowances referred to in paragraphs 17 and 18 of this Ruling, derived by AusAID employees described in paragraphs 3 to 5 of this Ruling deployed to Indonesia 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 Indonesia 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 Indonesia.

25. The pre-deployment and post-deployment transfer allowance referred to in paragraph 18 of this Ruling is not exempt from tax under subsection 23AG(1) of the ITAA 1936.

Example

26. In the 2004-2005 income year, Daniel, an AusAID 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 $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) × $60,000 = $19,574.67

Commissioner of Taxation
22 March 2006

Appendix 1 – Explanation

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.

27. 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.

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

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

30. 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.

31. 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.

32. 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.

33. 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 64 to 71 of this Ruling).

Resident of Australia

34. 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 Ruling only applies to the class of entities described in paragraphs 3 to 5 of this Ruling who remain Australian residents for tax purposes during their deployment to Indonesia.

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

Engaged in foreign service

36. '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).

37. 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'.

38. AusAID employees referred to in paragraphs 3 to 5 of this Ruling are considered to meet the above definition of an 'employee'.

39. Deployment of AusAID employees to Indonesia 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

40. Each AusAID employee based in Indonesia is expected to serve continuously in Indonesia 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'.

41. Should an AusAID employee depart Indonesia prior to the completion of 91 days of continuous service, that employee will normally be ineligible for the exemption.

42. However, in certain instances, an employee who departs Indonesia 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 forming part of a period of foreign service

43. 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.

44. Absences which form part of the period of foreign service include absences taken in accordance with the terms and conditions of employment because of accident or illness or 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.

45. A period in which an employee is absent on extended leave (see paragraph 44(b) of this Ruling) is not a period of 'foreign service' for the purposes of subsection 23AG(1) of the ITAA 1936. Additional recreation leave entitlements granted to employees posted overseas will not be considered to constitute extended leave where the additional leave is reasonable.

46. The Conditions of Employment grant the deployed AusAID employees 10 days additional recreation leave per annum or pro-rata for part year of deployment.

47. Given the nature of the overseas deployment, it is considered that the additional recreation leave granted to AusAID employees deployed in Indonesia is reasonable. Therefore, the period of additional recreation leave will form part of a continuous period of 'foreign service' for the purposes of subsection 23AG(1) of the ITAA 1936.

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

48. In certain limited circumstances, breaks other than those specified in paragraph 44 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 of such, 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 50 of this Ruling.

49. 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 51 to 53 of this Ruling.

Temporary absences not breaking the period of foreign service: the legislative rules

50. In determining whether the continuity of foreign service can be maintained, the AusAID employee should consider the application of:

- the former subsections 23AG(6A) to 23AG(6E) of the ITAA 1936 if the break occurs prior to 19 December 2005. The Commissioner's view on the application of those subsections is reflected in paragraphs 14 to 16 and the accompanying examples in paragraphs 30 and 31 of TR 96/15, and the examples in paragraphs 31A and 31B of the addendum to TR 96/15; or
- subsection 23AG(6A) of the ITAA 1936 if the break occurs on or after 19 December 2005. Paragraphs 51 to 53 of this Ruling provide an explanation of this tax provision.

Alternatively, the AusAID employee could seek professional advice from their taxation adviser or the Australian Taxation Office.

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

51. 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.

52. 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 AusAID 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 (subsections 23AG(6A) of the ITAA 1936).

53. The 1/6 legislative rule should not be confused with the one-sixth administrative test outlined at paragraphs 48 and 49 of this Ruling. The 1/6 legislative rule in subsection 23AG(6A) 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

54. 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 Division 13A, 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.

55. The exclusions to the definition of 'foreign earnings' in paragraph 54 of this Ruling are not, however, relevant to this scheme as they relate to pensions, annuities, eligible termination payments and other similar amounts.

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

57. These salary and allowances which are described in paragraphs 17 and 18 of this Ruling, with the exception of the transfer allowance come within the definition of 'foreign earnings' in subsection 23AG(7) of the ITAA 1936.

