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Australian Taxation Office

ROSA IN BRIEF – SHORTFALL INTEREST CHARGE

A quick reference tool explaining the shortfall interest charge that was introduced as a result of the review of aspects of income tax self assessment (ROSA).

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ABOUT THIS RESOURCE

BACKGROUND

In November 2003, the Treasurer announced the review of aspects of income tax self assessment. On 16 December 2004, the outcome of the review was announced by the Treasurer with the release of the *Report on Aspects of Income Tax Self Assessment (ROSA)*. The government endorsed all 54 recommendations in the report.

The recommendations are designed to improve taxpayer certainty through:

- a better framework for Tax Office advice
- increased protection
- reduced compliance costs
- mitigation of the interest and penalty consequences of taxpayer errors, and
- subsequent improvements as a result of better policy processes, law design and administrative approaches.

Those recommendations requiring legislative solutions were given effect by the *Tax Laws Amendment (Improvements to Self Assessment) Act (No. 1) 2005* and the *Tax Laws Amendment (Improvements to Self Assessment) Act (No. 2) 2005*. The majority of the remaining recommendations require administrative solutions and are being addressed progressively by the Tax Office.

In support of these changes, the Tax Office has developed a comprehensive skilling program to ensure our staff continues to meet taxpayers' needs. This program includes a series of *ROSA in brief* self-paced training products. (See 'Purpose of this product' for other *ROSA in brief* resources).

USING THIS RESOURCE

The ROSA in brief series is a self-paced learning resource for people involved in any aspect of self assessment. This resource should be read in conjunction with the:

- *Income Tax Assessment Act 1936* (ITAA 1936)
- *Income Tax Assessment Act 1997* (ITAA 1997), and
- *Taxation Administration Act 1953* (TAA).

Materials

You will need:

- the *Taxation Administration Act 1953*, and
- a calculator.

Time

This resource should take about one hour to read and complete.

Prerequisites

If you already have a working knowledge of the current general interest charge (GIC), this resource on the new shortfall interest charge (SIC) will provide an update on what the changes mean.

Icons

The following icons are used throughout this resource:

An important point or feature.

Refer to another source of information (for example, book or a website)

INTRODUCTION 01

PURPOSE OF THIS PRODUCT

The *ROSA in brief* series is designed to help people involved in any aspect of self assessment to gain a basic understanding of the key changes resulting from the review of self assessment (ROSA).

This *ROSA in brief* resource outlines the key aspects of the new shortfall interest charge (SIC).

The shortfall interest charge is a separate interest charge with a lower rate. It was introduced for shortfall cases (that is, where income tax assessments are amended, resulting in an increase in the tax liability). It applies to the increased amount of liability for the period before the issue of the amended assessment.

Other *ROSA in brief* resources include the following:

1 overview
2 private rulings
3 public rulings
4 oral advice
5 other written advice and publications
6 period of review
7 penalties
8 shortfall interest charge (this resource)
9 Part IVA

LEARNING OBJECTIVES

After completing this resource you will be able to:

- explain the policy reasons for the introduction of the shortfall interest charge
- identify circumstances in which the shortfall interest charge will apply
- calculate the shortfall interest charge under a variety of scenarios
- explain the new remission regime for the shortfall interest charge and the shortfall general interest charge, and
- explain the new objection and appeal rights for the shortfall interest charge.

02 OVERVIEW

POLICY RATIONALE

The underlying intent of the ROSA changes was to move the balance of fairness in favour of taxpayers who act in good faith.

The review recommended changes to the design of the general interest charge (GIC) to improve its operation in the context of self assessment. A separate interest charge has been introduced, with a lower interest rate, for shortfall cases (that is, where income tax assessments are amended, resulting in an increase in the tax liability).

A tax shortfall is different from a late payment of tax. A late payment occurs where a stated liability is not fully paid by the due date.

Before the introduction of the shortfall interest charge (SIC), an income tax shortfall was treated in the same way as a late payment, with the general interest charge being applied from the due date of the original assessment up to the time the amount was paid. This occurred because the due date for payment of a shortfall amount was the same as for the original assessment, automatically triggering the application of the general interest charge from that date.

In situations where the shortfall is identified later, the general interest charge (GIC) was imposed for the 'shortfall period' (the period between the due date for the original assessment and the correction of the shortfall).

The general interest charge is set at a high rate when compared to the indicators for commercial borrowings. The rationale behind this high rate is to encourage prompt payment of tax liabilities.

In the situation of a non-payment of an established and quantified tax debt, this higher rate (or premium) can be managed or avoided by arranging to use alternative low-cost finance. However, taxpayers are usually unaware of a tax shortfall until we issue them with an amended assessment, so they may not be in a position to respond to the incentive premium that is built into the general interest charge.

For this reason, the government created a new, lower interest charge specifically for the shortfall period while maintaining the general interest charge for late payments of unpaid tax and shortfall interest charge.

Both the shortfall interest charge and the general interest charge are designed to:

- act as an incentive to encourage taxpayers to pay their tax by the due date
- ensure that taxpayers who fail to fulfil their obligations do not receive an advantage over those who do, and
- compensate the community for the effect on the revenue caused by late payments.

The ROSA measure also allows us to remit the SIC if the Commissioner considers it fair and reasonable to do so. The Commissioner has extended our SIC remission policy to shortfall GIC.

All of these changes to the law aim to build flexibility into the self assessment system and improve transparency and fairness markedly in favour of taxpayers who act in good faith.

Main features

The main features of the new measure are:

- Income tax shortfalls now attract the lower shortfall interest charge instead of the general interest charge for the period before the issue of an amended assessment.
- The shortfall interest charge is
  - generally calculated from the date the earlier, understated assessment was due to be paid to the day before we issue the notice of amended assessment
  - calculated at a lower rate (four percentage points lower) than the general interest charge
  - tax deductible.
- The due date for the payment of the tax shortfall and related shortfall interest charge is 21 days (in practice 24 days, after time to deliver is taken into account) after the amended assessment is issued.
- Once the due date for the amended assessment has passed, the general interest charge applies to any unpaid tax and shortfall interest charge.
- We can remit the shortfall interest charge if the Commissioner considers it fair and reasonable to do so.
- We will give a written explanation for rejecting remission requests.
- Taxpayers have objection and appeal rights against unfavourable remission decision if the shortfall interest charge is significant (exceeds 20%) relative to the size of the shortfall.

> The provisions giving effect to the shortfall interest charge are contained in *Tax Laws Amendment (Improvement to Self Assessment) Act (No 1) 2005*, specifically Division 280 of Schedule 1 to the TAA. Consequential amendments were also made to the ITAA 1936 and the ITAA 1997 and the *Taxation (Interest on Overpayments and Early Payments) Act 1983*.

The new law versus the previous law

The following table provides a snapshot of the ROSA changes relating to the shortfall interest charge.

Previous treatment	As a result of ROSA
Income tax shortfalls attracted the general interest charge, with a seven percentage point uplift over the base rate, from the due date of the original assessment until paid.	Income tax shortfalls attract the shortfall interest charge from the date the earlier, understated assessment was due to the day before the notice of amended assessment is issued. This new interest charge is calculated at a rate three percentage points above the base rate.
The due date for payment of the tax shortfall was the due date for the original assessment.	The due date for the payment of the tax shortfall and related shortfall interest charge is 21 days (in practice 24 days) after the issue date of the shortfall and shortfall interest charge.
Shortfall amounts attracted the general interest charge from the original due date.	Shortfall amounts not paid by the new due date attract the general interest charge from that date.
The general interest charge was tax deductible.	Both the general interest charge, where it applies, and the shortfall interest charge are tax deductible.
The Commissioner had the power to remit the general interest charge.	The Commissioner still has the power to remit the general interest charge, where it applies. The Commissioner also has the power to remit the shortfall interest charge if the Commissioner considers it fair and reasonable to do so.
A taxpayer could only formally request reasons for a remission decision in limited circumstances under the *Administrative Decisions (Judicial Review) Act 1977*.	The Commissioner must give written reasons for rejecting a remission if the remission request is made in the approved form.
Taxpayers had no right of objection against a general interest charge remission decision. They could seek a review of a remission decision under the *Administrative Decisions (Judicial Review) Act 1977*.	Taxpayers may object against a decision not to remit a shortfall interest charge if the unremitted interest exceeds 20% of the tax shortfall. They also have the right to judicial review under the *Administrative Decisions (Judicial Review) Act 1977*.

TIMING

The shortfall interest charge and the new due date rule for amended assessments apply to income tax shortfalls for the 2004–05 and later income years.

Regardless of when an amendment is made, shortfall GIC is still payable in respect of:

- amended income tax liabilities for the 2000–01 to 2003–04 income years, and
- shortfalls raised for other tax-related liabilities.

For income tax shortfalls only, we also remit shortfall GIC that accrues from 1 July 2005 to the SIC rate.

> See paragraphs 41–45 of the *Law Administration Practice Statement PS LA 2006/8 – Remission of shortfall interest charge and general interest charge for shortfall periods* for the Commissioner's decision to remit the GIC to the SIC rate for the shortfall period that accrues from 1 July 2005.

