

ETRS/SRTL Public Ruling 2001/5

Public Ruling: The meaning of “wages” and “reward for services”

Relying on this Ruling

This is a public ruling within the meaning of Section 66 of Regulation 2000/18. Information in this ruling may be relied upon by taxpayers as the basis for determining their tax liability. This Ruling was revised with effect from 1 July 2003.

Introduction

1. Section 28 of Regulation 2000/18 imposes a wage income tax on “taxable wages” in respect of employment in East Timor. “Taxable wages” are defined in section 3 of the Regulation as “wages” less “exempt wages”. Wages that are exempt wages are specified in Part B of Section 5 of Schedule 1 of the Regulation.
2. It is the responsibility of persons who pay wages to withhold wage income tax from the wages paid (section 30 of Regulation 2000/18) and to deliver the withheld amount to the Central Payments Office or its nominated agent (section 31 of Regulation 2000/18). Where wage income tax has been correctly withheld from an employee’s wages, the employee has no further wage income tax liability in respect of those wages (section 33.1 of Regulation 2000/18). If wage income tax has *not* been correctly withheld from an employee’s wages, the Commissioner may make an assessment of the wage income tax due and this tax must be paid by the employee (section 33.2 of Regulation 2000/18).
3. The term “wages” is defined in section 3 of Regulation 2000/18 to include all types of payments and benefits that are a reward for services. The definition is reproduced in the appendix to this ruling. The last item in the list of items included in the meaning of wages is “non-wage benefits” in excess of a \$20 monthly threshold where the non-wage benefits are provided by an employer that is exempt from income tax. The definition of the term “non-wage benefits” is also reproduced in the appendix to this ruling.
4. In most cases, wages will be paid directly from an employer to an employee. However, an employee will be treated as receiving wages that are indirectly received because, for example, they are reinvested or accumulated for the person’s benefit or dealt with on the person’s behalf, including paid to another person (section 92 of Regulation 2000/18). Wages will be treated as being dealt with on a

person's behalf when that person is the person who provided services to which the payment relates.

5. The definitions of wages is extremely broad. It is intended to catch all types of remuneration without regard to its form or legal nature. It does not, however, extend to all benefits from an employer to an employee – the comprehensive listing of benefits included in wages are all read subject to the opening condition – they must be provided as a “reward for services”.

6. This Public Ruling discusses the concept of “reward for services” and explains the circumstances under which benefits from an employer to an employee will not be considered a reward for services.

7. There are two elements to the phrase “reward for services”. The first is the requirement that there be a connection between a benefit and the provision of services. The second is the requirement that the benefit amounts to a “reward” for an employee. The next (second) section of this Public Ruling addresses the need for a connection between a benefit and the provision of services for the benefit to constitute wages. The third section of this Public Ruling explains when a benefit will be considered a “reward”.

When is a benefit a reward *for* services?

8. For a benefit received by an employee to be wages, the benefit must be a reward *for* services. The requirement that the reward be *for* services and not *for* some other reason means it must be possible to identify a connection between a benefit received by a person and the provision of services for the benefit to be wages – in other words, the benefit must be a *consequence of* or the *result of* the provision of services.

9. Not all benefits provided by an employer to an employee will satisfy this connection requirement. For example, an employer may also be a friend of an employee and may make a gift such as a wedding gift in a personal capacity and not in the capacity of an employer.

10. Whether a benefit is made in consequence of a person's provision of services to an employer or in consequence of another relationship between the persons is an objective question of fact. The subjective understanding of the employee will not determine the character of the payment.

11. A number of factors can be used to determine the character of the payment. One test is to see whether the employer is an individual with a personal relationship with the person receiving a gift or a legal person or partnership. Only a natural person can have a personal

relationship with another natural person -- it is not possible for a business entity such as a legal person or a partnership to have a “personal” relationship with a natural person. Accordingly, whether or not a benefit from a legal person or a partnership is labelled a gift by the parties, if the payment is made from an employer to an employee, it will be considered a reward for services.

12. Another test is to see whether the benefit was provided on a once-off basis in consequence of a special event such as a wedding or graduation or whether it is a repetitive gift such as an annual Christmas gift. In the case of a repetitive gift, the employer is considered to regard the benefit a consequence of the continued employment of the employee. Even if the employer is a natural person and even if the parties claim the benefit is provided in consequence of a personal relationship between the two persons, because of its regularity, it will be seen as a consequence of the ongoing employment relationship.

