

## ATO RECEIVABLES POLICY

### PART G Penalties and Interest Relating to Receivables Activity

# CHAPTER 95

# VARIATION AND UNDERESTIMATION PENALTIES

*The policy in this chapter is to be followed by Tax Office staff. We have made every effort to ensure it is technically accurate, but in the interests of clarity it has been written in 'plain English' and should not be read or interpreted like legislation. If you feel that something in the chapter is wrong or misleading, please advise the Tax Office. .*

**Date of effect:** 24 July 2008 (This version replaces the 2006 version.)

**Key legislation:** Subdivision 45-G in Schedule 1 to the *Taxation Administration Act 1953*; Subdivision 162D of the *A New Tax System (Goods and Services Tax) Act 1999*; section 112B of the *Fringe Benefits Tax Assessment Act 1986*

## PURPOSE

1. This chapter deals with:

- Penalties in the form of general interest charge (GIC) that may apply to an entity as a result of underestimating:
  - a Instalment rates
  - b Instalment amounts
  - c Benchmark tax, or
  - d Other amounts
- The imposition and remission of GIC that apply to those variations, underestimations and adjustments in relation to fringe benefits tax (FBT), pay as you go (PAYG) instalments, provisional tax and company instalments.

## INTRODUCTION

2. The instalment systems for the payment of PAYG, goods and services tax (GST) and FBT instalments provide flexibility for entities whose circumstances change during the financial year and for whom the instalment amount or rate notified by the Commissioner is inappropriate, while also providing a disincentive to defer tax by underestimating their liability.
3. Subdivision 45-G in Schedule 1 to the *Taxation Administration Act 1953* (TAA), Subdivision 162-D of the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act) and section 112B of the *Fringe Benefit Tax Assessment Act 1986* (FBTAA) provide for the application of GIC in certain cases if varied instalment amounts are too low.
4. The amount to which the GIC is applied is calculated using formulae specified in the legislation.

5. GIC will not be imposed if instalments are less than the tax liabilities for the year and the entity has used the instalment rate or amount notified by the Commissioner or a rate or an amount higher than that notified by the Commissioner in determining its instalment amount.
6. The GIC must be notified to the entity by the Commissioner and the entity has 14 days to pay.

#### **A PAYG instalments**

7. Section 45-205 of Schedule 1 to the TAA provides that an entity may choose to vary an instalment rate for working out the amount of its instalment for an instalment quarter in an income year.
8. When an entity works out an amount of an instalment using an instalment rate it has chosen under section 45-205, it must notify that rate in the approved form for the quarter on or before the due date for the instalment - section 45-210 of Schedule 1 to the TAA.
9. Section 45-230 of Schedule 1 to the TAA prescribes that a penalty (being the GIC) is incurred if an entity varies its instalment rate under section 45-205 of Schedule 1 to the TAA such that the rate is less than 85% of its benchmark instalment rate for that income year as calculated by the Commissioner under Subdivision 45-K.
10. The GIC is payable on the shortfall in the quarterly instalment from the due date of the instalment until the due date for payment of assessed tax.
11. The GIC is payable on the amount worked out as follows:
 

(Rate discrepancy x instalment income for the variation quarter) + credit adjustment.
12. Sub-section 45-230(4) of Schedule 1 to the TAA requires the Commissioner to give an instalment payer written notice of the GIC and the instalment payer is required to pay the charge within 14 days.
13. Section 45-112 of Schedule 1 to the TAA provides that an entity that pays on the basis of GDP-adjusted notional tax may choose to work out the amount of the instalment on the basis of its estimate of its benchmark tax for that income year.
14. When an entity works out an amount of an instalment on the basis of its estimate of its benchmark tax for that income year it must notify the Commissioner in the approved form on or before the due date for the instalment - subsection 45-112(2) of Schedule 1 to the TAA.
15. Section 45-232 of the TAA prescribes that a penalty (being the GIC) is incurred if an instalment payer, being a quarterly instalment payer using the GDP adjusted notional tax method, estimates under section 45-112 of Schedule 1 to the TAA its benchmark tax amount such that it is less than 85% of its benchmark tax for that income year as calculated by the Commissioner under Subdivision 45-K.
16. The GIC is payable on the shortfall in the instalment from the due date of the instalment until the due date for payment of assessed tax.
17. The GIC is calculated on an amount as follows:
 

(Acceptable amount of the instalment - Actual amount)

if this amount is positive.
18. This amount ('the shortfall') is reduced if, for a later instalment quarter in the same income year the:

('Acceptable amount' of your instalment for the later quarter - Actual amount of your instalment for the later quarter)

is negative – subsection 45-233(1) of Schedule 1 to the TAA. That amount (expressed as a positive) is called a 'top up'.