IMPACT

All taxpayers are affected by the new measure. This includes individual self preparers, individuals who use tax agents, very small businesses, superannuation funds, trusts, partners, small and medium businesses and large businesses.

Taxpayers whose assessments for the 2004–05 and later income years are amended (resulting in an increased tax liability) benefit from reduced charges. For example, a taxpayer with a $1,000 tax shortfall over two years would incur a shortfall interest charge about $100 less than would have applied under the general interest charge (all other things being equal).

In the first year of operation of the shortfall interest charge, 87,577 amendments were issued with a shortfall interest charge.

Taxpayers can seek a review of a decision not to remit the shortfall interest charge if the unremitted interest exceeds 20% of the tax shortfall.

Law Administration Practice Statement PS LA 2006/8 provides guidelines for the remission of the shortfall interest charge and the general interest charge in shortfall instances not covered by the new measures. The practice statement is intended to provide tax professionals and the community with increased certainty and transparency about the remission of interest charges that accrue prior to the issue of a notice of amended assessment or adjustment.

Remission of general interest charge that accrues after the date of issue of the amended notice of assessment continues to be considered using the guidelines in chapter 93 of the *ATO Receivables Policy*.

APPLICATION OF THE SHORTFALL INTEREST CHARGE

03

LIABILITY FOR THE SHORTFALL INTEREST CHARGE

From the 2004–05 income year, a taxpayer whose income tax assessment is amended so as to increase their tax liability incurs the shortfall interest charge rather than the general interest charge on the shortfall during the shortfall period.

> A tax shortfall does not exist unless the taxpayer's overall liability is increased.

The shortfall amount for interest charge purposes may differ from the net amount payable in the amended notice of assessment. Essentially the shortfall amount represents the difference between the original assessment and the amended assessment using the following equation (for individuals and trusts):

A (Income tax) + O (Medicare levy) – G (Tax offsets)

EXAMPLE 1: Amended assessment with no shortfall

Alfred is a mechanic in the 30% tax bracket (plus the 1.5% Medicare levy).

When preparing his tax return for the 2004–05 income year, Alfred incorrectly claims a $400 deduction for childcare expenses, but also neglects to claim a valid $500 deduction for his tools of trade.

A later audit of Alfred's work-related expense claims leads to the Tax Office querying the deduction for the childcare expenses. In reviewing *TaxPack*, Alfred acknowledges that he was not entitled to that deduction, but does become aware of his entitlement to a deduction for replacement tools.

The amended assessment reduces Alfred's overall liability by $31.50 (that is, 31.5% × ($400 – $500)). Alfred does not have a tax shortfall and is not liable for the shortfall interest charge on the $400 childcare deduction that has been disallowed.

The shortfall interest charge applies on a daily compounding basis from the due date for payment of the earlier, understated assessment to the end of the day before the notice of the amended assessment is issued (the shortfall interest charge period).

The shortfall interest charge rate is calculated using the base interest rate plus three percentage points. The definition of base interest rate is dealt with later in the module.

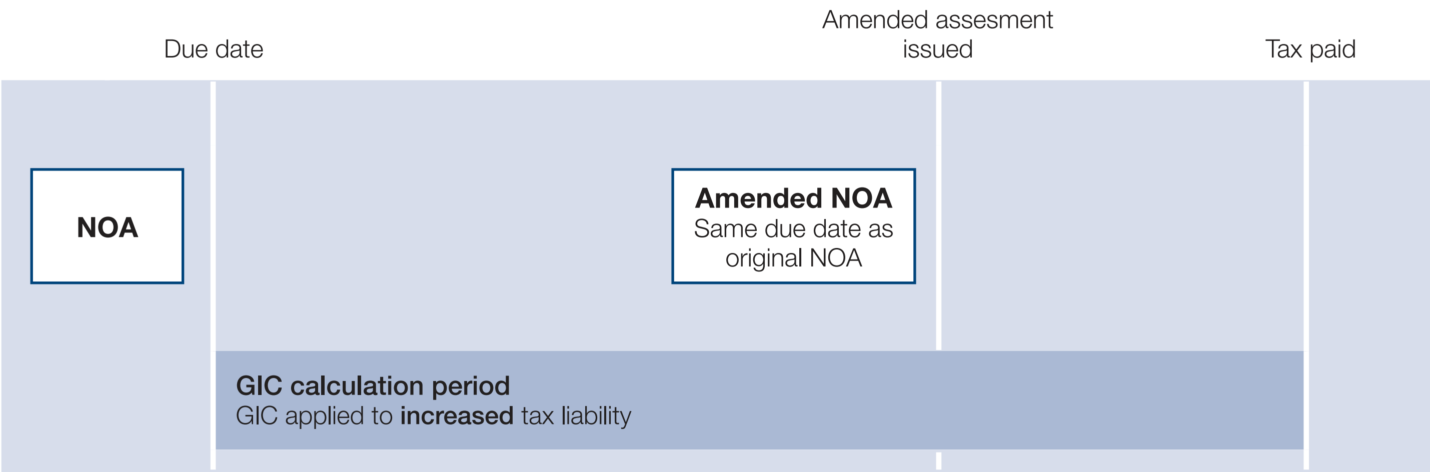
> The shortfall interest charge applies regardless of whether or not the taxpayer is liable to any penalty. Liability to the shortfall interest charge does not depend upon – or imply – culpability on the part of the taxpayer.

As per the legislation the new due date for payment of the tax shortfall and the related shortfall interest charge is 21 days after the date on which the Commissioner gives the notice increasing liability. Once this due date for the amended assessment has passed, the general interest charge will apply automatically to any unpaid tax and shortfall interest charge.

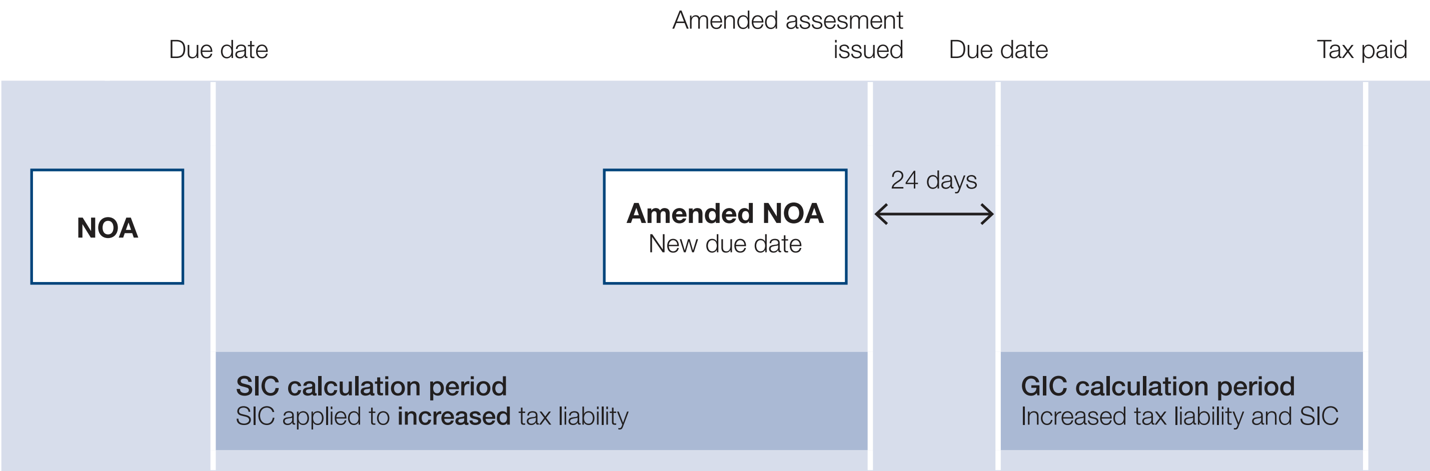
> Sections 28A and 29 of the *Acts Interpretation Act 1901* describe what is meant by the term 'give'.

In practice, however, the due date of a liability under an amended assessment and shortfall interest charge will be 24 days after the issue of the notice of amended assessment (21 days + 3 days for service). Similarly any shortfall interest charge will be calculated up to the day before the issue of the amended assessment. If the 24th day falls on a weekend or public holiday, the due date will be the next business day.

For 2000–01 – 2003–04 income years



For 2004–05 and later income years



Where an original assessment is issued and the tax liability is not fully paid by the due date, the general interest charge will continue to apply from the due date of that assessment to the time the amount including the accrued general interest charge is paid in full.

SHORTFALL INTEREST CHARGE PERIOD

Simple shortfall case

The shortfall interest charge exists for each day in the period during which the taxpayer's liability was understated. In the majority of cases, this period will run from the due date of the original assessment to the day before the Commissioner issues notice that the assessment has been amended upwards because of the shortfall (a 'debit' amendment).

EXAMPLE 2: Simple shortfall case

Jane is a part-time teacher in the 30% tax bracket (plus the 1.5% Medicare levy).

In her tax return for the 2004–05 income year Jane incorrectly claims a $200 deduction for her lunch time meal expenses. The due date for payment of the assessment based on that return is 21 November 2005.

A later audit of Jane's work-related expense claims results in her liability being increased by $63 (that is, 31.5% × $200), and her amended assessment is issued on 3 February 2007.

The shortfall interest charge would apply on the $63 for the 439 days from 21 November 2005 to 2 February 2007 (inclusive).

