TR 94/3 - Income tax: tax shortfall penalties: calculation of a tax shortfall and allocation of additional tax

This cover sheet is provided for information only. It does not form part of *TR 94/3 - Income tax: tax shortfall penalties: calculation of a tax shortfall and allocation of additional tax*

This document has changed over time. This is a consolidated version of the ruling which was published on *6 January 1994*

Generated on: 26 November 2026, 07:58:33 AM

Australian Taxation Office

Taxation Ruling
Income tax: tax shortfall penalties: calculation of a tax shortfall and allocation of additional tax

This Ruling, to the extent that it is capable of being a 'public ruling' in terms of Part IVAAA of the ***Taxation Administration Act 1953****, is a public ruling for the purposes of that Part. Taxation Ruling TR 92/1 explains when a Ruling is a public ruling and how it is binding on the Commissioner.*

contents	para
What this Ruling is about	**1**
Ruling	**2**
Date of effect	**9**
Examples	**10**

What this Ruling is about

1. This Ruling outlines the general basis on which additional tax should be calculated under sections 226G, 226H, 226J, 226K, 226L and 226M (the shortfall sections) of the *Income Tax Assessment Act 1936* (ITAA).

Ruling

2. Additional tax under the shortfall sections is calculated in respect of a tax shortfall or part of a tax shortfall. While a tax shortfall is broadly the difference between the tax properly payable by a taxpayer and the lowest amount of tax that would have been payable by the taxpayer if it were assessed on the basis of the taxpayer's return, a tax shortfall will frequently need to be split into its component parts to determine the correct application of the shortfall sections.

3. The examples below illustrate the calculations to be followed in applying shortfall sections. The examples recognise that in the course of an audit a tax officer may detect a number of items that require adjustment, some of which may warrant penalty at different rates, some of which may not. In addition, there may be adjustments made in a taxpayer's favour which may or may not relate to the debit adjustments made. Further, the adjustments may be to income, deductions, rebates, foreign tax credits or offsets of franking deficit tax.

4. The basic rule is that if there is no tax shortfall for a year then additional tax cannot be imposed. For example, if a taxpayer has

omitted an amount of income, but the tax related to that matter is more than offset by an adjustment in the taxpayer's favour (whether or not related to the omitted income), no additional tax would be payable. Accordingly, the examples below only cover situations where, after the various adjustments to the taxpayer's assessment, there is a tax shortfall. Although all of the examples assume that the taxpayer was taxable to start with, the same principles for calculating penalty would apply where a taxpayer had originally returned a loss, provided there was in fact a tax shortfall after all adjustments had been made.

5. Where a taxpayer is in a loss situation and the audit adjustments made cause the taxpayer to become taxable, the process for calculating penalties on a tax shortfall is identical to that where the taxpayer was in a taxable situation before adjustments are made. That is, each matter that results in a tax shortfall is examined separately to determine which prescribed rate should be applied to that matter in view of the taxpayer's demonstrated behaviour. Once the appropriate prescribed rates are determined they are applied to the tax shortfall or part thereof in the same ratio as each individual shortfall is to the total tax shortfall. In other words, the prescribed rates are applied to the tax shortfall or part thereof on a pro-rata basis.

6. The pro rata basis of apportioning a tax shortfall where there are multiple debit adjustments to tax payable is considered to be the most practical methods for apportioning a tax shortfall given the number of permutations that can arise. For example, some adjustments may attract penalty, while others may not. Adjustments could attract penalties at different rates. Some adjustments may be subject to further penalty tax under section 226X, while others could attract reduced penalty tax under sections 226Z and 226ZA. While other methods for apportioning a tax shortfall may be possible, they were considered to need more complex calculations where some of the permutations mentioned are present. For this reason, the pro rata method of apportionment was preferred.

7. The examples below are assumed to be in respect of assessments for the 1992-93 year of income for a resident individual taxpayer. The principles illustrated apply equally to the calculation of penalty under the shortfall sections for other categories of taxpayers.

8. Other rulings dealing with the imposition of additional tax are:

- TR 94/2 Transitional arrangements for 1992-93 substituted accounting periods;
- TR 94/4 Reasonable care, recklessness and intentional disregard;
- TR 94/5 Reasonably arguable;
- TR 94/6 Voluntary disclosures; and

- TR 94/7 Exercise of the Commissioner's discretion to remit penalty.