13. Note that, as mentioned previously, if a gift (or any other benefit) would be wages of an employee had it been made directly to the employee, it remains that person’s wages even if paid to another person.

14. A third test is based on the employer’s treatment of the expense for the benefit. If the employer treats the expense of the benefit in any way as an expense of his or her business enterprise, it will not be a gift in consequence of a personal relationship between the parties but will be remuneration for services and accordingly will fall within the definition of wages. By way of contrast, if the employer does not record the expense in any way that relates to his or her business but rather treats the expense solely as a personal expense, the benefit is likely to fall outside the definition of wages, provided the other tests mentioned above are also satisfied.

When is a benefit a *reward* for services?

15. Not all benefits received in consequence of employment will be a “reward” for services. The term reward implies a gain to the recipient, a payment that leaves the person in a better economic position because of the employment. A reward can be contrasted with a benefit that merely compensated a person for a loss or expense directly incurred in the course of carrying out employment responsibilities. This type of benefit would restore the person to the position they would have been in had they not been in employment and incurred an expense, but would not be a genuine gain or reward to them.

16. A example of a benefit that is in consequence of employment but is not a reward for services (because it is not an economic gain) is

the provision of tools or equipment or special clothing such as protective gloves or boots required to carry out employment tasks. These are benefits to the employee and they are in consequence of employment, but they are not rewards in the sense of gain to the employee. If the person were not employed they would not need the tools or equipment. The provision of these items is therefore not a gain to them – it merely leaves them in a position to carry out their employment services. The benefits are used directly in the course of carrying out employment responsibilities.

17. This is equally true of a reimbursement of expenses directly incurred in the course of carrying out employment responsibilities. For example, if an employee purchases tools or equipment used in carrying out employment services and the employer reimbursed those expenses, the benefit would not be a reward to the employee because there is no gain to that person compared to their position had they not been in employment.

18. Provision of benefits used in the course of employment and reimbursement of expenses incurred by an employee directly in the course of carrying out employment duties must be contrasted with benefits that put a person in the position to carry out employment or reimbursement of expenses that put a person in position to carry out employment but are not directly part of the employment process.

19. For example, if an employer provides food or clothing (other than special work or protective clothing) or accommodation to an employee or reimburses an employee's expenses for food or clothing or accommodation, the benefit or reimbursement will normally be considered a "reward" for services as it is a personal benefit or expense of the employee, not directly related to carrying out employment responsibilities. Everyone needs to eat and to wear clothes and to have accommodation in order to work. But these are not expenses directly related to carrying out employment duties since people would have these expenses even if they were not carrying out services for their employer. If the employer provides these benefits or reimburses the employee for the cost of these benefits, the employer is providing personal benefits to the employee and this is a reward or an economic benefit to the employee. It does not simply compensate the employee for expenses that he or she would not have suffered if the employee had not carried out employment responsibilities.

When the provision of food and accommodation or the reimbursement of food and accommodation expenses will *not* be considered a reward for services?

20. In some particular cases, expenses that would otherwise be personal expenses of an employee may be expenses related to carrying out employment services *away from the employee's ordinary place of residence*. An example would be the provision of airfares to travel to employment in East Timor or the reimbursement of such expenses where the employee retains an ordinary place of residence outside East Timor and will return to the ordinary place of residence when employment services have finished. The benefit of an air ticket or reimbursement of the cost of an air ticket does not relate to anything in the actual course of carrying out employment responsibilities. However, it is necessary for the employee to carry out those responsibilities at somewhere other than the place of the employee's ordinary residence.

21. As noted, the provision of (or reimbursement of) food, clothing or accommodation by an employer would normally be a reward for services. In exceptional circumstances, however, the reimbursement of accommodation expenses (or the provision of accommodation) will be compensation for an expense incurred only because of employment. This will be the case where an employee maintains a home or similar ordinary place of residence outside East Timor and is faced with the need for a second place of residence in East Timor to carry out employment responsibilities. If the employee provides the employer with proof that the employee has a home or similar ordinary place of residence outside East Timor and has a need for a second place of residence in East Timor only because of the employment responsibilities in East Timor, the provision of accommodation or the reimbursement of accommodation expenses will not form part of the employee's wages.