The calculation of shortfall interest charge in relation to a first amendment (as in example 2) is straightforward. The shortfall interest charge is applied to the shortfall amount for the period from the due date of the original assessment to the day before the notice of amended assessment is issued. This is regardless of how many *particulars* are being amended or whether the net shortfall is a result of a combination of debit and credit adjustments.

For 2004–05 and later income years, if the original assessment is a credit, the shortfall interest charge period begins on the day on which income tax would have been due to be paid if there had been any (that is, the notional due date).

An erroneous credit amendment

In some cases the tax shortfall does not arise from an error in the original assessment (as in example 2), but from the taxpayer later requesting a credit amendment that proves to be incorrect (that is, an erroneous credit amendment).

Although a tax shortfall would arise, the taxpayer does not receive any benefit until they receive the erroneous credit. In such cases, the shortfall interest charge period begins from the due date of the amended assessment that incorrectly reduced the previously assessed liability.

Refer to new subsection 204(2) of the ITAA 1936 to determine new due dates for amended assessments. Where no liability is payable under an amended assessment, new subsection 280-100(3) of Schedule 1 to the TAA prescribes that the shortfall interest charge period begins on the day on which income tax would have been due to be paid if there had been any.

EXAMPLE 3: An erroneous credit amendment

John is an office worker in the 30% tax bracket (plus the 1.5% Medicare levy).

John files his tax return for the 2004–05 income year. The due date for the payment of the assessment based on that return is 21 November 2005.

Later, a work colleague states that he had claimed a workplace deduction for a business suit, prompting John, who had purchased a $600 business suit in May 2005, to request an amendment to his assessment reducing his liability by $189 (that is, 31.5% × $600). We issue John's amended assessment on 3 January 2006, and he receives a cheque for $189. This amended assessment (being a credit amendment) has a notional due date of 27 January 2006 (that is, 24 days after the notice is issued to John).

A later audit of John's work-related expense claims results in his liability being increased by $189 (because John was not entitled to claim his business suit as a work-related expense). John's amended assessment is issued on 30 January 2007.

The shortfall interest charge on the $189 would apply for the period from 27 January 2006 to 29 January 2007 (inclusive).

In the above example, an amended assessment was issued to reverse a particular (the cost of a business suit) that related to an earlier credit amendment rather than the original assessment. Accordingly, the shortfall interest charge would be calculated from the notional due date of the amended credit assessment and not from the due date of the original assessment.

Any general interest charge for the period from the due date of an original assessment to the issue date of the credit amended assessment that was reduced because of the issue of the credit amendment would be reinstated to the account when the debit amended assessment issues.

Refer to new subsection 280-100(3) of Schedule 1 to the TAA and new subsection 204(2) of the ITAA 1936 to determine the notional due date of a credit amendment.

Multiple amendments

Where there are multiple amendments consisting of debit and credit adjustments it is intended that the shortfall interest charge apply to the various tax shortfall amounts during their respective shortfall periods. The shortfall interest charge period in the case of multiple amendments may run over the same periods.

EXAMPLE 4: Multiple amendments

John is an office worker in the 30% tax bracket (plus the 1.5% Medicare levy).

When preparing his tax return for the 2004–05 income year, John omits to declare $800 in dividend income (unfranked) and incorrectly claims a $400 deduction for his telephone line rental. The due date for payment of the assessment based on that return is 21 November 2005.

Later, a work colleague states that he had claimed a workplace deduction for a business suit, prompting John, who had spent $600 on a business suit in May 2005, to request an amendment to his assessment, reducing his tax liability by $189 (that is, 31.5% × $600). John is notified of this amendment, and receives a refund cheque for $189. The amended assessment has a notional due date of 20 December 2005.

Income matching of John's tax return reveals the omitted dividend income, resulting in an amended assessment increasing his tax liability by $252 (that is, 31.5% × $800). The amended assessment issues on 2 March 2006.

A later audit of John's work-related expenses denies the deduction for telephone line rental and the business suit, resulting in an amended assessment increasing his tax liability by $315 – 31.5% × ($400 + $600). The amended assessment issues on 30 January 2007.

The shortfall interest charge would be applied as follows.

- For the dividends: on $252 (that is, 31.5% × $800) for the 101 days from 21 November 2005 to 1 March 2006 (inclusive).
- For the telephone line rental: on $126 (that is, 31.5% × $400) for the 435 days from 21 November 2005 to 29 January 2007 (inclusive).
- For the business suit: on $189 (that is, 31.5% × $600) for the 406 days from 20 December 2005 to 29 January 2007 (inclusive).

DUE DATE FOR PAYMENT OF AMENDED ASSESSMENTS

Under the previous law, an amended assessment was due and payable at the same time as the original assessment. The general interest charge would also have accrued each day during the shortfall period and would have been due at the end of each day.

The new arrangements provide a prospective due date, allowing a 21-day payment period (which in practice is a 24-day payment period) for notified shortfall amounts and related shortfall interest charge.

EXAMPLE 5: 21-day payment period

John is an office worker in the 30% tax bracket (plus the 1.5% Medicare levy).

John incorrectly claims a $600 deduction for an ordinary business suit in his tax return for the 2004–05 income year. The due date for payment of the assessment on that return is 21 November 2005.

A later audit of John's tax return for the 2004–05 income year disallows the deduction for the business suit, resulting in an increased tax liability of $189 (that is, 31.5% × $600), with the amendment being issued on 30 January 2007.

Under the previous law:

- the shortfall amount of $189 would have been due and payable from the due date of the original assessment (21 November 2005), and
- the general interest charge would have applied to the shortfall amount on a daily basis from the due date of the original assessment (21 November 2005) until the day the taxpayer paid the total tax liability (including the general interest charge).

Under ROSA:

- the tax shortfall amount of $189 is due and payable on 23 February 2007, that is, 24 days after we issued John's amended notice of assessment (30 January 2007).
- the shortfall interest charge applies to the shortfall ($189) on a daily basis from the due date of the original assessment (21 November 2005) until 29 January 2007 (inclusive). The shortfall interest charge would be due and payable 24 days after the notice of the shortfall interest charge issued (20 February 2007).

The legislation requires the Commissioner to give the taxpayer a notice stating the amount of the shortfall interest charge liability. This amount can be included on another notice that the Commissioner gives to the taxpayer – such as the notice of amended assessment. In most cases the shortfall interest charge will be included on the notice of amended assessment. It follows that the shortfall amount and the shortfall interest charge will have the same due date.

Refer to section 280-110 of Schedule 1 to the TAA for the requirement to notify taxpayers of their SIC liability (which may be included in any other notice) and to subsections 204(2) and (2A) of the ITAA 1936 outlining the due dates for amended assessments and shortfall interest charge notices. These changes apply to amendments of assessments for the 2004–05 and later income years.

The new prospective due date will apply to all amended assessments.

In the case of credit amendments, no additional amount of tax will become due and payable at that date. However, the notional due date for the amended assessment will be the starting point for any shortfall interest charge period that might later arise from erroneous credits in that amended assessment (refer to example 4).

Relevance of previous due dates

As outlined above, an amended assessment has a new prospective due date.

The due date of the original assessment and any intervening amended assessments, however, will continue to be relevant for determining any shortfall interest charge and/or general interest charge.

The due date of an original assessment for the 2004–05 and later income years will continue to be the starting date for the shortfall interest charge on any tax shortfall arising from the original assessment.

The due date of *any* original assessment will continue to be the starting date for the general interest charge on any unpaid tax relating to that original assessment.

EXAMPLE 6: Relevant due dates and amended assessments

John is an office worker in the 30% tax bracket (plus the 1.5% Medicare levy).

When preparing his tax return for the 2004–05 income year, John omits to declare $800 in dividend income (unfranked) and incorrectly claims a $380 deduction for telephone line rental.

John lodges his tax return on time and receives a tax assessment for $1,000 due and payable on 21 November 2005. John makes no payment against that $1,000. Accordingly, the general interest charge begins to accrue from 21 November 2005.

Income matching identifies the omitted dividend income. On 2 March 2006, we issue an amended assessment increasing John's tax liability by $252 (that is, 31.5% × $800). We also notify him of the shortfall interest charge on that amount for the 101 days from 21 November 2005 to 1 March 2006 (inclusive). John pays the increased liability and the shortfall interest charge before the due date of 26 March 2006 (that is, 24 days after the amended notice of assessment issued).

As the $1,000 liability from the original assessment was not paid by 21 November 2005 general interest charge has been accruing on the outstanding balance from that date.

A later audit of John's work-related expenses denies the deduction for telephone line rental, resulting in a further amended assessment which issues on 30 January 2007. John's liability for the 2004–05 income year has been increased by $119 (that is, 31.5% × $380) and the shortfall interest charge applies on this amount for the 435 days from 21 November 2005 to 29 January 2007 (inclusive). The due date for the payment of these amounts is 23 February 2007 (that is, 24 days after we issued the notice of amended assessment). The general interest charge will accrue on the increased tax liability and shortfall interest charge if not paid in full by the due date.

As John has still made no payments against the unpaid $1,000 from the original assessment or the resulting general interest charge, the general interest charge will continue to accrue daily on the total balance of overdue amounts.