Date of effect

9. This Ruling sets out the current practice of the Australian Taxation Office and is not concerned with a change in interpretation. Consequently, it applies from the date on which the shortfall sections commenced to operate.

Examples

10. The examples below are based on combinations of the following income/rebate/credit adjustments, except for Example F which deals with a taxpayer in a loss situation. The abbreviations listed below are also used in the following examples:

TAXABLE INCOME AS RETURNED / ASSESSED (i.e. the Statement Tax)	(TIAR/A)	35,000
INCOME UNDERSTATED No. 1 (caused by recklessness - penalty 50%)	(IU No.1)	1,000
INCOME UNDERSTATED No. 2 (caused by lack of reasonable care - penalty 25%)	(IU No.2)	2,000
INCOME UNDERSTATED No. 3 (not culpable - no penalty)	(IU No.3)	500
INCOME OVERSTATED (OVERSTATEMENT OF INCOME UNRELATED TO THE UNDERSTATEMENTS)	(IO)	(300)
REBATE/CREDIT OVERSTATED No. 1 (caused by recklessness - penalty 50%)	(R/CO No.1)	500
REBATE/CREDIT OVERSTATED No. 2 (caused by lack of reasonable care - penalty 25%)	(R/CO No.2)	1,000
REBATE/CREDIT UNDERSTATED (UNDERSTATED REBATE/CREDIT UNRELATED TO OTHER REBATE/CREDIT MISSTATEMENTS)	(R/CU)	(400)

NOTES:

- for the purpose of calculating tax shortfalls in the following examples, the medicare levy is calculated at 1.25%, not 1.4% which applies from 1 July 1993;

- "credits" for penalty purposes are foreign tax credits under Divisions 18, 18A and 18B of Part III of the ITAA, and offsets of franking deficit tax;

- for the purpose of calculating tax shortfalls in the following examples, 1992-93 resident individual rates of tax have been used;

- for the purpose of calculating interest in the following examples, the tax is assumed to have been avoided for a period of one year, and the rate of interest for the purpose of section 170AA of the ITAA is assumed to be 9.6% for that whole year.

EXAMPLE A:

INCOME INCREASE

TAXABLE INCOME AS RETURNED / ASSESSED	(TIAR/A)	35,000
INCOME UNDERSTATEMENT No. 1 (penalty 50%)	(IU No.1)	1,000
INCOME UNDERSTATEMENT No. 2 (penalty 25%)	(IU No.2)	2,000
INCOME UNDERSTATEMENT No. 3 (no penalty 0%)	(IU No.3)	500
INCOME OVERSTATED (UNRELATED OVERSTATEMENTS)	(IO)	(300)

TIAR/A			35,000
Less IO			300
			34,700
Plus Net Debit Adjustment			
IU No.1	1,000		
IU No.2	2,000		
IU No.3	500		
	3,500		3,500
Amended Taxable Income (ATI)			38,200

Tax Shortfall

Tax on ATI of $38,200	9,886	(i.e. Proper Tax)
Less		
Tax on TIAR/A of $35,000	8,494	(i.e. Statement Tax)
Plus		
Medicare Levy Adjustment	40	([38,200 - 35,000] x 1.25%)
Tax Shortfall	1,432	

Allocation of Tax Shortfall to Income Misstatements

IU No.1	IU No.2	IU No.3
1,000 x 1,432	2,000 x 1,432	500 x 1,432
3,500	3,500	3,500
= 409.14	= 818.28	=204.57

Penalties

IU No.1	IU No.2	IU No.3
50% flat	25% flat	no penalty
409.14 x 50%	818.28 x 25%	
= 204.57	= 204.57	

Total Penalties = 204.57 + 204.57 = $409.14

Interest

1432 x 9.6% = $137.47 (deductible)

EXAMPLE B:

REBATE/CREDIT REDUCTION

TAXABLE INCOME AS RETURNED / ASSESSED	(TIAR/A)	35,000
REBATE/CREDIT OVERSTATED No. 1 (penalty 50%)	(R/CO No.1)	500
REBATE/CREDIT OVERSTATED No. 2 (penalty 25%)	(R/CO No.2)	1,000
REBATE/CREDIT UNDERSTATED (UNRELATED UNDERSTATED REBATE)	(R/CU)	(400)
TIAR/A		35,000
Amended Taxable Income (ATI)		35,000

