IT 2172 - Tax instalment deductions (paye) - remission of penalties - failure to deduct

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TAXATION RULING NO. IT 2172

TAX INSTALMENT DEDUCTIONS (PAYE) - REMISSION OF PENALTIES - FAILURE TO DEDUCT

F.O.I. EMBARGO: Edited for FOI Purposes

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I 1187286	FAILURE TO MAKE DEDUCTIONS FROM SALARY OR WAGES : PENALTY IMPOSITION AND REMISSION	221EAA 221N

PREAMBLE Where an employer, other than a government body, pays salary or wages to an employee without first making a deduction that is required to be made in accordance with section 221C, the employer is liable to a penalty pursuant to sub-section 221EAA(1). This is a new section which came into operation on 14 December 1984 and replaces a similar provision formerly in section 221N. This provision automatically comes into effect as soon as there has been a failure or refusal to deduct the relevant amount, i.e., there has been an under deduction or a complete failure to deduct. Section 221EAA applies only to failure to deduct situations that occur on or after 14 December 1984. The now repealed section 221N applies to those instances of failure to deduct that occurred prior to 14 December.

2. This ruling provides guidelines for the exercise of the Commissioner's discretion under section 221N to remit the statutory penalties imposed by section 221EAA. In providing these guidelines there is no intention of laying down any conditions which may restrict a Deputy Commissioner in exercising his discretion. The guidelines provided in this ruling supersede all previous guidelines issued. To the extent that earlier rulings or guidelines are intended to be retained, they have been incorporated in this ruling. The guidelines in this ruling have been dealt with under the following headings :

(i) determination of the undeducted amount;

(ii) calculation of penalty;

(iii) flat penalty;

(iv) late payment penalty; and

(v) other matters.

3. There are two components to the statutory penalty referred to in the above paragraphs. The first, imposed by paragraph 221EAA(1)(a), is an amount equal to the amount the

employer failed to deduct (the undeducted amount). For reasons which he thinks sufficient the Commissioner is able to remit the whole or any part of this fixed element of the penalty (sub-section 221N(2)). Paragraph 221EAA(1)(b) imposes the second component (the late payment element). This component is an amount equal to 20% per annum of so much of the undeducted amount as remains unpaid, calculated from the date when the deduction, if it had been made as required, should have been paid. A power to remit this late payment element of the penalty is available under sub-section 221N(1) in circumstances that parallel those in sub-section 207(1A) which provides for remission of additional tax imposed on unpaid income tax.

4. Where an employer, being a government body other than the Commonwealth, pays salary or wages without first making a deduction as required, the employer is liable to a penalty pursuant to sub-section 221EAA(2).

5. The penalty referred to in paragraph 4 above is an amount equal to 20% per annum of the undeducted amount calculated in respect of the period commencing on the day on which the employer should have made the deduction and ending on 30 June in the financial year in which that day occurred.

6. In the absence of extenuating circumstances, such as those outlined in paragraphs 22-24 of this ruling, the full amount of the penalty as provided by the legislation should be allowed to stand for government body employers. Of course, where extenuating circumstances exist, the same considerations should be given to a government body employer as would apply to a non-government body employer. Any request for remission of penalty pursuant to sub-section 221EAA(2) must be considered under the provisions of sub-section 221N(2).

RULING Determination of the Undeducted Amount

7. In determining the quantum of the undeducted amount for the purpose of deciding the level of penalty, consideration should be given to the cost effectiveness of the examination required to establish all relevant details. As a general rule, an inspection examination covering would be seen as normal.

8. Extension of the normal examination period should be limited, and should not be considered warranted without first having regard to whether :

(a) aggravating factors are present;

(b) substantial undeducted amounts have come to light from an examination covering (or a lesser period);

(c) any non-deduction detected during the examination period is likely to be absolved in part or full due to extenuating circumstances; or

(d) .

9. For the purpose of deciding whether to extend the initial examination period, it is considered that substantial undeducted amounts should be seen as those exceeding .

10. Regarding the duration of an extended examination period it has been decided that a further period of , represents the best balance between the need to ensure that the level of penalty imposed is an adequate deterrent to further offences, but at the same time is not too harsh, and the need to be conscious of the time and effort required to extend examinations. Only in extreme circumstances should the examination period be further extended.