Interest charge implications of the new prospective due date

Having a new prospective due date for amended assessments has implications for interest charges.

The payment period

Individual taxpayers who lodge on time have at least 24 days after their original assessment issues in which to make full payment of their outstanding tax liability. During this period there is no general interest charge applicable.

Consistent with this treatment, neither the shortfall interest charge nor the general interest charge on the shortfall will apply during this 24-day payment period for amended assessments. This ensures that the taxpayer can settle the matter by paying the notified amount by the due date without further (un-notified) interest accruing during this 24-day period.

If the due date for payment of a tax debt falls on a Saturday, Sunday or a public holiday for the whole of any state or territory, the payment can be made on the next business day (refer section 8AAZMB of the TAA). In these circumstances, all taxpayers receive the benefit of the extension, even if they are not located in the relevant state or territory.

> ! The general interest charge is not a tax debt for the purposes of section 8AAZMB of TAA.

EXAMPLE 7: Tax debt falls on a Saturday, Sunday or public holiday

Payment of a tax debt due on the date shown in the table below will be deferred to the next business day for all taxpayers regardless of where the taxpayer is located.

Situation	Procedure
An amended assessment issued to a taxpayer with Monday, 13 March 2006 being the due date for payment of tax and shortfall interest charge.	Monday, 13 March 2006 was a public holiday in South Australia (Adelaide Cup Day). The taxpayer could make the payment on the next business day without incurring any general interest charge.

> ! The new prospective due date may give rise to an entitlement to early payment interest under the *Taxation (Interest on Overpayments and Early Payments) Act 1983* for companies and superannuation funds. This entitlement will apply to both the early payment of a tax shortfall and the shortfall interest charge.

The general interest charge

If any tax remains unpaid after the due date, the general interest charge will apply. General interest charge is calculated on a daily compounding basis:

- starting on the day the amount is due and payable, and
- finishing on the last day that any tax and accrued general interest charge remains unpaid.

It will also accrue on the same basis for any unpaid shortfall interest charge.

The general interest charge is applied for any late payment because once the amounts owing have been notified and a payment period allowed, the taxpayer would generally be in a position to manage payment of the debt, for example, by arranging to use alternative lower-cost finance. Accordingly, the higher rate of the general interest charge is to encourage the payment of tax liabilities when they fall due.

> ! No tax shortfall amount will be subject to both the general interest charge and the shortfall interest charge in relation to the same day.

EXAMPLE 8: General interest charge

John is an office worker in the 30% tax bracket (plus the 1.5% Medicare levy).

When preparing his tax return for the 2004–05 income year, John omits to declare $800 in dividend income (unfranked). John has an income tax liability for the 2004–05 income year which is due and payable on 21 November 2005.

Income matching identifies the omitted dividend income. On 2 March 2006, we issue an amended assessment increasing John's liability by $252 (that is, 31.5% × $800). We also notify him of the shortfall interest charge on that amount for the 101 days from 21 November 2005 to 1 March 2006 (inclusive).

The due date for the amended assessment is 26 March 2006 (that is, 24 days after the notice was issued). John pays the increased tax liability, shortfall interest charge and the general interest charge in full on 30 April 2006.

John is liable for the general interest charge on a compounding daily basis from 26 March 2006 (the due date) to 29 April 2006 (the last day on which at the end of the day there still remained an amount of tax, shortfall interest charge or general interest charge that was unpaid).

The day in which full payment was made (that is, 30 April 2006) is not included in the period because at the end of that day there was no amount of tax, shortfall interest charge or general interest charge that remained unpaid.

Refer to subsection 204(3) of the ITAA 1936 for how we determine the GIC period. This subsection applies to amendments of assessments for the 2004–05 and later income years.

Shortfall interest charge and credit amendments

Where an assessment has been amended because of a tax shortfall and that shortfall is later overturned (possibly due to a court decision), the shortfall interest charge relating to that tax shortfall will be adjusted/reduced.

If the shortfall has been paid, the taxpayer will generally be eligible for interest on an overturned tax shortfall under the *Taxation (Interest on Overpayments and Early Payments) Act 1983*. The amendment as a result of an overturned tax shortfall will also entitle the taxpayer to interest on any related shortfall interest charge that has been paid.

Where a credit amendment is later overturned the general interest charge reduced by the credit amendment will be reinstated.

Refer to subsection 172(1) and 172(1A) of the ITAA 1936 regarding reinstating credit interest. These changes apply to amendments of assessments for the 2004–05 and later income years.

Tax deductibility of the shortfall interest charge

The shortfall interest charge is tax deductible. This is consistent with the tax deductibility of the general interest charge. However the general interest charge is deductible in the year that it accrues while the shortfall interest charge is deductible in the year that the taxpayer is given notice of the liability.

Assessable recoupment

Previously, an assessable recoupment occurred where the Commissioner had remitted an amount of general interest charge.

Subsection 20-25(2A) of the ITAA 1997 has been amended to include the shortfall interest charge as an assessable recoupment.

Because the taxpayer is entitled to claim a deduction for the general interest charge and the shortfall interest charge, the taxpayer must include any recouped amount in their assessable income.

CALCULATION OF THE SHORTFALL INTEREST CHARGE

The general interest charge rate for a day is arrived at by dividing an annualised rate by the number of days in the calendar year. The shortfall interest charge works in exactly the same manner, except its annualised rate is four percentage points lower than the general interest charge.

The shortfall interest charge uses the same base rate as the general interest charge. The base interest rate is defined in section 8AAD of the TAA. The base interest rate is adjusted quarterly, as the mean yield on 90-day Bank Accepted Bills for the middle month of the preceding quarter. The base interest rate must be rounded to two decimal places (rounding .005 upwards).

The daily shortfall interest charge rate is:

$$\frac{\text{Base interest rate for the day} + 3 \text{ percentage points}}{\text{Number of days in the calendar year}}$$

EXAMPLE 9: Calculation of the shortfall interest charge rate

Assume the mean yield on 90-day bank accepted bills for February 2006 was 5% per annum. The base rate applying in the second quarter of 2006 (that is, 1 April 2006 to 30 June 2006) would therefore be 5% per annum.

The annualised shortfall interest charge rate applying during that quarter would therefore be 8% (that is, 5% + 3%) per annum, resulting in a daily shortfall interest charge rate of 0.02191780% (that is, 8% ÷ 365).

In contrast, the applicable general interest charge rate during that quarter would be 12% per annum, corresponding to a daily general interest charge rate of 0.03287671% (that is, 12% ÷ 365).

The shortfall interest charge rate is applied on a daily compounding basis to the tax shortfall amount for the duration of the shortfall interest charge period.

This compounding effect means that for any day in the period, the tax shortfall amount and any shortfall interest charge accumulated to date is multiplied by the daily shortfall interest charge rate.

Calculation of the shortfall interest charge:

The daily shortfall interest charge rate is calculated using the formula:

$$(B + 3\%) \div Y$$

where:

- B is the base interest rate for the relevant quarter calculated by reference to the 90-day Bank Accepted Bills published by the Reserve Bank of Australia, and
- Y is the number of days in the calendar year.

Use the following formula to calculate the amount of shortfall interest charge payable in relation to a shortfall:

$$S \times (1 + R)^N - S$$

where:

- S is the shortfall amount
- R is the daily shortfall interest charge rate (as calculated above), and
- N is the number of days in the calculation period.

You can use a compounding interest calculator to do the calculations easily.

> ! If a calculation period spans more than one quarter, make a separate calculation for each quarter there has been a change in the shortfall interest charge rate. (For any second and subsequent quarter calculations, add the shortfall interest charge calculated for the previous quarter to the shortfall amount before starting the interest calculation.)

EXAMPLE 10: Calculation of the shortfall interest charge

A taxpayer had a $10,000 tax shortfall (S) for the whole of the second quarter of 2006, during which the base rate was 5% per annum resulting in a daily shortfall interest charge rate of 0.02191780% (see example 9).

- On 1 April 2006 the shortfall interest charge would be $2.19 ($10,000 × 0.0002191780).
- On 2 April 2006 the shortfall interest charge would be $2.19 ($10,002.19 × 0.0002191780).

Over the whole 91 days of the quarter, the total shortfall interest charge would amount to $201.43:

$$S \times (1 + R)^N - S$$

$$\$10{,}000 \times 1.0002191780^{91} - \$10{,}000$$

This compares with the general interest charge of $303.64 that would have been imposed on the tax shortfall under the previous legislation:

$$\$10{,}000 \times 1.0003287671^{91} - \$10{,}000$$

Refer to section 280-105 of Schedule 1 to the TAA to calculate the amount of shortfall interest charge.

04 REMISSION OF SIC AND SHORTFALL GIC

Under section 280-160 of Schedule 1 to the TAA, we may remit all or part of an amount of shortfall interest charge if the Commissioner considers it fair and reasonable to do so.

Remission can be requested by the taxpayer or initiated by the Commissioner.

In considering whether to grant remission, the Commissioner must have regard to two key principles.

1 Remission should not occur just because the benefit the taxpayer received from the temporary use of the shortfall amount is less than the shortfall interest charge. In essence this means that a taxpayer should not expect remission to be granted just because the loan benefit they received from having made a tax shortfall is lower than the shortfall interest charge.

