

Interest and Penalty Tax

Revenue Ruling TAA.007

Replaces TAA.006

Revenue Ruling TAA.007 was ceased on 27 February 2014 due to the issue of Revenue Ruling TAA.007 (version 2) on 28 February 2014

Preamble

The *Taxation Administration Act 1997* (TAA) was introduced on 1 July 1997 to ensure consistency in the administration of taxation laws. Taxation laws, as currently defined in the TAA, include the *Congestion Levy Act 2005*, the *Debits Tax Act 1990*, the *Duties Act 2000*, the *Financial Institutions Duty Act 1982*, the *Land Tax Act 2005*, the *Payroll Tax Act 2007* and the *Taxation (Reciprocal Powers) Act 1987*¹.

Interest and penalty provisions play an integral role in tax administration as they serve the following purposes:

- to deter non-compliance by making it unprofitable for taxpayers,
- to promote equity among taxpayers by ensuring that those who meet their obligations are not disadvantaged in comparison with those who do not, and
- to compensate the Victorian Government for being denied the use of funds to which it is entitled.

The policy intent of the penalty provisions is that the level of penalty should match the degree of culpability and that taxpayers should be encouraged to declare voluntarily any tax liabilities as soon as they are known. This is important given that Victorian taxation legislation frequently adopts the principle of self-assessment that places the onus on taxpayers to exercise reasonable care in the calculation and timely payment of their tax liabilities.

The Commissioner of State Revenue (the Commissioner) will exercise the discretionary powers contained in the interest and penalty provisions to meet contemporary standards of ethical, fair and sensible tax administration². In accordance with the Customer Charter, the Commissioner will start from the presumption that taxpayers have dealt with their tax affairs openly and honestly and, as a consequence, any error made would be due to ignorance or mistake rather than deliberate non-compliance.

Delegates of the Commissioner will assess or remit interest and penalties in accordance with this Revenue Ruling. In addition, they will be responsible for identifying situations where strict application of the Revenue Ruling would produce outcomes which are unreasonable and inconsistent with the stated policy objectives. In such cases, it may be necessary to vary the practices stated in this Revenue Ruling.

The State Revenue Office (SRO) has made some policy changes following a review of its policy and practice in the application of the interest and penalty provisions of Part 5 of the TAA. This Revenue Ruling implements these policy changes and incorporates the minor legislative amendments made to the TAA by the *State Taxation Acts (General Amendment) Act 2005* and the *State Taxation Acts Amendment Act 2007*³.

Ruling

Tax default

A tax default occurs when a taxpayer fails to pay tax in accordance with a taxation law. For example, a tax default occurs when there has been a late payment of tax by a taxpayer or when there has been a tax shortfall meaning that the taxpayer has paid less than the correct amount of tax.

Interest – section 24 of the TAA

If a tax default occurs, interest is calculated on the amount of tax unpaid on a daily basis from the due date for payment until (and including) the day upon which the tax unpaid was paid or a date agreed with the Commissioner (whichever is the earlier).

Interest is payable on tax unpaid and unpaid penalty tax but is not payable on any unpaid interest. Interest is also payable where judgment has been given by or entered in a Court for a debt that is, or includes, an amount of tax unpaid.

Interest rate – section 25 of the TAA

The interest rate consists of the following two components:

- a) A market rate component. The function of the market rate is to reimburse the Victorian Government for the financing costs incurred due to the late payment of tax. This rate equals the Bank Accepted Bills rate unless there is a current order, specifying a different rate, made by the Minister and published in the Government Gazette. On 1 July each year, a new Bank Accepted Bills rate is set automatically for the remainder of the financial year and is the average of the daily yields for 90 day Bank Accepted Bills published by the Reserve Bank of Australia for the preceding month of May.
- b) A premium rate component of 8% per annum. The functions of the premium rate are to penalise taxpayers for the late payment of tax and to deter

similar non-compliance by other taxpayers. Also, the premium rate of interest is applied to make it unattractive for taxpayers to pay other debts in preference to taxation debts and to encourage them to seek business finance to pay their tax liabilities when they fall due. Therefore the premium rate is usually charged for late payments of tax and instalment payments made under approved arrangements to pay arrears of tax.