22. In circumstances similar to those described in the previous paragraph, a portion of a person's food expenses may also not represent a reward for services. While it is true that persons would incur food expenses if they worked in East Timor or not, where employees are staying in a second residence, they are likely to incur higher food expenses than they would if they were in their ordinary residence outside of East Timor. This is because in most cases their residence in East Timor is unlikely to have the same food preparation and storage facilities as their ordinary place of residence and higher food costs, particularly for prepared foods, may be experienced.

23. To the extent an employer provides meals or reimburses the cost of meals in excess of the cost an employee would incur for meals at the employee's primary place of residence, the benefit will not be a reward and therefore will not be considered wages. The Commissioner considers provision to an employee in Dili of meals with a cost to the employer of U.S. \$9 per day or the actual reimbursement of meal expenses for such a person up to U.S. \$9 per day to be compensation for the additional cost of meals to these employees and thus outside the meaning of wages. The Commissioner considers provision to an employee outside of Dili of meals with a cost to the employer of U.S. \$6 per day or the actual reimbursement of meal expenses for such a person up to U.S. \$6 per day to be compensation for the additional cost of meals to these employees and thus outside the meaning of wages.

24. In some cases, employees with a home or similar place of residence outside East Timor will be furnished with "room and board" – that is, accommodation and some or all meals and incidentals such as laundry services – by an employer in East Timor or will be reimbursed for the expense of staying in accommodation where room and board is provided. In these circumstances up to U.S. \$15 per day for room and food supplied in Dili (up to U.S. \$11 per day for outside Dili) of the cost of room and board will be considered to be compensation for the additional costs to these employees and thus outside the meaning of wages.

Treatment of Living Away from Home Allowances

25. In some cases, rather than provide "second home" accommodation to employees or reimburse employees for the cost of maintaining a second place of residence in East Timor, employers will simply provide a "living away from home allowance". If the allowance is not tied to actual accommodation or additional food expenses but can be freely spent by the employee on anything the employee chooses, it will normally be considered to be another type of reward for performing services and thus will be considered wages. However, where the employee has provided the employer with evidence that the employee has a primary home or similar accommodation outside East Timor, it will be clear that some of the allowance will have to be spent on the additional cost of accommodation and the additional costs of meals in East Timor.

26. Provided that (a) an employer does not also provide accommodation or meals to an employee or reimburse those costs separately and (b) the employee has provided the employer with evidence that the employee has a primary home or similar accommodation outside East Timor, the Commissioner will accept

that “wages” do not include up to U.S. \$6 per day of an allowance used to pay for the additional costs of accommodation for an employee staying in Dili and up to U.S. \$5 per day of an allowance used to pay for the additional costs of accommodation for an employee staying outside Dili. Allowances up to these amounts will not, therefore be considered part of wages subject to wage income tax.

27. Additionally, under the circumstances described in the previous paragraph, the Commissioner will accept that up to U.S. \$9 per day of an allowance will be used to pay for the additional costs of meals and incidentals for an employee staying in Dili and up to U.S. \$6 per day of an allowance will be used to pay for the additional costs of meals and incidentals for an employee staying outside Dili. Allowances up to these amounts will not, therefore be considered part of wages subject to wage income tax.

ETRS to monitor payments for food and accommodation

28. In order to ensure that the maximum amounts for accommodation, meals and incidentals specified earlier in this ruling that the Commissioner of the ETRS will accept as not being wages remain realistic, the Commissioner shall ensure that surveys are completed at least annually for the purpose of reviewing those amounts and updating this ruling where appropriate.

29. As part of the ETRS’s routine taxpayer audit program, the ETRS will also review employer/employee arrangements which involve employees directly or indirectly receiving amounts for accommodation, meals or incidentals which are claimed to be not liable for wage income tax.

30. Where as a result of checks in accordance with the previous paragraph, the ETRS believes direct or indirect payments by an employer to an employee have been changed to reduce the amount of wages that would be subject to wage income tax in accordance with this ruling, and the employer cannot provide evidence to justify such changes, then the Commissioner may recharacterize the arrangement under section 93 of Regulation 2000/18. In addition to the adjustments allowed to be made by the Commissioner under that section, the ETRS may also decide to impose the penalty for understatement of tax in section 74 of Regulation 2000/18 and/or take prosecution action for evasion of tax under section 81 of that Regulation.