2 Remission should occur where the circumstances justify the Commonwealth bearing part of the cost of the delayed receipt of taxes. Such cases would usually entail delay, contributory cause or fault on the part of the Tax Office or other parties. Where these circumstances are readily apparent the Tax Office should initiate remission.

In addition, remission may not be warranted if a taxpayer has been obstructive or other circumstances mean that it would not be fair and reasonable to remit. In judging whether a taxpayer has acted in good faith, the totality of the circumstances relating to the shortfall need to be considered.

> Although the *Report on aspects of income tax self-assessment (ROSA)* only dealt with a discretion to remit the new shortfall interest charge, the Commissioner has specifically extended the same principles to the remission of the general interest charge in the shortfall period.
>
> The Commissioner's detailed policy for remission of shortfall interest charge and general interest charge accrued during shortfall periods is outlined in *Law Administration Practice Statement PS LA 2006/8*.

LAW ADMINISTRATION PRACTICE STATEMENT PS LA 2006/8

Law Administration Practice Statement PS LA 2006/8 ('the practice statement') is designed to assist tax officers in determining whether remission of SIC and GIC is warranted during the shortfall period.

The practice statement applies to interest charges that accrue during the shortfall period. That is:

- shortfall interest charge (SIC)
- shortfall general interest charge (GIC) – that is, GIC accrued during the shortfall period on a shortfall amount – and
- GIC and other interest charges under the former section 170AA of the ITAA 1936.

A reference in the practice statement relating to the remission of shortfall GIC will apply equally to remission of any interest imposed under the current or former section 170AA of the ITAA 1936.

> The terms 'shortfall amount', 'shortfall GIC' and 'shortfall period' are defined in paragraphs 22–24 of the practice statement.

The practice statement does not apply to remissions of shortfall GIC relating to the superannuation guarantee charge.

Unless specifically addressed, the practice statement does not apply to GIC that is not shortfall GIC.

> See the chapter 'General Interest Charge' in the *ATO Receivables Policy* for guidelines on remitting GIC in the two circumstances above.

Practice statement structure

For the purposes of the practice statement some terms are defined at paragraphs 14 to 26 of the document.

There is an explanation of SIC at paragraphs 27–29 and an explanation of the GIC relating to the shortfall period (income tax 2003-04 and earlier years and other taxes) at paragraphs 30–31.

A detailed remission policy is in paragraphs 32–123 and should be read in the context of the complete document.

A summary of the legislation for SIC and GIC is in paragraphs 124–150, while diagrams illustrating the interest charges and shortfall periods can be found at paragraph 151.

APPLICATION OF INTEREST CHARGES

The following table details the more common provisions relating to the imposition of interest charges on shortfall amounts.

Type of shortfall	Period to which shortfall relates:	Interest type	Legislative reference
Income tax	For 1999–2000 and earlier income years:		
	■ periods up to and including 30 June 1999	Interest	Former sections 170AA and 214A of the *Income Tax Assessment Act 1936* (ITAA 1936)
	■ periods on or after 1 July 1999	GIC	Former section 170AA ITAA 1936 and Division 1 of Part IIA of *Taxation Administration Act 1953* (TAA)
	2000–01 to 2003–04 income years	GIC	Section 204 ITAA 1936 and Division 1 of Part IIA of the TAA
	2004–05 and later income years	SIC	Division 280 in Schedule 1 to the TAA
Fringe benefits tax (FBT)	Amounts that are due to be paid on or after 1 July 1999	GIC	Section 93 of the *Fringe Benefits Tax Assessment Act 1986* and Division 1 of Part IIA of the TAA
Indirect taxes: ■ goods and services taxes (GST) ■ wine equalisation tax (WET) ■ luxury car tax	All periods	GIC	Section 40 and Division 1 of Part IIA of the TAA
Pay as you go withholding (PAYG(W))	All periods	GIC	Section 16-80 in Schedule 1 and Division 1 of Part IIA of the TAA

Date of effect

The date of effect for the practice statement is 1 July 2005. However some changes affect amendments from 1 July 2005 and others from 1 July 2006.

‘Issue’ date versus ‘given’ date

The law

Throughout the practice statement reference is made to the situation where an amended notice of assessment is **given** to the taxpayer. This approach is in line with the legislation and the definition of shortfall period. By definition the shortfall period ceases on the day before the Commissioner **gives** the taxpayer notice of an amended assessment.

For amendments of income tax assessments for the 2004–05 and later income years the due date for payment of the tax shortfall and related shortfall interest charge is 21 days after the date on which the Commissioner gives the notice increasing liability.

In practice

From a practical perspective, the shortfall period will cease on the day before we issue the taxpayer with a notice of amended assessment.

Further, for amendments of income tax assessments for 2004–05 and later income years, the due date for payment of the tax shortfall and related shortfall interest charge is 24 days after we issue the notice of amended assessment (21 days + 3 days service).

With this in mind and in keeping with the practical application of the law any reference to **given** in the practice statement (in the context outlined above) has been replaced in this training resource with the word **issued**.

General principles and practices

Some of the general principles and practices included in the practice statement are:

- remission of both SIC and shortfall GIC should occur where the circumstances justify the Commonwealth bearing part or all of the cost of delayed payments
- remission of GIC to the SIC rate (that is, reduce GIC by 4 percentage points) for income tax amendments for income years prior to 2004–05 for the shortfall period after 30 June 2005
- the Commissioner may remit where there has been delay or it has taken us longer than expected to issue an amended assessment
- taxpayers who reasonably rely in good faith on Tax Office advice, publications, general administrative practice and ATO interpretive decisions (ATO IDs) receive full protection from interest charges for the 24-day period following the issue of a notice showing the correct position.

Tax officers must initiate remission where circumstances justifying remission are readily apparent. Taxpayers can request remission of SIC or shortfall GIC at any time.

Factors to consider when making a remission decision

When considering a remission request or making a remission decision the following should be considered:

- the practice statement
- the statements and principles in the *Taxpayers' charter*
- the individual circumstances of the case, and
- the principles of the compliance model.

> ! Care should be taken to read all paragraphs of the practice statement and apply them within the context of each section and of the complete document.

The extent of the remission must take into account the individual circumstances of a case. In some cases remission of the interest charge to the base rate may be appropriate.

However, the extent of any remission must have regard to the particular circumstances and the extent to which factors beyond the taxpayer's control were responsible for the size and duration of the shortfall. In some cases, circumstances may justify remission to below the base rate, including full remission.

Extracts from the practice statement

The following information is taken from the practice statement and outlines examples of situations that may arise in any one case. Where the text, including examples, is italicised this represents a direct quote from the practice statement.

> ! Certain examples have been developed for this training product. These examples are not meant to be definitive answers to situations; each case needs to be judged on its own merits.

Remission of GIC to the SIC rate

As SIC only applies to income tax shortfalls for the 2004–05 and later income years, the GIC will still be imposed in relation to income tax shortfalls for earlier years (that is, income years prior to 2004–05).

The SIC regime was not applied to earlier income years because it would have resulted in unequal treatment of assessments for the same year. Those taxpayers whose assessments were amended before the introduction of the SIC would have had the higher GIC imposed. However, continuing to apply the higher GIC rate from 1 July 2005 could be seen to be unfair.

Accordingly, it is considered fair and reasonable that shortfall GIC be remitted to the SIC rate for the period from 1 July 2005 to the day before the amended assessment is issued.

EXAMPLE 11

An amendment to Anna's 2003–04 income tax assessment was issued on 13 February 2006. Shortfall GIC accrues from 1 December 2004 (being the due date for payment of both the original assessment and the amended assessment).

For the period from 1 July 2005 to 12 February 2006 only, the GIC would generally be remitted by 4 percentage points (equating it with the SIC rate).

Further remission during the shortfall period may occur if other circumstances detailed in the practice statement are applicable.

As the SIC regime only applies to income tax shortfalls, the above considerations do not apply to GIC imposed in respect of other shortfall amounts.

Circumstances where remission may be appropriate

The practice statement outlines a range of circumstances where remission may or may not be appropriate. The considerations set out in the practice statement are not exhaustive and are not intended to limit the Commissioner's discretion to remit interest charges when it is fair and reasonable to do so.

For a detailed discussion of some specific circumstances refer to paragraphs 46–123 of the practice statement.

Tax Office delay

The Commissioner may remit where there has been delay or a longer than expected time taken in issuing an amended assessment.

The practice statement provides the following examples that may arise in any one case:

Delay in commencing an audit

Not all audits start immediately following self-assessment by a taxpayer, due to the allocation of the Tax Office's resources.

In recognition of this constraint the Commissioner will apply a rule of thumb in determining, for remission purposes, when an audit should have commenced. In general it can be expected that an audit will commence within a period equal to 50% of the relevant period of review.

Cases may commence at a later time, for example, where information is provided to the Tax Office from an external source.

Where there has been an unreasonable delay in the Tax Office allocating a case for audit, remission of interest charges to the base rate may be appropriate for the period of such delay.

Where there is an unlimited period to amend an assessment it would normally be appropriate when considering remission to adopt the standard period of review applicable to the year being adjusted.

