PS LA 2007/22 - Remission of penalty for failure to withhold as required by Division 12 of Schedule 1 to the Taxation Administration Act 1953

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This document has changed over time. This version was published on *29 August 2007*

Generated on: 4 November 2026, 10:48:07 PM

Australian Government
Australian Taxation Office

Practice Statement Law Administration

PS LA 2007/22

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FOI status: may be released

This practice statement is issued under the authority of the Commissioner of Taxation and must be read in conjunction with Law Administration Practice Statement PS LA 1998/1. It must be followed by Tax Office staff unless doing so creates unintended consequences or is considered incorrect. Where this occurs Tax office staff must follow their business line's escalation process.

SUBJECT: Remission of penalty for failure to withhold as required by Division 12 of Schedule 1 to the *Taxation Administration Act 1953*

PURPOSE: This practice statement sets out guidelines for the remission of penalty for failure to withhold as required by Division 12 of Schedule 1 to the *Taxation Administration Act 1953*

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SCOPE

1. This practice statement sets out guidelines for the remission of penalties imposed under section 16-30 of Schedule 1 to the *Taxation Administration Act 1953* (the TAA) for failure to withhold an amount as required by Division 12 of Schedule 1 to the TAA (Division 12). These guidelines are split according to the type of failure to withhold:

   (a) failures to withhold amounts as required by Division 12 (except Subdivision 12-F) of Schedule 1 to the TAA from

   - payments for work and services
   - retirement payments, eligible termination payments and annuities
   - benefit and compensation payments
   - payments where a tax file number or Australian Business Number is not quoted
   - superannuation payments paid to a person that has departed Australia[1]
   - certain payments to foreign residents
   - payments in respect of mining on Aboriginal land, and natural resources.

   These guidelines are contained in paragraphs 18 to 38 of this practice statement.

   (b) failure to withhold amounts as required by Subdivision 12-F of Schedule 1 to the TAA from

   - dividend, interest and royalty payments to overseas persons.

   These guidelines are contained in paragraphs 43 to 47 of this practice statement.

2. This practice statement covers failure to withhold penalties imposed on a payer other than an 'exempt Australian government agency'.[2]

3. This practice statement relates to penalties imposed after 22 June 2006, subject to the exception noted in paragraph 5 below. Separate practice statements and rulings, listed below, apply for penalties imposed before 23 June 2006.

Remission of penalty amounts imposed before 23 June 2006

Payments made from 1 July 2002

4. Law Administration Practice Statement PS LA 2003/11[3] applies in respect of remission of failure to withhold penalties that relate to payments made from 1 July 2002 where the penalty has been imposed before 23 June 2006.

[1] In accordance with the definition in section 27A(1) of the *Income Tax Assessment Act 1936*

[2] 'Exempt Australian government agency' is defined in section 995-1 of the *Income Tax Assessment Act 1997* (ITAA 1997). Section 16-35, section 16-40 and section 16-43 of Schedule 1 to the TAA impose failure to withhold penalties on exempt Australian government agencies.

[3] PS LA 2003/11 Remission of penalty for failure to withhold as required by Division 12 of Schedule 1 to the *Taxation Administration Act 1953.*

Payments made from 1 July 2000 to 30 June 2002

5. Law Administration Practice Statement PS LA 2002/8[4] applies in respect of remission of failure to withhold penalties that relate to payments made from 1 July 2001 to 30 June 2002. However, where a tax officer determines from the guidelines in PS LA 2002/8 that the failure to withhold penalty will not be remitted in full,[5] the tax officer may refer to the guidelines in paragraphs 26 to 47 of this practice statement for guidance on the level of remission.[6]

6. Law Administration Practice Statement PS LA 2000/9[7] applies in respect of remission of failure to withhold penalties that relate to payments made from 1 July 2000 to 30 June 2001.

Payments made before 1 July 2000

7. Before 1 July 2000, an entity who made payments that fell within the ambit of the reportable payments system (RPS), the pay as you earn (PAYE) system or the prescribed payments system (PPS) was required to deduct tax instalments from those payments and remit the tax instalment deductions to the Commissioner.

8. Taxation Ruling TR 2000/3[8] (now withdrawn) applied in respect of remission of failure to deduct penalties that relate to payments made between 1 July 1999 and 30 June 2000.

