[Insert DD Month YYYY]

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[Insert Client Name]

[Insert Client Position]

[Insert Company Name]

[Insert Client Address]

[Suburb State Post Code]

Dear [Insert Client Name]

**Re:** **Foreign employment income**

This letter outlines some of the key issues relating to foreign employment income derived by an individual who is regarded as a resident of Australia for tax purposes during the year in which those earnings were derived.

Accordingly, it is critical to determine if an individual rendering such services will be regarded as a resident, as defined under section 6(1) of the *Income Tax Assessment Act* *1936* (**ITAA 1936**). The commentary below does not apply to a person who is regarded as a non-resident for Australian tax purposes.

**Executive Summary**

1. From 1 July 2016, only resident employees of certain non-Government, charitable organisations or the disciplined force of an Australian Government or authority will be exempt from Australian income tax on foreign earnings, where that person is engaged in foreign service for a continuous period of at least 91 days.
2. All other Australian resident employees are subject to tax in Australia on their foreign employment income. These resident employees may be entitled to a foreign income tax offset which can be applied to reduce or extinguish their Australian liability on such income.

**Exempt foreign earnings**

From 1 July 2016, an Australian resident individual engaged in foreign service will only be exempt on their foreign earnings under section 23AG of the ITAA 1936, where all of the following conditions are met:

* the individual was engaged in performing foreign service as an employee or office holder in a foreign country for a continuous period of at least 91 days,
* the individual’s service must be directly attributable to:
  + the delivery of Australian official development assistance by an employer (other than an Australian Government agency),
  + the activities of the individual’s employer in operating a developing country relief fund or a public disaster recovery fund in a developing country,
  + the activities of certain registered charities located in or pursuing objectives outside Australia, or
  + the person’s deployment outside of Australia as a member of disciplined force by an Australian Government or authority.
* the exemption is only available in respect of ‘foreign earnings’, which includes earnings, salaries, wages, commission, bonuses or allowances or amounts included in a person’s assessable income under the employee share scheme provisions included in Division 83A of the *Income Tax Assessment Act* *1997* (**ITAA 1997***)*. This does not include employment termination payments.

Special rules also apply under section 23AG(3) to calculate an individual resident’s tax payable on total income comprising both income which is exempt under this provision and other taxable income.

**Taxable foreign employment income**

As Australian resident individuals are taxed on their worldwide income, where the limited exemption under section 23AG of the ITAA 1936 does not apply, foreign sourced employment income is fully subject to income tax in Australia.

To relieve any double taxation, a tax offset is generally available to reduce the Australia tax liability for any foreign income tax paid. Consideration should also be given to the provisions of any relevant Double Tax Agreements entered into between Australia and the foreign country.

*Foreign income tax offset (FITO)*

Where a resident employee works overseas and is required to pay tax in that overseas country, that individual may be able to claim a FITO under Division 770 of the ITAA 1997.

The amount of the FITO (which is subject to a cap) is the amount of foreign tax that has actually been paid[[1]](#footnote-1) by the employee, to the extent that this relates to the foreign income.

The amount of the FITO that can be claimed is capped to the greater of $1,000 or the amount of Australian income tax that would have been payable on the foreign employment income (if no FITO were available), subject to certain assumptions that must be made[[2]](#footnote-2).

For example, assume an individual on assignment in Sweden is taxed $3,000 on employment income of $10,000 and assume that the amount of Australian tax on that same $10,000 employment income is $2,000 in Australia. In these circumstances, the amount of the FITO that can be claimed in the individual’s Australian income tax return cannot be greater than the Australian tax (limit) of $2,000.

The FITO is a non-refundable tax offset which can only apply to reduce or extinguish the individual’s Australian tax liability, but which cannot result in a tax refund if the amount of the offset exceeds that person’s income tax liability in Australia. Any unused FITO cannot be carried forward to later income years.

*Foreign Income Summary*

A resident individual that works overseas on assignment will generally be issued with a ‘Foreign Income Summary’ by their employer. This is similar to a domestic Income Summary but also includes details of all the information relevant to the individual’s assignment overseas including:

* gross salary and wages
* foreign taxes paid
* reportable fringe benefit amounts
* reportable employer superannuation contributions
* any lump sum payments.

The Foreign Income Summary can be used to substantiate the foreign tax paid for the purpose of claiming the FITO, however, the employee should also retain a copy of their host country tax return and/or notice of assessment to substantiate the foreign taxes paid.

*Fringe Benefits Tax (FBT)*

Any fringe benefits provided to an individual resident employee from an employer may be subject to FBT in Australia even though the employee is on assignment overseas. Where this is the case, any reportable fringe benefits must be included on the individual’s Income Summary or Foreign Income Summary.

It is important to note reportable fringe benefits may affect the amount of certain government allowances currently being received by the individual, such as family tax benefits.

*Substantiation for deductions*

Any expenses incurred as a result of a resident’s overseas employment must satisfy the normal substantiation requirements, in order for them to be eligible to be claimed as a deduction in that person’s individual income tax return. These substantiation requirements include, amongst other things, logbooks, receipts and declarations.

*Living Away From Home Allowance (LAFHA)*

A LAFHA, if structured appropriately, can be exempt from FBT whilst being tax free to employees. However, the concessional tax treatment of a LAFHA (and associated benefits) is limited to a maximum period of 12 months unless an employee is employed on a ‘fly‑in fly‑out’ (FIFO) or ‘drive‑in drive‑out’ basis (DIDO).

To be eligible for the concession an employee must:

* maintain a home in Australia (at which they usually reside) which is available for their immediate use and enjoyment at all times while living away from that home for their work,
* be able to substantiate all accommodation expenses,
* be able to substantiate all expenses incurred on food or drink, if the food or drink expenses incurred are more than the Commissioner of Taxation’s reasonable amounts, and
* provide their employer with the appropriate living away from home declaration(s).[[3]](#footnote-3)

Of particular relevance, if the food and drink allowance paid to the employee (as part of the LAFHA) exceeds the Commissioner’s reasonable food and drink component,[[4]](#footnote-4) the whole amount must be substantiated, not just the excess. This is in addition to substantiating all accommodation expenditure.

If the LAFHA does not meet the above criteria, the taxable value of the LAFHA fringe benefit for FBT purposes is generally the amount of the benefit unless the employee is engaged on a FIFO or DIDO basis, in which case certain concessional rules may apply.

If you have further queries on any details contained within this letter or on any other matter, please do not hesitate to contact me on [insert telephone number].

Yours faithfully

[**Insert Name and Title**]

1. A payment of foreign tax will qualify for a FITO where the foreign tax is paid by the employee or by a third party on the employee’s behalf (e.g. amounts of tax withheld by the employer). [↑](#footnote-ref-1)
2. These assumptions include disregarding deductions (excluding debt deductions) that relate to deriving assessable income on which foreign tax has been paid and any other foreign sourced income. [↑](#footnote-ref-2)
3. There are three possible declarations that may be required in order to access the concessional FBT treatment of a LAFHA, i.e. LAFHA declaration regarding employees who fly-in fly-out or drive-in drive-out, employee-related expenses and employees who maintain an Australian home. [↑](#footnote-ref-3)
4. For the 2023/24 FBT year see TD 2023/2. [↑](#footnote-ref-4)