11. Accordingly, where aggravating factors are present or an initial examination discloses undeducted amounts in excess of and there are no extenuating circumstances, the examination is to be extended, wherever practicable, to cover a six month period or the period from when the employer was previously prosecuted, penalised or warned, whichever is the lesser period.

Calculation of Total Penalty

12. In calculating the penalty to be imposed for failure to deduct there are two base amounts which must be taken into account, viz:

X - the undeducted amount; and

Y - the undeducted amount which remains unpaid.

13. Using these codes, the formula for calculation of penalty in respect of failure to deduct can be expressed as follows:

FLAT COMPONENT		LATE PAYMENT COMPONENT
X	+	$\frac{20}{100} \times \frac{n}{365} \times Y$

Note: Y = X in all cases, except where part payment of X has been made;

and

n = the number of days late, computed from the expiration of the period within which the amount that the employer failed to deduct would have been required to be paid to the Commissioner to the date of payment .

14. The reference in paragraph 221EAA(1)(b) to "so much of the undeducted amount as remains unpaid" has been interpreted to mean (subject to any payments made) that amount of flat penalty remaining unpaid after remission.

Flat Penalty

15. The discretion under sub-section 221N(2) to remit amounts payable under paragraph 221EAA(1)(a) is to be exercised in accordance with the following guidelines.

Basic Penalty

16. Unless there are aggravating factors (see paragraph 18) or extenuating circumstances (see paragraph 22), the statutory penalty is to be reduced to a basic penalty of 40% of the "undeducted amount" in all cases of failure to deduct falling within paragraph 221EAA(1)(a). This basic penalty assumes a reasonable degree of co-operation with official enquiries and is considered to be appropriate having regard to the following factors:

(a) it represents an effective deterrent so as to ensure that there is maximum compliance with the requirement to deduct tax at source;

(b) the penalty ensures that the employer is encouraged to ascertain his obligations while, at the same time, sufficient "penal" flexibility exists to take account of the different circumstances which will be encountered;

(c) employers who do not comply will not be seen to be benefitting economically at the expense of those who do. By imposing a minimum or base penalty for all cases of non-deduction, the incentive for risking detection by the Taxation Office is reduced; and

(d) the basic penalty aligns with the rate of penalty imposed for non-deduction under the prescribed payments system thereby facilitating comparable treatment for comparable offences.

17. The basic penalty and minimum inspection period, therefore, should be adjusted according to whether aggravating or extenuating circumstances are present.

Aggravating Factors

18. The basic penalty is to be increased by a further percentage of the undeducted amount, depending on the degree of seriousness of the particular offence but within the range of percentages indicated, for each of the following circumstances that exist:

(a) Deliberate steps have been taken, either before or after commencement of official enquiries, to conceal the true character of an employment arrangement or the identity of an employee - 20% to 50%.

(b) The above steps may be construed as involving corruption of, or collusion with, an employee - 20% to 50%.

(c) The employer has on a previous occasion been warned in writing, penalised or prosecuted for failure to make tax instalment deductions - 20% to 50%.

(d) The degree of co-operation is less than "reasonable" or such as to cause excessive delay in the completion of official enquiries - 20% to 50%.

19. In determining the level of penalty each of the aggravating factors listed above should be considered separately. The actual percentage selected from the range 20% to 50% should reflect the degree of culpability or, in the case of (d), resistance to official enquiries. It is expected that the greater part of these offences would fall within the 20% to 30% range with the higher end of the range being reserved for the most extreme cases.

20. Regarding item (c), which is concerned with the commission of previous offences, it is considered that the current offence under consideration should be treated as warranting a penalty greater than the basic penalty only if the prior warning, penalty or prosecution occurred within the previous 2 years.

21. Care should, of course, be exercised to ensure that the penalty calculated in accordance with the above guidelines does not exceed the statutory maximum of 100% of the undeducted amount.

Extenuating Circumstances

22. The basic penalty may be decreased in extenuating circumstances. It is not possible to specify all those situations where it is considered that further remission is warranted but in broad terms they will be situations where, more often than not because of a combination of circumstances rather than a single circumstance, the employer's offence is considered wholly or substantially excusable. Thus, while no one factor such as carelessness, ignorance, serious ill health or advanced age would normally warrant further remission, the presence of two or more such factors might well amount to extenuating circumstances warranting a reduction in penalty.