Tax Shortfall

Tax on ATI of $35,000		8,494
Less	Tax on TIAR/A of $35,000	8,494
		0
Plus	R/CO No.1	500
	R/CO No.2	1,000
		1,500
Less	R/CU	400
Tax Shortfall		1,100

Allocation of Tax Shortfall to Rebate/Credit Misstatements

R/CO No.1	R/CO No.2
500 x 1,100	1,000 x 1,100
1,500	1,500
= 366.66	= 733.33

Penalties

R/CO No.1	R/CO No.2
50% flat	25% flat
366.66 x 50%	733.33 x 25%
= 183.33	= 183.33

Total Penalties = 183.33 + 183.33 = $366.66

Interest

1,100 x 9.6% = $105.60 (deductible)

EXAMPLE C

INCOME INCREASE, REBATE/CREDIT INCREASE

TAXABLE INCOME AS RETURNED / ASSESSED	(TIAR/A)	35,000
INCOME UNDERSTATED No. 1 (penalty 50%)	(IU No.1)	1,000
INCOME UNDERSTATED No. 2 (penalty 25%)	(IU No.2)	2,000
INCOME UNDERSTATED No. 3 (no penalty)	(IU No.3)	500
INCOME OVERSTATED No. 4 (UNRELATED OVERSTATEMENT)	(IO)	(300)
REBATE/CREDIT UNDERSTATED (UNRELATED UNDERSTATED REBATE)	(R/CU)	(400)

TIAR/A			35,000
Less IO			300
			34,700
Plus Net debit adjustment			
	IU No.1	1,000	
	IU No.2	2,000	
	IU No.3	500	
		3,500	3,500
Amended Taxable Income (ATI)			38,200

Tax Shortfall

Tax on ATI of $38,200		9,886
Less	Tax on TIAR/A of $35,000	8,494
		1,392
Plus	Medicare Levy Adjustment	40
Less	Unrelated Rebate (R/CU)	(400)
Tax Shortfall		1,032

Allocation of Tax Shortfall to Income Misstatements

IU No.1	IU No.2	IU No.3
1,000 x 1,032	2,000 x 1,032	500 x 1,032
3,500	3,500	3,500
= 294.85	= 589.71	= 147.42

Penalties

U No.1	IU No.2	IU No.3
50% flat	25% flat	no penalty
294.85 x 50%	589.71 x 25%	
= 147.42	= 147.42	

Total Penalties = 147.42 + 147.42 = $294.84

Interest
1,032 x 9.6% = $99.07 (deductible)

EXAMPLE D

INCOME INCREASE, REBATE/CREDIT REDUCTION

TAXABLE INCOME AS RETURNED / ASSESSED	(TIAR/A)	35,000
INCOME UNDERSTATED No. 1 (penalty 50%)	(IU NO.1)	1,000
INCOME UNDERSTATED No. 2 (penalty 25%)	(IU No.2)	2,000
INCOME UNDERSTATED No. 3 (no penalty)	(IU No.3)	500
INCOME OVERSTATED (UNRELATED OVERSTATEMENT)	(IO)	(300)
REBATE/CREDIT OVERSTATED No. 1 (penalty 50%)	(R/CO No.1)	500
REBATE/CREDIT OVERSTATED No. 2 (penalty 25%)	(R/CO No.2)	1,000
REBATE/CREDIT UNDERSTATED (UNRELATED UNDERSTATED REBATE)	(R/CU)	(400)

TIAR/A		35,000
Less OI		300
		34,700
Plus Net debit adjustment		
IU No.1	1,000	
IU No.2	2,000	
IU No.3	500	
	3,500	3,500
Amended Taxable Income (ATI)		38,200

Tax Shortfall

Tax on ATI of $38,200	9,886
Less	
Tax on TIAR/A of $35,000	8,494
	1,392
Plus	
Medicare Levy Adjustment	40
	1,432
Plus	
R/CO No.1	500
R/CO No. 2	1,000
R/CU	(400)
	1,100
Tax Shortfall	2,532