19. The shortfall is reduced by so much of the top up as does not exceed the shortfall - subsection 45-233(3) of Schedule 1 to the TAA.
20. This reduction only has effect for each day in the period commencing at the beginning of the day on which the instalment for the later quarter was due, and ending on the day on which the assessed tax for the income year was due.
21. Subsection 45-232(5) of Schedule 1 to the TAA requires the Commissioner to give an instalment payer written notice of the GIC and the entity is required to pay the charge within 14 days.
22. Section 45-115 of Schedule 1 to the TAA provide that an entity who is an annual payer may choose to pay the annual instalment that it estimates will be its benchmark tax for that income year.
23. When an entity works out an amount of an instalment using its estimate of its benchmark tax for that income year it must notify the Commissioner in the approved form on or before the due date for the instalment - subsection 45-115(3) of Schedule 1 to the TAA.
24. Section 45-235 of the TAA prescribes that a penalty (being the GIC) is incurred if an instalment payer, being an annual instalment payer, estimates its instalment amount such that it is less than 85% of its benchmark tax for that income year as calculated by the Commissioner under Subdivision 45-K of Schedule 1 to the TAA.
25. If the estimated amount of the instalment was calculated under paragraph 45-115(1)(c) of Schedule 1 to the TAA, the GIC is payable on the difference between the estimated instalment amount and the lowest of:
  - the amount of the instalment worked using the most recent instalment rate notified by the Commissioner before the end of the income year
  - the most recent notional tax notified by the Commissioner before the end of the income year; or
  - the instalment payer's benchmark tax for the income year.
26. The GIC is payable on the shortfall in the annual instalment from the due date of the instalment until the due date for payment of assessed tax.
27. Subsection 45-235(5) of Schedule 1 to the TAA requires the Commissioner to give an instalment payer written notice of the GIC and the entity is required to pay the charge within 14 days.
28. If any of the GIC imposed under these provisions remains unpaid after the 14 day period, then GIC accrues on that unpaid amount for each day (starting at the end of the 14 days) during which either the unpaid amount or the GIC on the unpaid amount remains unpaid - subsections 45-230 (5), 45-232 (6), and 45-235(6) of Schedule 1 to the TAA.
29. The Commissioner may remit the GIC imposed under subsections 45-230(2), 45-232(2) or 45-235(3), if it is considered that because of special circumstances, it would be fair and reasonable to do so - section 45-240 of Schedule 1 to the TAA.

## **B GST instalments**

30. Subdivision 162-D of the GST Act imposes penalties where an entity varies their notified instalment amount and that varied amount is too low. The penalty is based on the GIC rate, and the machinery provisions in Division 298 of Schedule 1 to the TAA apply.

31. There are three circumstances where a penalty can arise if a varied instalment amount is too low. These are:

- the total of what has been paid (including the instalment payments) is less than 85% of the annual GST liability - section 162-175 of the GST Act
- the estimated annual GST amount is less than 85% of the annual GST liability or 75% of the annual GST liability if the GST instalment quarter ends on 30/9/01 - section 162-180 of the GST Act
- the varied instalment amount is not the correct proportion of the estimated annual GST amount - section 162-185 of the GST Act.

32. Section 162-175 of the GST Act imposes a penalty where the total of the varied GST instalments is less than 85% of the entity's actual GST liability for the year.

33. The penalty is levied for each quarter in which an entity pays the Tax Office a varied instalment amount - subsection 162-175(1). The amount of this penalty for a particular day is worked out by applying the GIC to an entity's GST instalment shortfall - subsection 162-175(2). An entity's GST instalment shortfall for each quarter, under this section, is worked out as follows:

[Annual GST liability for the instalment tax period x The appropriate percentage for the GST instalment quarter] - GST already payable subsection 162-175(3).