The period of review will differ according to the type of tax, year or period, the taxpayer, whether a return was lodged early or late and whether avoidance or evasion was involved. For further information on period of review refer to *ROSA in brief – period of review*.

Expected audit completion date exceeded

Cycle timeframes have been set for specific types of audit activity. They will differ according to the expected type of activities being audited, the tax type and the market.

When we notify a taxpayer of our intention to audit, we will generally provide an expected audit completion date in that notice. We determine this date by applying a pre-determined cycle timeframe and calculating the expected completion date.

Although we notify most taxpayers of our intention to audit, there are some circumstances where notification is not appropriate, for example, where we suspect a case involves evasion or fraud or other criminal activity.

Provided the scope of the audit remains much the same throughout the course of the audit and the taxpayer does not unreasonably delay or obstruct the progress of the audit, interest charges will be remitted to the base rate for the period that exceeds the expected audit completion date.

EXAMPLE 12

The GST record keeping audit cycle timeframe is 30 days. If the GST audit takes 40 days, remission to base rate for the final 10 days may be appropriate.

EXAMPLE 13

A GST office auditor starts a 'GST specific audit – phone' audit of a taxpayer's business on 23 June 2006. The audit cycle is 40 days. However, on 26 July 2006, 33 days into the audit, it becomes apparent to the auditor that there are several risks involved in the case and that the work is more appropriately considered a 'GST micro comprehensive' audit with a 225-days cycle. The case is transferred to a GST field auditor on 27 July 2006. The timeframe for completion will extend to 225 days. This longer audit cycle still starts on 23 June 2006.

The use of expected audit completion date as a reason for remission applies to audits which started on or after 1 July 2006, except for large corporate audits where a '2 year' policy applies for audits that started on or after 1 July 2005: see paragraphs 65–69 of the practice statement for more information.

For audits that began before these dates, remission will be considered on a case-by-case basis using the principles outlined in the practice statement.

EXAMPLE 14

An audit commences on 1 July 2006. It has a cycle time of 120 days, making an expected audit completion date of 28 October 2006. Although the taxpayer and agent are not obstructive they do not supply the relevant information quickly. The auditor takes a week's leave not realising the issues are slightly more complex than first anticipated. The amended notice of assessment does not issue until 14 December 2006.

Remission to the base rate will be applicable from 29 October 2006 to 13 December 2006.

Remission for periods during the audit cycle timeframe may still be granted if there are other grounds for doing so, as set out in other sections of the practice statement. Where such a remission is granted this decision may need to be taken into account when determining the extent of remission for the period beyond the expected completion date.

EXAMPLE 15

An audit commences on 1 March 2007 and has an expected completion date of 30 July 2007. The amended notice of assessment with an increased tax liability does not issue until 31 October 2007. Because there was an unreasonable Tax Office delay (see below or refer to paragraph 58 of the practice statement) it is decided to grant full remission of the interest charge for the period 1 May 2007 to 30 June 2007.

Remission to the base rate would normally be applicable for the period the audit exceeded the expected completion date, that is, for three months (1 August 2007 to 31 October 2007). However, taking the earlier remission decision into account (full remission for a period of two months), remission to the base rate is only appropriate for one month – 1 October 2007 to 31 October 2007.

Terms such as 'commencement of audit', 'completion of audit', 'expected audit completion date' and 'audit cycle timeframes' are defined terms for the purpose of the practice statement.

Unreasonable delay

Although an audit may be completed within the cycle timeframe and before the expected audit completion date, this does not exclude other grounds for remission from applying. For example, there may have been unreasonable delays or periods of inactivity outside the control of the taxpayer that may warrant remission of interest charges.

The practice statement provides a general rule that if there is no action on a case for more than 30 days and it was possible for the case to progress during that time, full remission of the interest charges for the period of unreasonable delay would be appropriate.

The cycle timeframe is set to enable Tax Office auditors to complete the audit as well as other appropriate duties that may occur concurrently. If there are up to 30 days where the auditor does not work on the audit and the audit is completed within the benchmark, generally there is no remission.

EXAMPLE 16

An audit of John's 2004–05 income tax affairs commences on 1 July 2006 with an expected audit completion date of 27 November 2006.

On 2 September 2006 the auditor seeks more information from the client and provides a response date of 30 September 2006. By that date all the necessary information to determine a shortfall has been gathered and interviews have occurred.

On 2 October 2006 the auditor submits his final audit report to his team leader to authorise the case result. The team leader does not review the submission until 15 November 2006 and then authorises the result without change. The amendment issues on 20 November 2006.

Assuming no other circumstances apply, full remission of interest charges would be appropriate from 2 October 2006 to 15 November 2006 (the total period of inactivity which exceeds 30 days).

Tax Office delay in obtaining information from a third party

Where the Tax Office or the taxpayer experiences delay in obtaining information from a third party and this information is not otherwise available to the taxpayer, remission to the base rate is warranted for the period of the delay.

EXAMPLE 17

A taxpayer who is a self-preparer transfers a rental property to his son as a wedding gift, totally unaware of the CGT implications. An audit of the taxpayer's affairs reveals the transfer. The case officer engages the services on an independent valuer to ascertain the market value of the property for CGT purposes.

The valuation is delayed by 45 days due to the illness of the valuer. The taxpayer's assessment is amended to reflect the shortfall tax on the omission of the capital gain.

Remission of interest charges to the base rate would be warranted for the period of delay caused by the independent valuer.

If the delay in obtaining information is because the taxpayer is unwilling or unable to supply information that they should have, or that they are readily able to obtain, remission will generally not be granted for the delay.

Longer resolution times due to complexity of issues

There may be complex issues underlying a shortfall. Accordingly, it may take some time for the Commissioner to come to a view as to the proper operation of the law. This may result in an interruption between the commencement of an audit and the amendment of the assessment.

The practice statement makes it very clear that the referral of a complex matter to a specialist forum or network does not in itself constitute a delay that would warrant remission of interest charges.

In general, the cycle timeframes will factor in issues of complexity and the time taken for their resolution.

However, remission to the base rate would be warranted where the resolution of the issue took longer than would be expected and resulted in the case exceeding the expected audit completion date.

Large corporate audits – delay based upon reasonable time for completion of audit

The Commissioner announced in October 2005 that remission based on the expectation that it is reasonable for a large corporate audit to be concluded within two years of the notification of its commencement would generally be appropriate.

The practice statement gives effect to this announcement – for large corporates, SIC and shortfall GIC will be remitted to the base rate for the period that an audit extends beyond two years. The only time this policy does not apply is in exceptional cases that involve blatant obstruction/delay. Such cases will need approval at the executive level.

> This approach applies for audits that started on or after 1 July 2005. For audits that started before this date, remission based on delay will continue to be considered on a case-by-case basis using the principles outlined in the practice statement.

This 'two-year' policy does not apply to some transfer pricing audits. Refer to paragraph 68 of the practice statement.

This 'two-year' policy does not preclude remission being granted on other grounds as outlined in the practice statement.

Cases involving evasion or fraud

If evasion or fraud is involved remission is not normally granted. This applies even where some of the delay was attributable to the Tax Office or the expected audit completion date is exceeded.

The rationale for this approach is that the taxpayer would have been aware of the potential tax shortfall and could have taken steps to reduce their exposure to interest charges.

Remission in cases of evasion or fraud would still need to be considered on a case-by-case basis but having due regard to the circumstances giving rise to the shortfall.

Taxpayer delay

Delay is outside the taxpayer's control

The practice statement makes provision for delays that are outside the taxpayer's control.

In these circumstances full remission for the period of the delay may be appropriate.

These circumstances include delays in supplying information or documents for an audit that were directly attributable to:

- natural disasters (flood, fire, drought, earthquake and the like)
- other disasters that may have, or have had, a significant impact on a taxpayer or region; or
- the serious illness of the taxpayer where there is no other person that could have mitigated the length of the delay.

Conversely, remission is not usually appropriate if the reasons for the delay are within the taxpayer's control. For example, the taxpayer takes an extended vacation after an audit has started.

If, however, the taxpayer had booked the travel before the audit started, or needs to travel overseas for business purposes, their circumstances could be taken into account for remission to the base rate.

EXAMPLE 18

Before the start of an income tax audit in the micro segment, an STS taxpayer goes overseas on a business trip. As a consequence of this travel, the case officer may not be able to complete the audit by the expected audit completion date.

The business trip is legitimate and pre-planned. On return from the trip, the taxpayer cooperates fully and the audit is completed and results in a tax shortfall.

In these circumstances remission to the base rate for the period beyond the expected audit cycle time may be appropriate.

Taxpayer contributed to the delay

Remission of interest charges is not generally warranted if the taxpayer unreasonably delays or obstructs the progress of an audit and the audit is completed beyond the expected audit completion date.

Such conduct includes repeated failure by the taxpayer to:

- keep appointments or supply information, or
- respond adequately to reasonable requests for information.

A worked example is provided in the practice statement.

Taxpayer requests further time (delay)

Interest charges may be remitted to the base rate for the period where the taxpayer requests extra time where the gathering of the information with all due diligence by the taxpayer necessitates that extra time.

EXAMPLE 19

The taxpayer needs six weeks additional time to gather and supply information. The auditor accepts this and allows the time requested. Interest charges would be remitted to the base rate for the period of delay.