Reimbursement of other expenses

31. Regulation 2000/18 provides that expenses reimbursed or discharged by an employer will be subject to wage income tax. In some cases, expenses that would otherwise be personal expenses of an employee may be expenses related to carrying out employment services away from the employee's ordinary place of residence. The test is whether the reimbursement is a "reward" for service or a benefit that merely compensated a person for a loss or expense directly incurred in the course of carrying out employment responsibilities.

32. The reimbursement of airfares to travel to employment in East Timor is discussed earlier as being in this category. Also included would be reimbursement of medical expenses and vaccinations required for a person to come to East Timor to carry out employment responsibilities. In these situations, the reimbursed expense is not a reward for service and would not be included in wages.

Summary

33. For the reasons outlined in this Public Ruling, the following amounts are not considered to be wages subject to the wages income tax, where the employee has provided evidence to the employer that the employee has a primary home or similar accommodation outside East Timor:

- actual provision of accommodation
- actual reimbursement of accommodation cost
- provision of meals and incidentals in Dili up to a cost to the employer of U.S. \$9 per day and provision of meals and incidentals outside Dili up to a cost to the employer of U.S. \$6 per day
- actual reimbursement of the cost of meals and incidentals in Dili up to U.S. \$9 per day and actual reimbursement of the cost of meals and incidentals outside Dili up to U.S. \$6 per day
- provision of room and food in Dili up to a cost to the employer of U.S. \$15 per day and provision of room and board outside Dili up to U.S. \$11 per day
- actual reimbursement of the cost of room and food in Dili up to U.S. \$15 per day and actual reimbursement of the cost of room and board outside Dili up to U.S. \$11 per day
- payment of a living-away-from-home allowance where the employee does not receive any of the benefits mentioned in previous paragraphs, subject to the following limits:
 - allowance in respect of accommodation

- in Dili U.S. \$6 per day
 - outside of Dili U.S. \$5 per day
- allowance in respect of meals and incidentals
 - in Dili U.S. \$9 per day
 - outside of Dili U.S. \$6 per day
- actual reimbursement of additional costs arising from the need of the employee to carry out employment responsibilities away from the employee's ordinary residence, where it does not constitute a "reward" for service e.g. reimbursement for the cost of vaccinations

Date of Effect

34. This Public Ruling has effect from 1 July 2003.

Appendix: Definition of wages and non-wage benefits (section 3 of Regulation 2000/18)

"wages" means any reward for services provided by an *employer* to an *employee*, including:

- (a) any salary provided to the *employee*, including leave pay, overtime payments, commissions, and bonuses;
- (b) director's fees;
- (c) the value of gifts provided by an *employer* to an *employee*;
- (d) any allowance provided by the *employer* for the benefit of an *employee*;
- (e) any payment provided by the *employer* in respect of loss or termination of employment;
- (f) any payments however described made on termination of employment in respect of entitlements outstanding at the time of termination;
- (g) the reimbursement or discharge by an *employer* of any expense of the *employee* including utilities expenses;
- (h) the amount of any reimbursement or discharge by an *employer* of an *employee's* medical expenses;
- (i) the amount of any waiver where any *employer* waives an obligation of the *employee* to pay an amount owing to the *employer*; and

- (j) *non-wage benefits* greater than \$20 provided in a calendar month to *employees* of an *employer* that is exempt from income tax.

“non-wage benefits” means any reward for services provided by an *employer* to an *employee*, including:

- (a) the market value of any non-cash benefit provided by an *employer* to an *employee*;
- (b) the value determined by the *Commissioner* of the provision by the *employer* to an *employee* of the use of a motor vehicle wholly or partly for private purposes of the *employee*;
- (c) the value determined by the *Commissioner* of the provision by the *employer* of accommodation or housing;
- (d) the value determined by the *Commissioner* of the provision by an *employer* to an *employee* of a housekeeper, driver, guard, gardener, or other domestic assistant; and
- (e) the cost to the *employer* of providing an *employee* with any meal, refreshment, or entertainment except in the course of providing a *good* or service for the *employer* where the *Commissioner* considers that the cost of provision for the *employer* is reasonable.

Angelo Almeida
Commissioner of East Timor Revenue Service
1 July 2003

Legislative references:

definition of “wages” Reg 2000/18 s 3
definition of “non-wage benefits” Reg 2000/18 s 3