Minimum amount of interest – section 26 of the TAA

If the amount of interest calculated on tax unpaid is less than \$20, no interest will be imposed.

Remission of interest – section 28 of the TAA

The Commissioner, in such circumstances as the Commissioner considers appropriate, may remit the market rate and premium rate components of interest rate by any amount.

Remission of market rate

The market rate of interest will be remitted only in exceptional circumstances. In determining whether to remit the market rate of interest, the Commissioner will consider whether there is any reason that the Victorian Government should bear the financing costs of revenue forgone as a result of the tax default (and the exposure to the risks and uncertainty of revenue loss).

The market rate of interest may be fully remitted if the SRO has contributed to a tax default by a taxpayer. For example, remission of the market rate may be appropriate if the SRO has been unable to provide a taxpayer with a decision in a timely manner or has provided advice which has been shown subsequently to be incorrect.

Full remission of premium rate

Remission of the whole of the premium rate of interest may occur in the following circumstances where:

- a) the market rate component of interest is partially or fully remitted, or
- b) penalty tax has been imposed in accordance with the taxpayer's culpability for a tax default and there is no need for an additional penalty in the form of premium rate interest.

Partial remission of premium rate

Partial remission of the premium rate of interest may occur where no penalty tax is imposed. The sole purpose of the premium interest is to ensure that a taxpayer with a tax default receives a less favourable treatment than a taxpayer who paid the correct tax on time.

In circumstances where a taxpayer has taken reasonable care to comply with a taxation law, the imposition of premium interest is not required either as a penalty or as a deterrent for others. However, to impose only the market rate of interest on the tax unpaid would place this taxpayer at an advantage when compared with a taxpayer who paid tax on time by borrowing at normal business rate which is likely

to be 3% higher than the market rate. It is therefore considered equitable to remit the premium rate of interest by 5% (from 8% to 3%) for tax unpaid by those taxpayers whose culpability does not warrant a penalty tax or premium interest of 8%.

Penalty tax – section 29 of the TAA

Penalty tax is imposed, in addition to interest, on the amount of tax unpaid when a tax default occurs. Penalty tax is not payable in respect of a tax default which consists of a failure to pay interest or penalty tax previously imposed.

Penalty tax rates – section 30 of the TAA

The standard rates of penalty tax to be applied to tax unpaid are:

- 25 per cent
- 75 per cent if the Commissioner is satisfied that the taxpayer's intentional disregard of a taxation law contributed to the tax default, or
- Zero per cent at the Commissioner's discretion, if the Commissioner is satisfied that:
 - a) the taxpayer took reasonable care to comply with the taxation law, or
 - b) the tax default occurred solely because of circumstances beyond the control of the taxpayer.

The Commissioner will not be satisfied that there were circumstances outside the control of the taxpayer unless the taxpayer took all reasonable steps to avoid or mitigate the tax default.

Reduction in penalty tax – section 31 of the TAA

A taxpayer is entitled to a reduction in the penalty tax rate if the taxpayer voluntarily makes a written disclosure which enables the Commissioner to determine the nature and extent of the tax default. The reduction in the rate of penalty tax is intended to provide an incentive to taxpayers to voluntarily provide full details of a tax default and co-operate with the Commissioner in establishing the exact amount of tax outstanding. The rate of penalty tax is reduced by:

- 80% if a written disclosure is made before the Commissioner commences an investigation into a known or suspected tax default by the taxpayer, or
- 20% if a written disclosure is made during the Commissioner's investigation into a known or suspected tax default by the taxpayer;

Limitation on reduction in penalty tax – section 31(3) of the TAA

The reduction in the rate of penalty tax does not apply to a written disclosure by a taxpayer if:

- a) the tax default involved a failure to lodge a return and pay tax by the due date under a taxation law, or
- b) the taxpayer lodged a return by the due date that disclosed a liability to pay tax but a tax default arose because the taxpayer did not pay that amount of tax by the due date.