34. Where an entity is liable to this penalty for more than one GST instalment quarter in the financial year, the amount of the GST instalment shortfall for later GST instalment quarters is reduced by the amount of the preceding quarter(s) GST instalment shortfall. Note: This reduction does not apply to a shortfall for the first GST instalment quarter, as there is no preceding quarter for that financial year - subsection 162-175(4).

35. Where the sum of the GST instalment shortfalls for previous GST instalment quarters is greater than the shortfall amount for the current GST instalment quarter, the entity is not liable for a penalty under section 162-175 of the GST Act for that GST instalment quarter. Penalty would fall for consideration under section 162-180 or section 162-185.

36. Section 162-180 of the GST Act imposes a penalty where the estimated annual GST liability on which the entity based their varied instalment amount is less than 85% (or 75% if the estimate relates to the GST instalment quarter that ends on 30 September 2001) of the actual annual GST liability for the financial year; and the varied instalment amount for that quarter is less than or equal to 25% of the annual GST liability for the instalment tax period. An entity will only be subject to this penalty if it is not subject to a penalty under section 162-175 of the GST Act - subsection 162-180(1).

37. The penalty is calculated by applying the GIC to the GST instalment shortfall for each quarter (subsection 162-180(2) of the GST Act). The GST instalment shortfall for each quarter, under this section, is the amount worked out as follows:

[The annual GST liability for the instalment tax period - The estimated annual GST amount for the GST instalment quarter] x The appropriate percentage for the GST instalment quarter - subsection 162-180(3).

38. The estimated annual GST amount relating to each GST instalment quarter is the amount notified by the entity on its current business activity statement, or if not notified, the amount relating to the preceding GST instalment quarter. However, where the entity has shown an amount that would be less than the estimation (based on their instalment amounts) the estimated annual GST amount is worked out as follows:

[GST already payable / the appropriate percentage for the GST instalment quarter].

For example, where an entity notified the tax office that their estimated annual GST amount for the first quarter was \$40,000 but paid \$12,000 as the first quarter instalment, the estimated annual amount for that quarter would be revised to \$48,000 (that is \$12,000/25%) - subsection 162-180(5).

39. Where the GST instalment quarter in question is not the first GST instalment quarter in the financial year, and the entity is liable to this penalty for more than one GST instalment quarter in that year, the GST instalment shortfall for the quarter in question is reduced by the GST instalment shortfalls in the earlier instalment quarter(s). Where the sum of those amounts for prior GST instalment quarters is greater than the GST instalment shortfall amount on which the penalty will be applied for the later GST instalment quarter, the entity is not liable for a penalty for that GST instalment quarter - subsection 162-180(4).

40. Under section 162-195 of the GST Act, if an entity is liable to pay a penalty under either section 162-175 or 162-180 of the GST Act, the amount of the GST instalment shortfall (which is applied to the penalty) is reduced if:

- the entity's notified instalment amount is less than 25% of its annual GST liability for the instalment tax period, or
- the Commissioner has not provided the entity with a notified instalment amount, and is satisfied that the notified instalment amount would have been less than 25% of its annual GST liability.

41. The reduction in the GST instalment shortfall is the difference between the annual GST liability that should have been paid in a particular quarter, and the sum of the entity's 'notified and other amounts'. These are comprised of the entity's notified instalment amounts (or what would have been the entity's notified instalment amounts had the Commissioner notified the entity of them) and any net amounts for the financial year (if the instalment tax period is part of a financial year). Note: Where the net amount is less than zero, this amount is subtracted from the remaining amounts - subsection 162-195(2).

42. The entity is not liable for a penalty under section 162-175 or section 162-180 of the GST Act (as the case may be) in relation to a quarter, if because of the reduction, an entity's GST instalment shortfall for the GST instalment quarter is less than zero - subsection 162-195(3).

43. Section 162-185 of the GST Act imposes a penalty where the varied instalment amount for a quarter, together with GST paid or payable for any previous quarters in the financial year, is less than the progressive total of GST instalments worked out on the basis of estimated annual GST amount and applicable to that quarter. This penalty will only apply if an entity has varied its GST instalment and is not liable to a penalty for that quarter under section 162-175 or section 162-180 of the GST Act.