23. Subject to these comments, circumstances where a further remission would be warranted would include cases where

it is clear that -

(i) the employer's offence was occasioned by carelessness of a less serious nature and there are other mitigating factors, e.g., advanced age or serious illness, which excuse the carelessness to a substantial extent;

(ii) the employer's offence was occasioned by ignorance of the law in the sense that, in the particular circumstances, the employer could not reasonably be expected to have been aware of the requirements in question;

(iii) the employer has made a genuine and excusable mistake in interpreting the law, i.e., there was a genuine belief by the employer that deductions were not required;

(iv) there is a serious and genuine dispute as to whether the employee is in fact an employee or a sub-contractor and accordingly whether deductions should have been made under the PAYE System or the Prescribed Payment System or neither; or

(v) the effect of the penalty, having regard to the employer's net assets and his potential earning capacity, would be such as to amount to a "ruinous imposition", i.e., leave the employer with little or no remaining assets.

24. In cases such as these the circumstances will have been considered sufficient to warrant a further reduction of the penalty on the grounds that the employer's offence is wholly or substantially excusable. In the former case, i.e., where the offence is considered substantially, but not wholly, excusable a reduction in the basic penalty to, say, 20% might be appropriate. In the latter case, where the circumstances are such that the employer's offence is wholly excusable, the whole of the penalty may be remitted.

Late Payment Penalty

Level Of Penalty To Be Imposed In The First Instance

25. The penalty for failure to deduct comprises a flat penalty in respect of the offence itself, and a per annum penalty to take account of the delay in collecting the revenue. The comments below relate only to the level of the late payment component to be imposed in the first instance, which will be additional to the amount of flat penalty as provided for in the preceding guidelines.

26. In deciding the level of late payment penalty in respect of an undeducted amount, any consideration of the employer holding trust moneys on behalf of employees is obviously not relevant.

27. The paramount consideration in this situation is the loss incurred by the Government by not having moneys, which should have been deducted and remitted, available for use. The question to be answered therefore is whether there should be any remission of the per annum component.

28. As indicated previously, remission of the late payment penalty component for failure to deduct and for failure to pay is provided for under the same sub-section, i.e., sub-section 221N(1). In summary, for a remission to be granted, the employer must be able to demonstrate, firstly, that because of certain circumstances he was unable to pay the deductions when they fell due and, secondly, that he has made all reasonable efforts to mitigate, or mitigate the effects of, those circumstances. Alternatively, remission may be granted where there are special circumstances considered by the Commissioner to warrant it.

29. There is some difficulty in applying the legislative remission guidelines based on circumstances contributing to a "delay in payment" in a failure to deduct situation. The fact is that nothing caused the delay in payment other than the employer's failure to deduct amounts as required. Accordingly, it would seem more appropriate to consider remission in terms of the factors which led to the failure to deduct.

30. In this regard, and bearing in mind that the flat penalty component to be imposed already provides for a partial remission based on the circumstances surrounding the failure to deduct, it has been decided that the per annum component should generally be allowed to stand in full, i.e., 20% per annum of the flat component deemed payable after remission. This would also be consistent with the policy as suggested for failure to pay.

Requests For Remission Of Penalty After Imposition

31. As the circumstances warranting remission would normally be evident at the time of raising the penalty and bearing in mind that these circumstances would have been taken into account in determining the level of flat penalty on which the per annum component is based, it is suggested that no further remission of the per annum component be granted. If it transpires, as a result of a request for remission, that the flat penalty is to be reduced, the per annum penalty would also be reduced as a direct consequence of the calculation formula. Where the flat penalty is remitted in full, no per annum penalty would be payable.

Other matters

32. To enable the extent of penalty remissions to be determined by supervisors, officers are required to comment specifically and separately in their reports and penalty submissions on the extent to which aggravating factors or extenuating circumstances exist. In determining the extent of penalty remissions, approving officers exercising the

Commissioner's discretion should clearly state the reasons for their decisions. This action will be necessary for the proper investigation of complaints regarding penalties by, or on behalf of, employers and for Head Office monitoring purposes.

33. Where a decision is made to remit part only, or not to remit any part, of the statutory penalty, approving officers should ensure that the employer is notified in writing of the decision. Officers preparing penalty submissions and approving officers are to ensure that decisions concerning the remission of penalty are made promptly.

34. Where the whole of the statutory penalty is remitted, approving officers should ensure that the employer is notified in writing of the decision and warned that any similar offences in the future will not necessarily result in a full remission.

COMMISSIONER OF TAXATION
9 July 1985