The purpose of the restriction in section 31(3) of TAA is to deny a taxpayer who has registered with the SRO to lodge returns and pay tax periodically but failed to meet these obligations, an automatic reduction in the rate of penalty tax. It is the Commissioner's practice to raise an assessment of estimated tax payable when a registered taxpayer has failed to lodge a return and pay tax for a period. However, if the taxpayer subsequently provides a return or information showing that the estimated liability for the period is incorrect, the return or information will not be regarded as a voluntary disclosure before an investigation. A reassessment will be made and penalty tax will be recalculated by applying the rate of penalty tax, used in the initial assessment, to the correct amount of tax.

Increase in penalty tax for concealment – section 32 of the TAA

The prime penalty tax rates determined by section 30 will be increased by 20% if the taxpayer hinders or conceals information during an investigation into a known or suspected tax default by the taxpayer.

Statutory rates of penalty tax

The rates of penalty tax resulting from the application of sections 30, 31 and 32 of the TAA can be summarised as follows:

Penalty Category	Prime Rate %	Voluntary Disclosure Before Investigation %	Voluntary Disclosure During Investigation %	Concealment or Hindrance during Investigation %
Reasonable care or circumstances beyond the control of the taxpayer	0	0	0	0
Failure to take reasonable care but no intentional disregard of a taxation law	25	5	20	30
Intentional disregard of a taxation law	75	15	60	90

Minimum amount of penalty tax – section 33 of the TAA

Penalty tax is not imposed if it amounts to less than \$20.

Remission of penalty tax – section 35 of the TAA

The Commissioner has an unrestricted discretion to remit all or part of any penalty tax imposed in whatever circumstances the Commissioner considers appropriate. It is this discretion which enables penalty tax to be imposed at rates other than those set out in sections 30, 31 and 32 of the TAA.

The Commissioner's classification of tax defaults

In the Commissioner's opinion, the application of interest and penalty should vary according to the nature of the tax default. The Commissioner has classified tax defaults into two categories: late payment tax default and tax shortfall tax default.

Late payment tax default

A late payment tax default occurs when:

- a registered taxpayer pays the correct tax for a return period after the due date for payment, but before the Commissioner has issued an assessment for that period
- a taxpayer lodges a document/statement after the time permitted by legislation and pays the correct duty/tax at the time of lodgement
- a taxpayer fails to pay an assessment (for tax, penalty tax or interest) by the due date shown on the notice of assessment, or
- a taxpayer fails to pay an instalment under an arrangement to pay tax by instalments

A late payment tax default will not be charged penalty tax but will be charged interest at the sum of the market and premium rates.

The Commissioner reserves the right to impose penalty tax for late payment tax defaults if the same registered taxpayer pays tax late more than twice within a financial year. The rate of penalty tax will depend on whether the Commissioner determines that the taxpayer has demonstrated a failure to take reasonable care or intentional disregard of a taxation law.

Late annual adjustment payments for payroll tax will be charged penalty tax because the Commissioner already provides a concession in the form of extra time for payment⁴.

Tax shortfall tax default

A tax shortfall occurs when no tax, or less than the full amount of tax payable, has been paid in accordance with a taxation law. A tax shortfall tax default may include:

- a failure to register and pay tax as required under a taxation law
- the understatement of a liability and the associated underpayment of tax
- the incorrect application of an exemption resulting in an underpayment of tax
- a failure to notify the Commissioner of the cessation of an exemption resulting in an underpayment of tax
- a failure to notify the Commissioner of a breach of the conditions attached to a private ruling.

Penalty tax will be imposed depending on the taxpayer's culpability for the tax default. If penalty tax is imposed, interest will be charged at the market rate only.

If the Commissioner is satisfied that no penalty tax should be imposed because the taxpayer took reasonable care to comply with a taxation law, interest will be charged at the sum of market rate plus premium rate of 3%.

If the Commissioner is satisfied that no penalty tax is payable because the tax default occurred due to circumstances outside the control of the taxpayer, interest may only be charged at the market rate.

If the Commissioner is satisfied that the tax default was caused wholly or partly due to the taxpayer's intentional disregard of a taxation law, penalty tax may be imposed at a rate between 15% and 90%. Under these circumstances, interest will be charged at the market rate only.