44. This penalty ensures that an entity that correctly estimates its annual GST amount cannot vary their instalments to zero in the first three quarters and then pay 100% of the estimated annual GST liability in the last quarter.
45. The penalty applies the GIC to the GST instalment shortfall for a quarter. The GST instalment shortfall, under this section, is the estimated annual GST amount relating to the GST instalment quarter multiplied by the appropriate percentage for that quarter less the 'GST paid'. An entity's 'GST paid' is the sum of the varied instalment amount for the GST instalment quarter, plus any GST instalments for earlier GST instalment quarters (if any), plus any early net amounts for prior tax periods in the financial year (if any) - paragraph 162-185(1)(c) of the GST Act.
46. A penalty under Subdivision 162-D of the GST Act is imposed at the GIC rate for each day in the period:
  - starting on the due date for the GST instalment for the GST instalment quarter, and
  - finishing at the end of the day before the entity must, under section 162-110, pay to the Commissioner its net amount for the instalment tax period that includes that GST instalment quarter.
47. Generally, penalties imposed under Subdivision 162-D of the GST Act are worked out by multiplying the GIC rate for that day by the sum of the following amounts:
  - so much of the charge from previous days remains unpaid
  - the specified amount.
48. However, section 162-200 of the GST Act allows penalties to be reduced in certain circumstances. Section 162-200 provides that where the GST shortfall in a quarter is made up in a later instalment period in the financial year, the penalty is reduced by the amount by which the later GST instalments exceed 25% of the annual GST liability. The amount of this excess is called the top up. If some of this top up has already been applied to reduce a GST instalment shortfall in a previous quarter, later quarters' shortfalls can be reduced by so much of the top up that has not been previously applied. Where an amount of a GST instalment shortfall is made up in a later GST instalment quarter, the period for which the penalty is imposed (on the original shortfall) will end on the day before that shortfall amount was made up.
49. The machinery provisions for a penalty applied under Subdivision 162-D are found in Division 298 in Schedule 1 to the TAA. Section 298-5 in Schedule 1 expressly includes the GST instalment shortfall penalties within the scope of that Division. Although section 298-5 refers to Subdivision 162-C of the GST Act rather than Subdivision 162-D, there is a 'Note' in section 162-140 that a penalty may be applied under Subdivision 162-D if a variation of a GST instalment amount is too much of an underestimate of an entity's total GST liability.
50. This is considered sufficient to link Subdivision 162-C of the GST Act with Subdivision 162-D and bring the latter within the scope of Division 298 of the TAA. This means that a notice of penalty determined under Subdivision 162-D is subject to the requirements in section 298-10 of the TAA. Therefore, a notice of liability to pay the penalty must be given to the entity, and according to section 298-15 of the TAA, the notice must specify a due date for payment for the penalty. This due date must be at least fourteen days after the notice is given to the entity.
51. Under section 298-25 of the TAA, if any of the penalty remains unpaid after it is due, the entity is liable to pay GIC on the unpaid amount of the penalty for each day in the period that:

- started at the beginning of the day by which the amount was due to be paid, and
- finishes at the end of the last day, at the end of which, any of the following remains unpaid:
  - the amount
  - GIC on any of the amount.

52. Section 298-20 in Schedule 1 to the TAA allows the Commissioner to remit all or part of the penalty. If the entity seeks remission of the penalty under this section, and the Commissioner decides not to remit the penalty or to remit only part of it, there is a requirement under subsection 298-20(2) to give written notice of the remission decision to the entity. This is a separate notice to that required under section 298-10 referred to earlier. If the amount of penalty payable after the decision is made is more than 2 penalty units, and the entity is dissatisfied with the decision, it may lodge an objection against the decision in accordance with Part IVC of the TAA - subsection 298-20(3).

53. All of the penalties under Subdivision 162-D are worked out by applying GIC to the GST instalment shortfall for the GST instalment quarter. However, this has to be read in conjunction with section 162-205, which clarifies that the Subdivision does not make an entity liable to pay the GIC. This means that while Subdivision 162-D applies the GIC for the purposes of calculating the penalty, the penalty has to be viewed as a discrete liability in its own right. It cannot be collected as GIC.

