IT 2433 - Income tax : substituted accounting periods : adjustments to taxable income

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TAXATION RULING NO. IT 2433

INCOME TAX : SUBSTITUTED ACCOUNTING PERIODS : ADJUSTMENTS TO TAXABLE INCOME

F.O.I. EMBARGO: May be released

REF N.O. REF: 85/5447-1 DATE OF EFFECT: Immediate

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F.O.I. INDEX DETAIL

REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:
I 1206517	SUBSTITUTED ACCOUNTING PERIODS	18(1)

OTHER RULINGS ON THIS TOPIC IT 2360

PREAMBLE In the course of setting out guidelines to be followed in dealing with applications under sub-section 18(1) of the Income Tax Assessment Act for leave to adopt accounting periods other than 30 June Taxation Ruling No. IT 2360 explains the adjustments to taxable income that are required to be made in the year of changeover to ensure that an appropriate amount of tax is paid in the year of changeover.

2. The Ruling also states that the measures announced by the Treasurer in the 1986-87 Budget Speech to amend the income tax law to advance the due dates for payment of quarterly instalments and assessments by companies whose accounting periods for income tax purposes end on a date earlier than 30 June do not affect the necessity to make adjustments to taxable income in the year of changeover.

3. Since the release of Taxation Ruling No. IT 2360 the measures announced by the Treasurer have become law effective for the accounting period which substitutes for the income year ended 30 June 1987. Payment of quarterly instalments of company tax by companies whose accounting period ends on or before 31 May in lieu of the succeeding 30 June is governed by section 221AB. Companies to which section 221AB applies are required to pay instalments of company tax 1 1/2, 4 1/2 and 7 1/2 months after the end of their accounting periods. Transitional arrangements have been made to ameliorate the doubling up of instalments of company tax which would otherwise occur in the year ended 30 June 1987.

4. Following the enactment of section 221AB the need to make adjustments to taxable income in a year where a company is granted leave to adopt an accounting period in lieu of the succeeding 30 June has been reviewed. It has been claimed that, in these cases, adjustments to taxable income in the year of changeover, in addition to advanced instalments of company tax, unfairly disadvantages companies involved. To take an illustration, a company, up to and including the year ended

30 June 1987, has had an accounting period ended 30 June. It is granted leave to adopt an accounting period ending on 31 December 1987 in lieu of the succeeding 30 June 1988. In the 12 months period from 1 July 1987 to 30 June 1988 the company is required to pay 4 instalments of company tax in respect of its income tax liability for the year ended 30 June 1987 and, by virtue of section 221AB, it is also required to pay two instalments of company tax liability for the accounting period ended 31 December 1987. To require an adjustment of taxable income in respect to the accounting period ended 31 December 1987 would, it is claimed, seriously disadvantage companies involved.

RULING

5. It has been decided that companies which are granted leave to adopt an accounting period ending between 1 December and 30 June in lieu of the succeeding 30 June will no longer be required to make an adjustment of taxable income in the year of changeover. Fairness can be achieved through the provisions in the income tax law relating to instalments of company tax.

6. In the illustration given above the first instalment of company tax for the accounting period ended 31 December 1987 will be due on 15 February 1988, i.e. 1 1/2 months after the end of the accounting period. The instalment would be based on one-quarter of the tax payable for the accounting period ended 30 June 1987. It is likely that the income tax payable on the company's taxable income for the accounting period 1 July 1987 to 31 December 1987 will be less than that payable for the year of income ended 30 June 1987 were it assessed for a 12 month period. In these circumstances, once a company has been served with a notice specifying the amount payable as an instalment of company tax, it may, under section 221AG, make an estimate of the taxable income and income tax payable for the accounting period ended 31 December 1987. Unless there are reasons for the estimate not being accepted, e.g. there could be factors which indicate that the company's taxable income will be above the estimate, the amount payable as an instalment of company tax will be equal to one-quarter of the estimate.