9. Taxation Ruling TR 97/8[9] (now withdrawn) applied in respect of remission of failure to deduct penalties that relate to payments made before 1 July 1999.

STATEMENT

10. The Commissioner may remit all or part of a penalty imposed by section 16-30 of Schedule 1 to the TAA (the penalty) pursuant to the discretion contained in section 298-20 of Schedule 1 to the TAA. The decision to remit the penalty amount (the remission decision) should be made before the penalty notice is issued and will be based on the circumstances of the case under consideration and the entity's behaviour.

11. A decision to remit all or part of the penalty under subsection 298-20(1) of Schedule 1 to the TAA should be made with regard to the following objectives of the penalty regime:

    - decisions should be made based on the individual circumstances of the case
    - decisions should be consistent with the principles of the taxpayers' charter and the compliance model

[4] PS LA 2002/8 Administration of penalties under the new tax system.
[5] For example where the entity's skills and experience indicate that it is reasonable to conclude that the entity should have been aware of their withholding obligation. See paragraph 60 of PS LA 2002/8.
[6] PS LA 2002/8 does not provide guidance on levels of remissions for PAYG withholding penalties.
[7] PS LA 2000/9 Remission of penalties under the new tax system.
[8] TR 2000/3 Income tax: remission of penalty and General Interest Charge for failure to make deductions from RPS, PAYE and PPS payments.
[9] TR 97/8 Income tax: RPS, PAYE and PPS remission of penalty for failure to deduct tax.

- to promote consistent treatment, penalties imposed should not be remitted without just cause or arbitrarily. The Commissioner must ensure that the decision to remit in part or in full or not to remit at all is made in good faith and is reasonable. All relevant matters and no irrelevant matters must be taken into consideration in making the decision, and
- the discretion to remit penalties should be administered in a fashion to effect improvements to future compliance by payer entities and to provide certainty for those entities. These objectives should be achieved without causing unintended or unjust results.

12. An important principle contained in the taxpayers' charter and the compliance model is that the Commissioner will adopt a fair and reasonable approach in his administration of the tax system, and in doing so, will take into consideration the issues faced by entities in meeting their obligations. This principle applies to decisions on penalties, in the same way as it applies to any other decision that the Commissioner may make which affects an entity.

13. It is also important to understand that the pay as you go (withholding) (PAYG(W)) provisions constitute a collection system, rather than a tax. Therefore, a failure to withhold the required amount does not, in itself, necessarily result in a loss to the revenue, unlike a tax shortfall. If PAYG(W) is not withheld by the payer, the loss to the revenue will arise:

    (i) in the case of dividend, interest or royalty payments to overseas persons – if the payee does not otherwise pay the tax, and

    (ii) in other cases – upon the assessment of the payee's tax liability if the payee omits the income from their income tax return.

14. In making a remission decision in relation to penalties imposed for a failure to withhold under Division 12 (except Subdivision 12-F) of Schedule 1 to the TAA, tax officers should consider the factors outlined at paragraphs 18 to 38 of this practice statement.

15. In making a remission decision in relation to penalties imposed for a failure to withhold under Subdivision 12-F of Schedule 1 to the TAA, tax officers should consider the factors outlined at paragraphs 43 to 47 of this practice statement.

16. Tax officers must give written notice to the entity of the entity's liability to pay the penalty and of the reasons why the entity is liable to pay the penalty. The tax officer may do so in any other notice he or she gives to the entity but is not required to give reasons if he or she decides to remit the entire penalty. If the officer decides to remit none or only part of the penalty they must give to the entity written notice of that decision and the reasons for it (subsections 298-10 and 298-20 of Schedule 1 to the TAA).

17. Tax officers making remission decisions should record the following information on the appropriate information technology system:

- relevant facts relating to the failure to withhold
- the remission decision (that is, the level of penalty remission and relevant calculations)
- the reasons for the decision (that is, the tax officer's consideration of the circumstances relevant to the decision)
- the written notice of the remission decision given to the entity, and

- any other relevant information.

EXPLANATION

Failures to withhold under Division 12 (except Subdivision 12-F) of Schedule 1 to the TAA

18. The PAYG(W) system is contained in Part 2-5 of Schedule 1 to the TAA. Division 12 of this Part requires an entity (the payer) to withhold an amount from certain payments made to an individual or other entity (the payee).