The practice statement also provides an example of where interest charges would not normally be remitted.

Taxpayer delay due to an associate or agent's delay

The general principle is that where a delay in establishing a shortfall is caused by a third party, remission of interest charges to the base rate may be warranted for the period of delay.

This principle will generally not apply where the third party is an associate of the taxpayer or not dealing at arm's length with the taxpayer.

Remission based on this ground will not usually be given unless the delay is reasonable and beyond anyone's control.

A delay caused by a taxpayer's tax agent or other representative will generally be considered a delay attributable to the taxpayer. Refer to the practice statement for an example of where a delay caused by a tax agent may be considered reasonable.

Legal professional privilege

Taxpayers may claim legal professional privilege for some documents. Such claims form part of the normal dealings of a taxpayer with the Tax Office.

Reasonable claims for legal professional privilege or access to professional advisors' working papers may lead to cases being completed after the expected audit completion date. In these circumstances, interest charges would generally be remitted to the base rate for the period that goes beyond the audit completion date.

Unprompted voluntary disclosure

As a general principle, if a taxpayer makes a voluntary disclosure of a shortfall (that is, a self-amendment) the disclosure itself is not grounds for remission.

This principle is based on the notion that taxpayers who assess incorrectly, even if they exercise reasonable care, should not end up in a more beneficial position than taxpayers who assess and pay correctly.

However, in some cases the circumstances surrounding the voluntary disclosure will make it fair and reasonable to remit interest charges. In these circumstances remission would generally be to the base rate.

Any remission of interest charges on the basis of voluntary disclosure should consider the factors outlined in paragraph 84 of the practice statement.

EXAMPLE 20

Big Co. Ltd. has an internal assurance practice of reviewing its income tax returns before the statutory time limit for amending assessments expires. As part of this process Big Co. Ltd. identifies a shortfall and immediately lodges an amendment request. As no audit activity was being undertaken or planned by the Tax Office in respect of the issue or income year, remission of interest charges to base rate would be appropriate in this case.

The Tax Office may adopt specific interest rate remission incentives to encourage voluntary disclosure in particular compliance programs. This is dealt with further at paragraph 88 of the practice statement.

Delay in processing requests for amendment by taxpayers

Where a taxpayer self-amends (that is, voluntarily corrects an error in an earlier return or statement), we have published service standards for processing that amendment or adjustment.

Our service standards are available on our website **www.ato.gov.au**

Once we have all the information we need to process an amendment or adjustment, the Commissioner will remit the interest charges for any delay beyond the published standard.

EXAMPLE 21

Raji lodges a 2004-05 amendment request on 1 August 2006. All the information is included in the request. This amendment is lodged in writing (not via ELS), and should be processed within 56 days of receipt, that is by 26 September 2006. Because of a backlog in work, the amended notice of assessment is not issued until 5 October 2006. Remission in full should occur for the period from 27 September 2006 to 4 October 2006.

Advance payment of shortfall amount

If a shortfall amount is subject to shortfall GIC, GIC would stop accruing upon payment of the shortfall.

Paying some or all of a shortfall amount before the issue of an amended assessment does not stop SIC accruing on the total shortfall up to the day before the amended assessment is issued. However, any benefit a taxpayer may have because of non-payment ceases when full payment is made. Therefore, SIC will be remitted in full for the period after full payment has been made.

Such remission is subject to any entitlement to interest on early payment (see next paragraph). Naturally, where a part payment of the shortfall has been made, a partial remission reflecting the portion of the shortfall paid will be given for the post-payment period.

To ensure a revenue-neutral position for the period following payment, the extent of any SIC remission will take into account any interest the taxpayer may be entitled to under the *Taxation (Interest on Overpayments and Early Payments) Act 1983*, in particular, entitlement to interest on early payment (IEP) under Part IIA of that Act.

Any remission of SIC from the date of payment should be reduced by an amount equal to the IEP entitlement that accrues between the date of payment and the day before the amended notice of assessment is issued.

For further information on ‘Interest on Early Payments’ refer to Chapter 82 of the *ATO Receivables Policy*.

An IEP entitlement relating to the period from the date the notice is issued to the due date of the amended assessment does not affect the level of remission.

EXAMPLE 22

After discovering a shortfall, Compliant Pty Ltd lodges an amendment request on 1 July 2006 and on the same date makes a payment of $1,000 – the tax payable on the shortfall. An amended assessment for the $1,000 tax shortfall is issued to the taxpayer on 1 August 2006 and is due for payment on 25 August 2006.

SIC on the $1,000 shortfall is payable for the period from 1 December 2005, the due date of Compliant Pty Ltd's original assessment, to 31 July 2006, the day before the notice of amended assessment is issued to the taxpayer.

However as payment of the shortfall was made on 1 July 2006, remission of SIC for the period 1 July 2006 to 31 July 2006 is justified.

As Compliant Pty Ltd is entitled to interest on early payment (IEP) for the period from 1 July 2006 (the day the early payment was made) to 25 August 2006 (the due date of the amended assessment) the amount of the SIC remission would be determined as follows:

SIC for the period 1 July 2006 to 31 July 2006 less interest on early payment entitlement for period 1 July 2006 to 31 July 2006.

Costs of administration

We may remit interest charge amounts because they are minimal. For example, the imposition of an amount of SIC or GIC below a small threshold will result in remission as part of our automated processes.

Reliance on Tax Office advice or general administrative practice

A taxpayer is protected under the law from the GIC or the SIC that relates to a shortfall if:

- *the taxpayer relies in good faith on advice given to them or their agent by the Commissioner: or a statement in a publication approved in writing by the Commissioner, unless the advice or the statement or publication is labelled as non-binding: or*
- *the taxpayer relies in good faith on the Commissioner's general administrative practice.*

This statutory protection applies:

- to interest charges under a relevant provision (as defined in section 357-55 of Schedule 1 to the TAA), and
- if, on or after 1 January 2006, the taxpayer relied upon the advice, statement or general administrative practice.

In these circumstances, a taxpayer is not liable to pay GIC or SIC to the extent that the charge relates to a shortfall amount. This protection, however, does not apply to any GIC that accrues more than 21 days after the Commissioner notifies the taxpayer of the correct position. In practice, the protection will apply for at least 24 days after the issue of the amended assessment or adjustment.

Refer to subsection 361-5(1) and (2) of Schedule 1 to the TAA regarding statutory protection from the general interest charge and the shortfall interest charge. This applies to things done on or after 1 January 2006.

EXAMPLE 23

John, an STS taxpayer, lodges his 2004–05 income tax return on 5 February 2006. In preparing his return, John contacted the Tax Office on 27 January 2006 for advice about claiming the cost of some repairs to his business premises. He received a general publication about claiming deductions for repairs which incorrectly stated that repairs of a capital nature are also deductible. John relied on this publication and claimed all repair costs as a deduction.

A notice of assessment was issued to John with a due date of 1 May 2006. A later audit of John's tax return determined the repairs were of a capital nature and hence the cost was not deductible.

A notice of amended assessment was issued to John on 1 October 2006 with a due date of 25 October 2006.

Assuming John acted reasonably and in good faith when relying on the publication, statutory protection from SIC on the shortfall amount applies. However, there is no statutory protection for GIC that accrues more than 24 days after the Commissioner issued John with an amended assessment (that is, in this case the due date of the amended assessment). Therefore if John did not pay his amended assessment by 25 October 2006, late payment GIC would apply.

Guidelines for remission of late payment GIC are contained in the *ATO Receivables Policy*.

Statutory protection does not apply if:

- a shortfall arises under a provision that is not a relevant provision, or
- a shortfall amount caused by reliance on a non-ruling advice, statement in a publication approved in writing by the Commissioner, or general administrative practice occurred before 1 January 2006

In situations that do not fall within the relevant statutory protection as described above, the policy for remission of interest charges applies as follows:

- a shortfall may arise as a result of a taxpayer having in good faith followed Tax Office advice, a statement in a publication approved in writing by the Commissioner or a general administrative practice, and
- where the advice, statement or practice is incorrect or misleading and the taxpayer makes a mistake as a result, any interest charges that apply in the period until 24 days after the Commissioner issues a notice advising the taxpayer of the correct position, will be remitted in full.

> This remission policy mirrors the protection given by section 361-5 of Schedule 1 to the TAA.

EXAMPLE 24

John, an STS taxpayer, lodged his 2004–05 income tax return on 5 September 2005. In preparing his return, John contacted the Tax Office on 2 August 2005 for advice about claiming the cost of some repairs to his business premises. He received a general publication about claiming deductions for repairs which incorrectly stated that repairs of a capital nature are also deductible. John relied on this publication and claimed all repair costs as a deduction.

A notice of assessment was issued to John with a due date of 21 November 2005. A later audit of John's tax return determined the repairs were of a capital nature and hence the cost was not deductible.

A notice of amended assessment was issued to John on 1 March 2006 with a due date of 25 March 2006.

Statutory protection from SIC would not apply for the whole shortfall period because the advice was relied on prior to 1 January 2006. However, assuming John acted reasonably and in good faith when relying on the publication, SIC would be remitted in full for the period from 21 November 2005 until 28 February 2006, in accordance with Tax Office policy.