54. The penalty is a tax-related liability for the purposes of section 255-1 of Schedule 1 to the TAA, and is recoverable as a debt due to the Commonwealth under section 255-5.

### **C FBT instalments**

55. An employer is required to pay FBT instalments where their 'notional tax amount' is more than \$3,000. Generally the 'notional tax amount' will be the amount of tax assessed for the most recent FBT year for which an assessment has been made. However, an employer may vary the amount of the instalments by making an estimate of the tax that will be payable for the year.

56. Where an employer has made an estimate of tax which was taken to be the 'notional tax amount' and the estimate is less than 90% of the tax assessed for the year, section 112B of the FBTAA prescribes that the employer will be liable to pay GIC.

57. The employer is liable to the GIC on the difference between the amount of the underpaid instalment and the amount worked out using the formula:

$$[\text{Minimum tax amount} \times \text{Relevant fraction}] - [\text{Previous instalments} - \text{Previous credits}].$$

58. The employer is liable to pay the charge for each day in the GIC period that there is a shortfall - subsection 112B(2) of the FBTAA.

59. The GIC period is defined in section 109 of the FBTAA.

For the first three instalments, it is the period:

- from the day that the instalment became due and payable
- until the end of the day before the next instalment is due.

For the fourth instalment, it is the period:

- from the day that the instalment became due and payable
- until the end of 20 May.

60. The amount of the GIC is additional tax payable.

61. Section 8AAG of the TAA allows the Commissioner to remit all or part of the GIC.

## POLICY

### Remission of penalties – general approach

62. The Commissioner will apply, to the extent permissible by law, the principles outlined in Chapter 93 'General interest charge'. It is considered that these principles would reflect the legislative intent. Remission would not be considered if the entity were to rely on general grounds for the request, nor would it be considered if the entity were to rely on factors that could only be remotely linked to the underestimation.

63. The Commissioner will consider all of the factors put forward by an entity in the request for remission, their effect upon the estimates provided and the steps taken to alleviate the underestimation. In particular, the Commissioner will consider:

- (i) factors beyond the control of the entity

64. An entity may be able to demonstrate that the significantly improved revenue (for example assessable 'windfall' gains) or reduced costs were as a result of factors beyond their control and clearly could not be predicted. In considering any remission of GIC, it is also necessary to consider what steps were taken by an entity, particularly quarterly instalment payers, to rectify any potential underpayment in later instalments.

- (ii) acts or omissions of the entity

65. Remission of the GIC would not be considered if inaccurate estimations of instalment rate or benchmark tax arose due to acts or omissions within the control of the entity. Inadequate record keeping or delays in updating records or consulting advisors would not be considered sufficient reason for remission unless such delays were caused by circumstances outside the entity's control. It is necessary to determine whether the underestimation was caused by the entity's direct involvement or otherwise and what steps were taken, if any, to relieve the effects of the circumstances.

- (iii) relieving the circumstances or effects of circumstances

66. The Commissioner must consider the entity's efforts to relieve all of the circumstances that led to the underestimation or the effect of those circumstances, irrespective of whether the circumstances were subject to, or beyond, the entity's control. To be eligible for remission, the entity would be expected to have taken all reasonable action possible, promptly, in an attempt to lessen the severity of the circumstances.

- (iv) fair and reasonable

67. A decision by the Commissioner to remit GIC because it is fair and reasonable must be considered in view of the legislative policy that entities should be liable to additional charges if they underestimate. Not only must the exercise of the power to remit be fair to the entity concerned, it must be fair to the whole community. In other words an entity which underestimates should not be given any advantage over those entities who organise their affairs to ensure they pay correct instalment

liabilities. Entities will need to demonstrate that it is fair and reasonable to remit the GIC, having regard to the nature of the specific event or decision.

- (v) good compliance history
- 68. The extent of any remission would be reduced if the entity's recent compliance record had been unsatisfactory. It would be unfair to entities who meet their obligations if those who choose not to comply are given the same level of remission.

**Chapter 95 - Archived version**

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