19. Section 16-70 of Schedule 1 to the TAA requires the entity to pay amounts withheld to the Commissioner.

20. No administrative penalty applies where an entity withholds an amount from a payment as required, notifies the Commissioner of the amount as required, but fails to pay this amount to the Commissioner by the due date. However, the general interest charge (GIC) will apply to these late payments (section 16-80 of Schedule 1 to the TAA).

21. An entity that fails to withhold an amount as required by Division 12 is liable to a penalty equal to the amount that the entity failed to withhold (section 16-30 of Schedule 1 to the TAA).

22. Although the penalty amount is equal to the amount that the entity should have withheld, it should be emphasised that statutorily it is a penalty, not a means of collecting amounts that should have been withheld from payments. In most cases, payees are not entitled to a credit where their payer did not withhold an amount from their payments, even if their payer has paid a penalty amount for failure to withhold.[10]

23. The penalty amount is payable on the date specified on the notice given to an entity advising them of their liability to pay the penalty. This date must be at least 14 days after the notice is given to an entity (section 298-15 of Schedule 1 to the TAA).

24. If the penalty amount remains unpaid after it is due, the entity is also liable to a GIC on the unpaid penalty amount (section 298-25 of Schedule 1 to the TAA).

25. The Commissioner has the discretion to remit all or part of the GIC to which an entity is liable (section 8AAG of the TAA). An entity may request that the GIC be remitted; however, the onus is on the entity to show that remission is warranted. Tax officers making decisions on the remission of the GIC should do so in accordance with the guidelines in PS LA 2006/11 ATO Receivables Policy.

Factors to consider when making a remission decision

26. The main features of our approach to remission of penalties for failure to withhold are:

    - the remission levels deal with a range of behaviours varying from a voluntary disclosure to a deliberate decision not to comply

[10] Payees are only entitled to a credit on assessment for amounts withheld from withholding payments made to them during the year (section 18-15 of Schedule 1 to the TAA). This does not apply to payments made in accordance with Subdivision 12-F of Schedule 1 to the TAA.

- attempts to hide non-compliance or mislead the Tax Office result in a lower level of remission
- a voluntary disclosure is rewarded through higher remission levels, and
- a repeat occurrence results in a lower level of remission.

27. To maintain consistency with other tax penalties, the starting point for considering penalty remission is to consider the entity's conduct both at, and leading up to, the time that the failure to withhold occurred. Tax officers should determine the extent of penalty remission on a case by case basis using the remission levels shown in the table below as a guide.

Description	**Level of remission**	**Penalty Amount**
Intentional disregard An entity knowingly decides not to withhold the correct amount as required.	25%	75%
Recklessness An entity's actions demonstrate gross carelessness showing a disregard or indifference to their obligations.	50%	50%
Failure to take reasonable care An entity fails to exercise the care that a reasonable, ordinary entity would exercise to fulfil the entity's tax obligations.	75%	25%
Voluntary disclosure On their own initiative an entity brings to the attention of the Tax Office details of a payment from which they have failed to withhold the correct amount.	100%	0%

28. The reasonable care test requires an entity to take the care that a reasonable, ordinary person would take in all the circumstances of the entity to fulfil their taxation obligations. Provided that they may be judged to have tried their best to fulfil these obligations, having regard to their experience, education, skill and other relevant circumstances, the entity will be considered to have exercised reasonable care and will not be liable to pay a penalty for their failure to withhold amounts of PAYG(W).

29. The figures referred to in the above table are percentages of the amount that the entity failed to withhold. These levels of remission are a starting point before taking into account additional factors which will either increase or decrease the penalty amount, based on the circumstances of the entity. See paragraphs 35 to 38 of this practice statement.

30. The terms used in the above table are not new. A full explanation of the terms 'intentional disregard', 'recklessness' and 'reasonable care' can be found in Taxation Ruling TR 94/4.[11] A full explanation of the term 'voluntary disclosure' can be found in Taxation Ruling TR 94/6.[12]

[11] Taxation Ruling TR 94/4 Income tax: tax shortfall penalties: reasonable care, recklessness and intentional disregard.
[12] Taxation Ruling TR 94/6 Income tax: tax shortfall penalties: voluntary disclosures

Voluntary disclosure

31. As stated in the table above, an entity will be considered to have made a voluntary disclosure where on their own initiative they have brought to the attention of the Tax Office details of a payment from which they have failed to withhold the correct amount.