Allocation of Tax Shortfall to Income and Rebate/Credit Misstatements

IU No.1
1,000 x 1,432
3,500
= 409.14

IU No.2
2,000 x 1,432
3,500
= 818.28

IU No.3
500 x 1,432
3,500
= 204.57

R/CO No.1
500 x 1,100
1,500
= 366.66

R/CO No.2
1,000 x 1,100
1,500
= 733.33

Penalties

IU No.1
50% flat
409.14 x 50%
= 204.57

IU No.2
25% flat
818.28 x 25%
= 204.57

IU No.3
no penalty

R/CO No.1
50% flat
366.66 x 50%
= 183.33

R/CO No.2
25% flat
733.33 x 25%
= 183.33

Total Penalties = 204.57 + 204.57 + 183.33 + 183.33 = $775.80

Interest

2532 x 9.6% = $243.07 (deductible)

EXAMPLE E

INCOME REDUCTION, REBATE/CREDIT REDUCTION

TAXABLE INCOME AS RETURNED / ASSESSED	(TIAR/A)	35,000
INCOME OVERSTATED	(IO)	(300)
REBATE/CREDIT OVERSTATED No. 1 (penalty 50%)	(R/CO No.1)	500
REBATE/CREDIT OVERSTATED No. 2 (penalty 25%)	(R/CO No.2)	1,000
REBATE/CREDIT UNDERSTATEMENT (UNRELATED UNDERSTATED REBATE)	(R/CU)	(400)

TIAR/A	35,000
Less IO	300
Amended Taxable Income (ATI)	34,700

Tax Shortfall

Tax on ATI of $34,700		8,380
Less Tax on TIAR/A of $35,000		8,494
		(114)
Less Medicare Levy Adjustment		(3.75)
		(117.75)
Plus R/CO No.1	500	
R/CO No.2	1,000	
	1,500	1,500.00
		1,382.25
Less R/C U		400.00
Tax Shortfall		982.25

Allocation of Tax Shortfall to Rebate/Credit Misstatements

R/CO No.1	R/CO No.2
500 x 982.25	1,000 x 982.25
1,500	1,500
= 327.41	= 654.83

Penalties

R/CO No.1	R/CO No.2
50% flat	25% flat
327.41 x 50%	654.83 x 25%
= 163.70	= 163.70

Total Penalties = 163.70 + 163.70 = $327.40

Interest

982.25 x 9.6% = $94.29 (deductible)

EXAMPLE F

INCOME INCREASE (IN A LOSS SITUATION)

TAXABLE INCOME AS RETURNED / ASSESSED	(TIAR/A)	(15,000)
INCOME UNDERSTATEMENT No. 1 (penalty 50%)	(IU No.1)	10,000
INCOME UNDERSTATEMENT No. 2 (penalty 25%)	(IU No.2)	18,000
INCOME UNDERSTATEMENT No. 3 (no penalty)	(IU No.3)	1,500
INCOME OVERSTATED (UNRELATED OVERSTATEMENTS)	(IO)	(300)

TIAR/A		(15,000)
Add IO		(300)
		(15,300)
Plus Net Debit Adjustment		
IU No.1	10,000	
IU No.2	18,000	
IU No.3	1,500	
		29,500
Amended Taxable Income (ATI)		14,200

Tax Shortfall

Tax on ATI of $14,200	1,760	
Less		
Tax on TIAR/A of $(15,000)	NIL	
Plus		
Medicare Levy Adjustment	177.50	(14,200 x 1.25%)
Tax Shortfall	1,937.50	

Allocation of Tax Shortfall to Income Misstatements

IU No.1	IU No.2	IU No.3
10,000 x 1,937.50	18,000 x 1,937.50	1,500 x1 ,937.50
29,500	29,500	29,500
= 656.78	= 1,182.20	= 98.52

Penalties

IU No.1	IU No.2	IU No.3
50% flat	25% flat	no penalty
656.78 x 50%	1,182.20 x 25%	
= 328.39	= 295.55	

Total Penalties = 328.39 + 295.55 = $623.94

Interest

1,937.50 x 9.6% = $186.00 (deductible)

Commissioner of Taxation

6 January 1993

ISSN 1039 - 0731

ATO references
NO 93/2071-7
BO

Previously released in draft form
as TR 93/D19

Price $1.20

FOI index detail
reference number
I 1014104

subject references
- additional tax
- calculation
- self assessment
- tax shortfall

legislative references
- ITAA 170AA; ITAA 226G; ITAA 226H; ITAA 226J; ITAA 226K; ITAA 226L; ITAA 226M