If the Commissioner finds that the taxpayer failed to take reasonable care but did not intentionally disregard a taxation law, penalty tax may be imposed at a rate between 5% and 30%. Under these circumstances, interest will also be charged at the market rate only.

Table of interest and penalty charges

The application of interest and penalty tax for various tax defaults is summarised in the following table.

Tax default	Taxpayers culpability	Penalty tax flat rate	Market rate p.a.	Premium rate p.a.
Late payment	N/A	Nil	Yes	8%
Repeated late payment	Treated as a tax shortfall	5% - 90%	Yes	No
Tax shortfall	Circumstances outside taxpayer's control	Nil	Yes	No
	Taxpayer took reasonable care to comply with a taxation law	Nil	Yes	Reduced to 3%
	Failure to take reasonable care but no intentional disregard of a taxation law	5% - 30%	Yes	No
	Intentional disregard of a taxation law	15% - 90%	Yes	No

Taxpayer's culpability when taxpayer's representative has contributed to a tax default

If a taxpayer authorises a person to act as his/her representative or agent in the conduct of his/her tax affairs, the Commissioner will consider any action

of the taxpayer's representative to be an action of the taxpayer. Accordingly, the taxpayer will be responsible for a tax default which arose from the action or failure of the taxpayer's representative. The standard of reasonable care will be judged according to the circumstances and expertise of the taxpayer's representative, however, the liability for penalty tax remains with the taxpayer.

There are circumstances where a tax default was due to a failure of a third party, who is not the taxpayer's representative, to provide timely or accurate information which is necessary to determine the taxpayer's liability for tax. The behaviour of a third party will not influence the Commissioner's determination of a taxpayer's culpability for a tax default. The Commissioner will take into account factors such as whether the taxpayer could reasonably have been expected to know about the accuracy of the information provided by a third party. The Commissioner will also consider whether the taxpayer did all that was possible and reasonable to assist the third party to provide the required information.

Clarification of terms used in this Revenue Ruling

Tax

Tax is defined in section 3 of the TAA to mean a tax, levy, duty and any other amount payable under a taxation law. It also includes interest and penalty tax under part 5 of the TAA.

Taxpayer

A taxpayer is a person who has, or may have, a liability to pay tax. The taxpayer may or may not have received a notice of assessment of the tax liability. A reference to taxpayer in this Revenue Ruling includes a person who is authorised to act as the taxpayer's representative.

Tax unpaid

Tax unpaid refers to a tax liability under a taxation law, which has not been discharged. If, at the time the tax default occurred, there is an overpayment of tax by the taxpayer, such overpayment can be offset against the unpaid tax within the same tax line so that interest or penalty tax is payable on the net amount of unpaid tax. The offsetting of an overpayment against an underpayment of tax must not extend beyond the statutory time limit under the relevant refund provisions of a taxation law.

Reasonable care

A taxpayer is expected to take reasonable care to ensure that they discharge their tax liabilities, however, the standard of reasonable care may vary depending on the taxpayer's circumstances. The SRO recognises that a tax default may occur despite a taxpayer's good intentions and efforts to comply with taxation laws. It is not the SRO's policy to impose penalties for an occasional honest mistake made by a taxpayer.

The standard of reasonable care requires taxpayers to keep complete and accurate records, make diligent efforts to understand and comply with the law, seek expert advice on uncertain or complex matters and be honest in their dealings with the SRO. The following actions, alone or in combination, may indicate that a taxpayer had taken reasonable care:

- a) the taxpayer has maintained appropriate and proper recording systems
- b) the taxpayer has taken reasonable steps to be aware of his taxation obligations and has familiarised himself/herself with the relevant legislation so as not to overlook the legislative requirements
- c) the taxpayer has applied any relevant Revenue Rulings in good faith
- d) the taxpayer has sought professional advice or private rulings for uncertain or complex matters where no Revenue Ruling applied or his/her circumstances differed from those described in a Revenue Ruling
- e) the taxpayer has acted in good faith in applying any independent tax advice received
- f) the taxpayer has observed any private ruling received and has notified the Commissioner of any changes in the information on which the private ruling was provided
- g) the taxpayer has acted promptly to seek advice or provide information once made aware, from any source, that he might have a tax liability
- h) the taxpayer has voluntarily disclosed to the Commissioner, a tax default which was neither known nor suspected by the Commissioner, or
- i) the taxpayer has sought a private ruling from the Commissioner before relying on any legislative exemption or concession which requires the Commissioner to exercise his discretion or grant approval.