32. A voluntary disclosure must be a true and correct written statement that contains all the material facts for it to qualify for the concessional treatment afforded to voluntary disclosures.

33. An entity will be taken to have used its own initiative in relation to making a voluntary disclosure if the disclosure is made before being told of anticipated audit action by the Tax Office.

34. However, repeated voluntary disclosures by an entity may indicate the entity is being careless. Where this is the case, the remission of penalty for voluntary disclosure should not apply.

Factors that may increase or decrease the level of penalty

35. After considering the remission levels in the table at paragraph 27 of this practice statement, the next step is for the tax officer to determine whether there are any factors that will increase or decrease the level of penalty. These are sometimes called 'aggravating'[13] or 'mitigating'[14] circumstances.

36. Factors that may increase or decrease the level of penalty should be considered and adjustments made, if appropriate, to the penalty that has been determined using the table in paragraph 27 of this practice statement.

37. The penalty should be increased by 20 per cent where an entity has failed to withhold an amount from a payment as required by Division 12 and:

- has taken steps to prevent or obstruct the Commissioner from finding out about the failure to withhold, or
- has been penalised in a previous period for failing to withhold and the tax officer considers that there has been no lasting improvement to the entity's compliance to their taxation obligations.

38. The penalty should be decreased by 20 per cent where an entity tells the Commissioner of a failure to withhold after the Commissioner has advised of an intention to conduct an audit and the disclosure can reasonably be estimated to have saved the Commissioner a significant amount of time or resources in the conduct of the audit.

39. ***Example 1***

Kevin runs a labour hire firm supplying secretaries and administrative assistants to clients. He is aware that he is required to withhold amounts of PAYG(W) from payments to the workers and admitted as much to a tax officer when queried, upon audit, of his failure to do so.

[13] Aggravating circumstances may lead to the penalty being increased.
[14] Mitigating circumstances may lead to the penalty being decreased.

Kevin has chosen to disregard his obligation to withhold amounts of PAYG(W) and has offered no explanation or reason to mitigate against a finding that he has intentionally disregarded the law. Therefore, the failure to withhold penalty is remitted by 25% from 100% to 75%.

40. ***Example 2***

Richard has recently immigrated from Eastern Europe and runs a small bakery employing two family members. He is vaguely aware of an obligation by some employers to withhold amounts of PAYG(W) from employees' wages, but had assumed that this just applied to businesses with 100 or more employees, that is, those to whom the unfair dismissal laws applied.

Upon audit, he is informed of his obligation to withhold from wages paid to any employees, and he immediately provides copies of bank statements identifying direct transfers of wages into the employees' accounts.

The tax officer takes into account Richard's lack of experience in Australian business and taxation affairs and is cognisant of the importance of encouraging him to meet his PAYG(W) obligations in future. The tax officer therefore determines that Richard's failure to withhold constituted a lack of reasonable care, warranting the remission of failure to withhold penalty by 75% from 100% to 25%.

Richard's positive co-operation upon realising his error has significantly expedited the resolution of the audit and the penalty is further reduced by 20% of 25%, that is, 5%, resulting in a final penalty of 20%.

41. ***Example 3***

Amy runs a small café and employs two full-time staff whom she pays by cheque and from whose wages she withholds amounts of PAYG(W). She also employs one part-time waitperson for the busy periods whom she pays by cash and from whose wages she does not withhold any amounts of PAYG(W).

Amy was aware that she should have been withholding amounts of PAYG(W) from the cash wages but knew that her part-time staff member would not work for her if they were required to pay tax on this income.

However, after a couple of years, she has decided to regularise her business taxation affairs and has advised her part-time staff member that PAYG(W) will be withheld in future and has also alerted the Tax Office to her past failure to withhold.

As Amy has made a voluntary disclosure that was not initiated by any notified Tax Office audit action, the failure to withhold penalty will be remitted in full.

42. Where a tax officer has considered all of the factors outlined in paragraphs 18 to 38 of this practice statement and concluded that no penalty should be remitted (for example, in cases of severe non-compliance) the case may be appropriate for referral to the Director of Public Prosecutions. See paragraph 48 of this practice statement.