There is no statutory protection for GIC which accrues more than 24 days after the Commissioner issues John with an amended assessment (that is, in this case the due date of the amended assessment). Therefore if John did not pay his amended assessment by 25 March 2006, late payment GIC would apply.

Guidelines for remission of late payment GIC are contained in the ATO Receivables Policy.

Reliance on ATO interpretative decisions (ATO IDs)

ATO IDs are not published as a form of advice but rather as precedential ATO views for tax officers. Nevertheless, our policy is that, if a taxpayer reasonably relies in good faith on an ATO ID by applying it to their own circumstances (which are not materially different from those described in the ATO ID) and that ATO ID is later found to be incorrect, they will not have to pay any interest charge. The precise situation varies depending on whether or not section 361-5 of Schedule 1 to the TAA is applicable. If it:

- is applicable – interest charges are not imposed for the period up until 24 days after the Commissioner notifies the taxpayer of the correct position, or
- is not applicable – interest charges for the period up until 24 days after the Commissioner notifies the taxpayer of the correct position will be remitted in full.

Reliance on subsequently overturned judicial interpretation

An unintended tax shortfall may result where a taxpayer lodges a return or activity statement having regard to a decision of a tribunal or court and afterwards a court of higher authority overturns that decision.

In these situations, SIC or shortfall GIC will be remitted in full, provided that:

- the tribunal or court decision relied upon in the preparation of the return clearly applied to the taxpayer's circumstances, and
- appropriate amendment requests are lodged within a reasonable time after the date of the final court decision. (There may be some circumstances where the Tax Office will initiate amendments).

Interest charges that accrue from the date of the final court decision will not generally be remitted if the taxpayer does not lodge an amendment request within a reasonable time.

Taxpayer could not have been aware of shortfall when lodging return

There may be times when a tax shortfall arises where the taxpayer did not know and could not have known that the shortfall would arise. This may occur, for example, where a return or activity statement is correct at the time of lodgment but future events trigger the need to adjust a liability.

Examples of these types of events are outlined in the practice statement.

In such situations the case officer must review each case on its merit. Where appropriate, full remission may be granted if the amendment request is lodged within a reasonable time after the need to amend arises.

Remission on these grounds only applies if the factual circumstances are such that the taxpayer could not have known about the shortfall when lodging their return.

Contrast this with the situation where the taxpayer mistakenly believed the law operated in a way such that a shortfall would not arise. In these circumstances remission would not be warranted.

Other matters covered in the practice statement

Other matters covered in the practice statement that have not been discussed in this module include:

- Remission as an incentive for some compliance programs
- Tax shortfall offset by a related credit
- Change or potential change in legislation with retrospective effect
- GST 'wash' transactions
- Cases involving the use of the Commissioner's discretion to treat a particular document as a tax invoice or adjustment note

REASONS FOR A REMISSION DECISION

To improve confidence in the objectivity of Tax Office remission decisions, we provide a taxpayer with reasons if they request remission of the shortfall interest charge and we decide not to remit the entire amount.

> Refer to section 280-165 of Schedule 1 to the TAA and section 25D of the Acts Interpretation Act 190, which outlines the rules about the contents of a statement of reasons.

Reasons must be provided where the taxpayer has initiated the remission through making a remission request in the approved form. ('Approved form' has the meaning given by section 388–50 of Schedule 1 to the TAA.) However in all other cases reasons for decisions should be provided in accordance with our commitment under the *Taxpayers' charter*.

These new arrangements do not affect any existing right to request reasons under other administrative law mechanisms such as the *Administrative Decisions (Judicial Review) Act 1977* (ADJR).

OBJECTING AGAINST A REMISSION DECISION

Under the general interest charge regime, there is no mechanism to challenge a remission decision under the tax law. No review of the merits of the decision is available. The ADJR review rights still exist as do our commitments under the Taxpayers' charter.

For shortfall interest charge taxpayers now have a mechanism to challenge our decision if we do not remit the entire amount of the shortfall interest charge.

The objection, review and appeal rights available in Part IVC of the TAA are available if the unremitted shortfall interest charge exceeds 20% of the tax shortfall.

> Refer to section 280-170 of Schedule 1 to the TAA.

Without the 20% threshold, the cost of objections and appeals would be excessive relative to the potential penalty effect from the shortfall interest charge being above loan benefits that taxpayers receive from the temporary use of the shortfall funds.

It is acknowledged that large tax shortfalls can result in large amounts of shortfall interest charge without exceeding the 20% threshold. A large shortfall interest charge does not, in itself, imply a large penalty effect.

Accordingly, formal objection and appeal rights are not available merely because the amount of the shortfall interest charge is large in dollar terms.

The new provision applies regardless of whether we have remitted in full or in part, as long as the total unremitted amount is more than 20% of the shortfall amount.

The new objection provisions apply regardless of whether the remission decision is initiated by the taxpayer or the Commissioner. A remission decision must have been made before objection rights are triggered.

A taxpayer is not required to request remission before objecting to a failure to remit an amount of the shortfall interest charge if the Commissioner has already made a decision not to remit.

> Where taxpayers lack formal appeal rights, this does not prevent the Commissioner from initiating remission of the shortfall interest charge.

EXAMPLE 25: Objecting to remission decisions

Jim's original assessment for the 2004–05 income year was issued on 28 November 2005 with a due date of 22 December 2005.

We amended Jim's original assessment and increased his tax liability by $10,000. He was issued with an amendment on 10 March 2007 with a due date of 3 April 2007. The shortfall interest charge was applied for the period 22 December 2005 to 9 March 2007 (that is, 443 days) and amounted to $1,019.54.

Jim made a written request for a full remission of the shortfall interest charge. We refused the remission request and provided reasons for our decision. Jim could not object to that decision using section 280-170 of Schedule 1 to the TAA, because the unremitted amount of the shortfall interest charge of $1,019.54 does not exceed 20% of the tax shortfall amount of $10,000 (it is only 10.2%).

Jim could challenge the decision under the *Administrative Decisions (Judicial Review) Act 1997* or other administrative law mechanisms.

Furthermore, the Commissioner may remit any amount of the shortfall interest charge (for example, if additional material facts come to light).

04 REFERENCES

CROSS REFERENCING

The following table provides a cross reference between the ROSA recommendations, the relevant legislative provisions and explanatory memorandum paragraphs.

ROSA recommendations	Provisions in the law	EM paragraphs
5.1 From the 2004–05 income year, the standard interest charge applying to income tax shortfalls (that is, the tax difference between the original and amended assessment) should be lower than the GIC rate, reflecting the benchmark cost of finance for a business.	Subsection 280-105(2) of Schedule 1 to the TAA	2.35–2.37
5.2 The new lower uplift factor should be implemented by a separate pre-amendment shortfall interest charge, in lieu of the GIC. GIC will continue to apply to crystallised debts from the new due date.	Section 280-100 of Schedule 1 to the TAA	2.25–2.34
5.3 The Commissioner should have a broad discretion to remit the new shortfall interest charge, where he considers it fair and reasonable. Without limiting the generality of the above: ■ Remission should have regard to the broad intention that shortfall interest be imposed at a uniform rate, rather than being tailored to the circumstances of particular taxpayers. ■ Remission should generally occur where circumstances justify the revenue bearing part of the cost of delayed receipt of taxes.		Section 280–160 of Schedule 1 to the TAA
5.4 Where unremitted shortfall interest exceeds 20% of the tax shortfall, the taxpayer should be entitled to object to the decision not to remit. Objection decisions should be subject to review and appeal where the shortfall interest remaining after determination of the objection exceeds 20% of the tax shortfall.	Section 280-170 of Schedule 1 to the TAA	2.74–2.82
5.5 When notifying taxpayers of a shortfall interest liability, the Tax Office should advise taxpayers on how to seek remission.	Administrative	Not applicable
5.6 The Tax Office should provide reasons for rejecting shortfall interest remission requests.	Section 280-165 of Schedule 1 to the TAA	2.70–2.73

GLOSSARY

The following abbreviations and acronyms are used throughout this module.

ATO ID	Australian Tax Office interpretative decision
Commissioner	Commissioner of Taxation
GIC	General interest charge
GST	Goods and services tax
IEP	Interest on early payment
ITAA 1936	*Income Tax Assessment Act 1936*
ITAA 1997	*Income Tax Assessment Act 1997*
NOA	Notice of assessment
ROSA	Report on aspects of income tax self-assessment
SIC	Shortfall interest charge
TAA	*Taxation Administration Act 1953*
The practice statement	*Law Administration Practice Statement PS LA 2006/8 – Remission of shortfall interest charge and general interest charge for shortfall periods*

MORE INFORMATION

A copy of the *Report on aspects of income tax self assessment* can be found on the Treasury website at **http://selfassessment.treasury.gov.au/content/report.asp**

The *Tax Laws Amendment (Improvements to Self Assessment) Act (No. 1) 2005* [portable document format, 272 kB] can be found on the Tax Office website at **http://law.ato.gov.au/pdf/20050075.pdf**

The *Law Administration Practice Statement PS LA 2006/8 – Remission of shortfall interest charge and general interest charge for shortfall periods* can be found on the Tax Office website at **http://law.ato.gov.au/pdf/ps06_008.pdf**