

POST-IMPLEMENTATION REVIEW: LIMITING TAX CONCESSIONS FOR AUSTRALIANS WORKING OVERSEAS

The measure was announced in the 2009-10 Budget and was part of a package of measures to improve the fairness and integrity of the tax system. Broadly the measure significantly narrowed the scope of an existing income tax exemption for the foreign service income of Australians working overseas in certain circumstances. In essence, the exemption would now only apply with respect to foreign service related to development, aid, defence and related activities. The exemption is contained in section 23AG of the Income Tax Assessment Act 1936.

In developing the policy, the Department of the Treasury self-assessed the proposal as having a minor impact on business and/or the not-for-profit sector, in accordance with the Best Practice Regulation requirements that applied at the time. However, as a RIS exemption for this proposal was provided by the then Prime Minister, a PIR is required. As the impacts of this policy have not been significant, the Department of the Treasury offers you the following assessment as our PIR.

Problem

Prior to the implementation of this amendment certain foreign employment income earned by Australians working overseas for a continuous period of 91 days or more was exempt from Australian income tax. The original intent of section 23AG was to relieve double taxation. However, in practice, little foreign tax may have actually been paid on the foreign income concerned. This was inconsistent with the principle that Australians are taxed on their worldwide income and created inequitable treatment between those Australian residents working overseas who were eligible for the exemption and those that were not (a distinction that had no economic justification).

Objectives

The objective of the measure was to limit the application of an income tax exemption that no longer served its original policy intent, resulted in the inequitable treatment of Australian taxpayers and potentially led to double non-taxation (contrary to Australian tax principles).

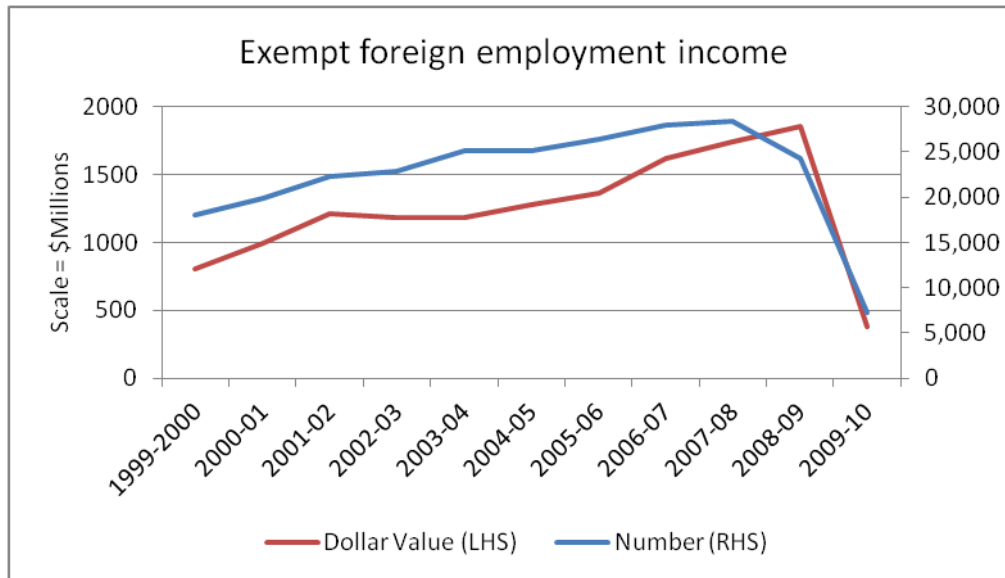
To the extent that any double taxation might arise, this was better addressed through the Foreign Income Tax Offset (FITO) regime which allows an Australian taxpayer to offset tax paid overseas (with respect to foreign income) against their Australian tax liability. In addition, the abolition of the exemption was expected to remove significant compliance costs then incurred by taxpayers seeking to utilise the exemption as well as costs incurred by the ATO in administering the provisions (the existing provisions gave rise to a number of ruling requests seeking clarification as to its operation).

Impact analysis

Overall the changes resulted in little compliance impact on taxpayers. Whilst the changes did result in increased compliance costs in some areas these should be considered in the context of a significant decrease in compliance cost in other areas.

The removal of the exemption has resulted in more companies with staff overseas needing to apply Australia's PAYG (Withholding) regime with respect to the foreign source income of their employees. In addition, individuals now need to apply Australia's FITO regime to ensure that they receive a credit for foreign income tax paid. With respect to the remaining class of persons eligible for the exemption in section 23AG, there has also been an increased demand for private rulings from the ATO on whether the new (narrower) class of exemptions applies to an individual's circumstances.

However, given the uncertainty under the previous regime as to whether the exemption applied to an individual's circumstances, and the significant number of applications for private rulings that were made, the substantial narrowing of the class of persons now eligible for the exemption is expected to have also significantly decreased the overall compliance burden on taxpayers. An analysis of taxation statistics (up until 2009-10) confirms that the 2009-10 income year saw a decrease in number (69%) and value (80%) of relevant claims.



Consultation

In addition to public consultation on exposure draft legislation, the measure underwent extensive public consultation as part of a Senate Economics Committee review of the Tax Laws Amendment (2009 Budget Measures No. 1) Bill 2009 (which contained the changes to 23AG). The Committee handed down its report on 22 June 2009.

The Committee received submissions from a range of stakeholders, including affected individuals, Australian companies operating overseas as well as peak and other representative bodies writing on behalf of their members/clients. Principally the submissions raised concerns with respect to the effective increase of tax liabilities for staff working overseas. This would, it was argued, impact on the competitiveness of Australian firms operating internationally. In relation to the compliance impacts on business, the need for companies to comply with PAYG (Withholding) obligations, for payroll staff to understand foreign tax laws and for individuals to apply the FITO regimes with respect to their personal tax arrangements were raised.

Following the implementation of the measure, discussions with the Australian Taxation Office have confirmed the overall reduction in applications for private rulings with respect to the exemptions in section 23AG.

Conclusion

The measure is meeting its original policy intent of removing an unwarranted tax exemption and providing equity in the treatment of taxpayers. Although the imposition of taxation on amounts that were previously exempt has necessarily led to additional compliance costs for some affected taxpayers (in the same way that the imposition of any taxation brings with it compliance costs), the reduction in the number of taxpayers eligible for the exemption has reduced the need for taxpayers

to determine their eligibility for the exemption (including the need to apply for private rulings from the ATO).