7. In the substituted accounting period following the first year of a substituted accounting period, i.e. the year ended 31 December 1988, instalments of company tax will be calculated on one-quarter of the income tax assessed in the preceding year. This means that a company will be liable to tax on a full 12 months income but its instalments of company tax will be based on tax payable on income derived for a shorter period. In the above illustration the company would be liable to tax on income derived during the period from 1 January to 31 December 1988 but instalments of company tax would be based on the income tax payable for the accounting period ended 31 December 1987 - a six month period. Most likely, instalments of company tax will not reflect the actual amount of income tax payable by the company for the accounting period following the first year of a substituted accounting period. The matter can be rectified by making an estimate, in terms of sub-section 221AE(4), of the amount of income tax which will be payable in the following year.

8. As a condition of granting leave to adopt an accounting period ending between 1 December and 30 June in lieu of the succeeding 30 June companies should be required to agree to provide a statement estimating their taxable income for the accounting period following the first year of a substituted accounting period. The statement should be provided within 30 days of the end of the first full year of the substituted accounting period to enable this office to issue a notice under sub-section 221AF(1) specifying the amount payable as an instalment of company tax.

9. In the above example, this would mean that the company is to provide an estimate of its taxable income for the accounting period ended 31 December 1988 by 30 January 1989.

10. Annexure A to this Ruling illustrates the adjustments which would be made in terms of sub-section 221AE(4) and section 221AG. It shows that companies which balance between 1 December and 30 June in lieu of the subsequent 30 June will not be disadvantaged as compared to 30 June balancing companies.

BALANCE DATED BETWEEN 1 JULY AND 30 NOVEMBER

11. Companies which adopt balance dates between 1 July and 30 November in lieu of the preceding 30 June are not affected by the advancing of the due date for company tax instalments and do not have any altered income tax obligations. As a result there is no need to change the practice of requiring the companies to pay income tax in respect of the taxable income derived up to the end of a company's new accounting period.

NEW COMPANIES

12. Where a company commences trading on 1 November and seeks leave to adopt an accounting period ending on 31 December in lieu of subsequent 30 June income tax liability of the company is to be based on its taxable income for the period from 1 November to 31 December. There will be no necessity to make any adjustments to taxable income but it will be necessary to impose the condition referred to in paragraph 8 above. The advancing of instalments of company tax denies any advantage to the company.

OTHER MATTERS

13. The decision to no longer require adjustments to the taxable income of companies which balance between 1 December and 30 June in lieu of the succeeding 30 June does not mean that adjustments already made where a company may have changed its accounting period some years ago can now be reversed. The circumstances where a reversal adjustment can be made are explained in paragraphs 30 to 32 of Taxation Ruling No. IT 2360. However, if any adjustment has been made to a company's taxable income in the year of income substituted for the year ended 30 June 1987 the adjustment may be reversed where the requirements of this Ruling are otherwise observed.

14. The transitional arrangements referred to in paragraph 3 do not apply to situations covered by this Ruling. They apply to companies which, prior to the enactment of section 221AB, had been granted leave to adopt accounting periods affected by section 221AB.

COMMISSIONER OF TAXATION
23 July 1987

APPENDIX

ANNEXURE A

In this example both companies have tax payable of $12m. in each year of income

COMPANY A		BALANCES ON 30 JUNE		
Earliest Date for Company Year End	Tax Instalments	Year Ended 30/6/Y1	Year Ended 30/6/Y2	Year Ended 30/6/Y3
15/8/Y1	3			
15/11/Y1	3			
15/2/Y2	3			
Balance	3			
15/8/Y2		3	15/11/Y2 3	15/2/Y3 3
Balance		3		
15/5/Y3	15/8/Y3			3
Balance				
15/11/Y3			3	
15/2/Y4			3	
Balance			3	
15/5/Y4				
TOTAL	12	12	12	12

instalments based on one-quarter of $6m. after section 221AG estimate by one-quarter of $12m.

* instalments based on one-quarter of $12m. after sub-section 221AE(4) deter one-quarter of $6m.