Failures to withhold under Subdivision 12-F of Schedule 1 to the TAA from dividend, interest and royalty payments to overseas persons

43. Subdivision 12-F of Schedule 1 to the TAA contains specific rules about payers withholding from certain dividend, interest and royalty payments they make to overseas entities or receive for foreign residents (DIR payments). To the extent a payer fails to withhold from a DIR payment or withholds less than required, they are liable to a penalty equal to the amount that the payer failed to withhold.. However, unlike with PAYG(W) generally, if an entity has paid an amount of penalty for a withholding payment covered by Subdivision 12-F, the entity liable to pay the withholding tax, that is the payee, is entitled to a credit equal to the amount of the penalty (section 18-35 of Schedule 1 to the TAA). The total of the amounts withheld and the penalty amount (if any), if paid in full, will ordinarily result in the payee's withholding tax liability on the DIR being met, or 'paid'.

44. A payer who fails to withhold as required may seek from the Commissioner and be granted a penalty remission. Subsection 18-35(2) provides that the payee's credit is commensurately reduced by any penalty remission granted to the payer. The result in that event is to leave the payee's withholding tax liability undischarged, or 'unpaid', to that extent, notwithstanding the payer paying all of the remitted penalty amount. Further, if a payer has failed to withhold from an interest or a royalty payment (not so a dividend) and would otherwise get a tax deduction for the payment they cannot get the deduction until the withholding tax for the interest or royalty is paid (section 26-25 of the *Income Tax Assessment Act 1997*). The effect of subsection 18-35(2) is therefore that a penalty remission ordinarily precludes the interest or royalty payer getting a deduction for the payment unless the payee or payer somehow makes good the withholding tax deficiency, for example the payee makes separate payment to the Tax Office.

45. The Commissioner will not, as a matter of policy, remit a penalty for failing to withhold from an interest or royalty payment if the remission would have the effect of denying the payer a deduction otherwise available to it and the payer does not therefore agree to it. The question therefore remains of when the Commissioner would remit the failure to withhold penalty.

46. Where payers do not withhold the required amount from a DIR payment the likelihood of a loss to the revenue can be high given the jurisdictional difficulties the Commissioner may face in seeking to enforce payment of what is an Australian tax by a foreign resident payee situated in another country. Ensuring withholding tax is efficiently collected is the object of the DIR collection regime, an object that depends largely on payers properly complying with their collection obligations.

47. Consistent with that object the Commissioner's policy is that only in exceptional circumstances should officers grant a remission of penalty for failing to withhold from a DIR payment. Each case must be decided on its facts but an example where remission may be warranted is where a payer was not and could not reasonably be expected to have been aware of their proper withholding obligations. The remission rate in any particular case will again depend on the facts but, as a general proposition, the rate should reflect the fact that non-collection usually means a permanent loss to the revenue. With this in mind, remissions in excess of 10% would ordinarily be granted only in exceptional circumstances.

Prosecution

48. As an alternative to an administrative penalty for failing to withhold, the Commissioner can seek to have an offence prosecuted (section 16-25 of Schedule 1 to the TAA) by referring the matter to the Director of Public Prosecutions. The Commissioner will generally not seek to prosecute unless the case involves serious non-compliance. This is in keeping with the compliance model concept that the most severe compliance strategies are to be restricted to those who are most non-compliant. The Tax Office policy on prosecution is fully explained in the *ATO Prosecution Policy*.[15] Where prosecution action is instituted, the entity is not liable for a civil or administrative penalty for the same offence (section 8ZE of the TAA).

[15] The ATO Prosecution Policy is contained in Corporate Management Practice Statement PS CM 2007/02 Fraud control and the prosecution process.

Subject references	Failure to withhold Dividend, interest and royalties PAYG withholding Remission of penalty
Legislative references	TAA 1953 Pt IIA TAA 1953 Sch 1 Div 12 TAA 1953 Sch 1 Div 16 TAA 1953 Sch 1 Div 298
Related public rulings	IT 2246; TR 94/4; TR 94/6; TR 97/8; TR 2000/3
Related practice statements	PS LA 2000/9; PS LA 2002/8; PS LA 2003/11; PS LA 2006/2; PS LA 2007/3
Case references	
Other references	
File references	2003/014849
Date issued	8 October 2007
Date of effect	**23 June 2006**
Other Business Lines consulted	**GST, CS & C, LBI, OCTC**
Amendment history	**20 July 2011** Contact details updated **16 September 2008:** Contact officer updated **8 April 2008:** Contact officer updated **13 February 2008:** Contact officer updated