Taxation Administration Act 1953 Individuals engaged in foreign service – Legislative instrument

Explanatory Statement

General Outline of Instrument

1. The pay as you go withholding system allows many taxpayers to make provision for their income tax liabilities by requiring payers to withhold amounts from certain income payments, including payments made to individuals employed in a foreign country or countries.
2. This instrument is made by the Commissioner of Taxation (the Commissioner) pursuant to section 15-15 of Schedule 1 to the *Taxation Administration Act 1953*.
3. This is a legislative instrument for the purposes of the *Legislative Instruments Act 2003*.

Date of effect

4. The instrument applies from the day after it is registered on the Federal Register of Legislative Instruments.

What is this instrument about?

5. This instrument ensures the withholding from payments made to individuals employed in a foreign country or countries closely approximates the Australian income tax that will be payable on the relevant income.
6. This instrument is necessary due to amendments to Section 23AG of the *Income Tax Assessment Act 1936*, effective from 1 July 2009.

What is the effect of this Instrument?

7. The effect of this instrument is to ensure that amounts withheld from payments made to individuals engaged in foreign service under the Pay as you go withholding system for Australian taxation purposes are calculated with consideration to the amount of tax that is required to be withheld for the relevant payment period and paid to the foreign country for that service.
8. The instrument requires payers to reduce the Australian dollar equivalent of the amount that would normally be withheld in Australia

under the relevant Pay as you go withholding tax table by the Australian dollar equivalent of the amount of tax to be withheld and paid to the foreign country.

9. Without this instrument, tax withheld for affected employees could be too high unless they choose to apply individually for a variation to consider their entitlement to a foreign income tax offset.

10. The information in this instrument will be used by Australian payers, professional advisers, software developers and the Australian Taxation Office.

11. An assessment of the compliance cost impact indicates that the impact will be low for implementation and no change in on-going compliance costs. The instrument is routine in nature.

Background

12. The *Taxation Administration Act 1953* empowers the Commissioner to make withholding schedules specifying the amounts, formulas and procedures to be used for working out the amount required to be withheld by an entity from certain categories of payment, including payments made to employees that are engaged in a foreign country or countries.

13. The *Taxation Administration Act 1953* further empowers the Commissioner to vary the rate of withholding specified in the schedules to meet the special circumstances of a particular case or class of cases.

14. The Commissioner uses these powers to ensure that amounts withheld, in most cases, closely approximate the amount of income tax which will ultimately be payable on the relevant income.

15. In the 2009-10 Budget, the Government announced changes to the exemption rules for foreign employment income derived by Australian residents who are engaged in foreign service for a continuous period of 91 days or more.

16. The *Tax Laws Amendment (2009 Budget Measures No. 1) Act 2009* provides that, from 1 July 2009, income derived from foreign service is exempt from income tax only when directly attributable to any of the following:

    (a) the delivery of Australian official development assistance by the person's employer;
    (b) the activities of the person's employer in operating a public fund covered by item 9.1.1 or 9.1.2 of the table in subsection 30-80(1) of the *Income Tax Assessment Act 1997* (international affairs deductible gift recipients);
    (c) the activities of the person's employer, if the employer is exempt from income tax because of paragraph 50-50(c) or (d) of the *Income Tax Assessment Act 1997* (prescribed institutions located or pursuing objectives outside Australia);
    (d) the person's deployment outside Australia as a member of a disciplined force by:
        (i) the Commonwealth, a State or a Territory;

(ii) an authority of the Commonwealth, a State or a Territory or

(e) an activity of a kind specified in the regulations.

17. The changes remove the income tax exemption for income that would have been otherwise exempt prior to 1 July 2009, meaning that income will need to be included in individual tax returns. Affected taxpayers may be entitled to a foreign income tax offset for amounts of foreign tax paid.
18. This instrument acts to ensure that the amount required to be withheld in these circumstances better matches the amount of income tax which will be payable on the relevant income.

Consultation

19. The power to vary amounts required to be withheld is a routine part of tax administration.
20. The Tax Office will provide the necessary information and advice to affected payers and software providers during the transition period.

Example

Norman is an Australian resident that has been sent to work in Papua New Guinea for 4 months from July 2009. He is to be paid K3,850 weekly by his Australian employer. The tax system in Papua New Guinea requires that K462 is withheld and paid for the individual’s tax purposes (12% is the applicable rate to foreign contractors).

Norman has claimed the tax-free threshold with respect to his Australian employment but is not eligible for any tax offsets, nor does he have a Higher Education Loan Program or Student Financial Supplement Scheme debt. Norman is not entitled to leave loading.

Assume for the purposes of this example, the exchange rate that applies for converting Papua New Guinean Kina to Australian Dollars for the purposes of this example is 2.36.

1. Convert the earnings in K to AU$:

   K3,850 / 2.36 = $1,631.36

2. Calculate the Australian amount to be withheld from amount calculated at 1. in accordance with the relevant Pay as you go withholding tax table (NAT 1004):

   Amount to be withheld from $1,631.99 = $404

3. Reduce the amount calculated at 2. by the amount to be withheld and paid to the foreign country:

Amount to be withheld and paid to foreign country = K462
Convert this amount to AU$ = K462/2.36
= $195.76

Amount to be withheld = $404 – $195.76 = $208.24
Rounded to the nearest dollar = **$208**

The amount to be withheld for Australian Pay as you go withholding purposes from the payment of K3,850 is AU$208.

Erin Holland
Deputy Commissioner of Taxation
10 July 2009

Legislative references:
Taxation Administration Act 1953
Legislative Instruments Act 2003
Income Tax Assessment Act 1936
Income Tax Assessment Act 1997
Tax Laws Amendment (2009 Budget Measures No. 1) Act 2009