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

From that foreign service

59. 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.

60. 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.

61. The receipt of the following allowances:

- cost of living allowance;
- cost of posting allowance;
- hardship allowance;

- child allowances;
- special location allowance;
- household maintenance allowance; and
- additional household allowance,

are considered to be foreign earnings from the foreign service as they relate to engaging in foreign service in Indonesia.

62. 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.

63. An AusAID 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 foreign earnings derived from that foreign service. It is paid as a compensation for non-reimbursed expenditure incurred by the AusAID 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

64. 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)).

65. Australia has entered into a tax treaty with Indonesia (the Indonesian Agreement) which is contained in Schedule 37 of the *International Tax Agreements Act 1953* (the Agreements Act).

66. Article 19(1) of the Indonesian Agreement provides that remuneration paid by Australia to any individual in respect of services rendered in the discharge of governmental functions shall be taxable only in Australia. However, such remuneration will be taxable only in Indonesia if the services are rendered in Indonesia and the individual is a resident and citizen of Indonesia, or did not become a resident of Indonesia solely for the purpose of performing the services.

67. Paragraph 69 of Taxation Ruling TR 2005/8 provides that the term 'services rendered in the discharge of governmental functions' means those services rendered by an employee or office holder in the completion of *any* functions undertaken by government.

68. For the period of deployment, the AusAID employees remain Australian residents and receive remuneration, in the form of salary and allowances, from the Australian Government. This remuneration will be received in respect of services rendered as Development Program Specialists as part of the Australia – Indonesia Partnership for Reconstruction and Development program in the discharge of governmental functions.

69. Therefore, under article 19(1) of the Indonesian Agreement the income received by the AusAID employees while deployed in Indonesia is taxable only in Australia and, as such, will not be subject to taxation in Indonesia.

70. However, article 19(1) of the Indonesian Agreement is not the only reason why the AusAID employees' income will not be subject to tax in Indonesia. Article XI of the Government Treaty provides that the income tax liability of Australian personnel, including AusAID employees deployed to Indonesia, shall be borne by the Government of the Republic of Indonesia. This effectively exempts the AusAID employees from paying Indonesian income tax on salaries and allowances derived while deployed in Indonesia.

71. As a result, the foreign earnings of the deployed AusAID employees are not exempt from tax in Indonesia solely because of any of the reasons listed in subsection 23AG(2) of the ITAA 1936. Therefore, subsection 23AG(2) will not operate to deny the 'foreign earnings' exemption under subsection 23AG(1) of the ITAA 1936.

Exemption with progression

72. The 'foreign earnings' of AusAID 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).

73. 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.

74. 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 Indonesia are deductible from exempt income.

Appendix 2 – Detailed contents list

75. The following is a detailed contents list for this Ruling:

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 92/20; TR 96/15; TR 2005/8; IT 2650

Subject references:

- exempt foreign income
- exempt income
- foreign exempt employment income
- foreign income
- foreign income deductions
- foreign salary & wages
- foreign source income
- international tax
- Indonesia
- overseas countries
- overseas employees
- overseas tax laws
- residence of individuals

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)
- ITAA 1936 23AG(2)(f)
- ITAA 1936 23AG(2)(g)
- ITAA 1936 23AG(3)
- ITAA 1936 23AG(6)
- ITAA 1936 23AG(6A)
- ITAA 1936 23AG(6E)
- ITAA 1936 23AG(7)
- ITAA 1936 Pt III Div 2 Subdiv AA
- ITAA 1936 27A(1)
- ITAA 1936 Pt III Div 13A
- ITAA 1997 6-5
- ITAA 1997 6-5(2)
- ITAA 1997 6-15(2)
- ITAA 1997 11-15
- TAA 1953
- Copyright Act 1968
- International Tax Agreements Act 1953 Sch 37

Other references:

- General Agreement on Development Co-operation between the Government of Australia and the Government of Indonesia, 9 July 1998

ATO references

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