There are additional factors which the Commissioner will take into account when determining whether a taxpayer has demonstrated reasonable care, including:

- a) the taxpayer's knowledge of tax legislation and the extent of information available on the taxation issue, particularly where the tax default relates to new legislative provisions which have been in place for less than 12 months
- b) the taxpayer's access to expert advice
- c) the complexity of the law relating to the tax default and whether the taxpayer had a reasonably arguable position (i.e. a position which has legal merit and a substantial chance of acceptance by a court or tribunal)
- d) the extent of the taxpayer's commercial experience and whether the standard accounting or commercial practices in the taxpayer's field of business

contributed to the taxpayer's misapplication of a taxation law

- e) the taxpayer's familiarity with the English language and
- f) the Commissioner's satisfaction that the tax default was due to an isolated, honest, unintended mistake having regard to the taxpayer's compliance history.

Circumstances beyond a taxpayer's control

Circumstances beyond the control of the taxpayer include, but are not limited to, the following:

- postal or delivery delays but not where the taxpayer could arrange for an alternative means of delivery because the taxpayer is aware of the likelihood of a delay
- fires, flood or other natural disasters
- key personnel not available due to sudden resignation, illness or death and
- computer breakdowns including third party systems such as Electronic Funds Transfer systems.

Intentional disregard of a taxation law

It is the Commissioner's view that intentional disregard of a taxation law means a deliberate act or omission by the taxpayer which causes a tax default. This may be determined on the basis of direct evidence of a taxpayer's intention (e.g. admission by taxpayer) or can be inferred from the surrounding circumstances and conduct of the taxpayer.

Examples of conduct, which may demonstrate intentional disregard of a taxation law:

- a) use of contrived or artificial avoidance schemes which prove to be legally flawed
- b) tax evasion or fraud
- c) knowingly making false or misleading records or statements
- d) knowingly concealing relevant facts on a tax liability
- e) ignoring a private ruling or Revenue Ruling of which the taxpayer is aware, particularly on a matter where the law is clearly established
- f) failing to assess in accordance with well established principles of tax law
- g) failing to meet a tax liability after being advised of its existence by the SRO or another person, or
- h) repeating a tax default on a same matter or a closely related matter.

Concealment or hindrance of an investigation

Concealment or hindrance of an investigation means an act or omission by a taxpayer, occurring during the course of an investigation which prevents or hinders the Commissioner from finding the existence, nature or extent of a tax default.

Voluntary disclosures before or during an investigation

A voluntary disclosure before an investigation is one which is made before the commencement of an investigation under Division 2 of Part 9 of the TAA. A voluntary disclosure must be in writing and provide sufficient information to enable the Commissioner to determine the nature and extent of the tax default and assess the correct tax payable.

The penalty tax reduction for a voluntary disclosure before investigation is a concession for taxpayers who co-operate fully in providing the Commissioner with information and thereby avoid the need for a formal investigation. An investigation of a member of a payroll tax group does not mean that the other members of the group are also subject to the same investigation.

A voluntary disclosure during investigation occurs when a taxpayer actively assists the investigation by obtaining, compiling and providing the information necessary to determine the nature and extent of a tax default. A taxpayer's response to the commencement of an investigation will not be considered to be a voluntary disclosure if the taxpayer does no more than respond to requests for information and allow investigators access to books and records. The reduction in penalty tax for a voluntary disclosure during investigation provides an incentive for taxpayers. This reduces the time and work required by investigators to complete an investigation once it has commenced.

Commencement and completion of an investigation

An investigation begins when the SRO informs a taxpayer in writing that an investigation has commenced examining the taxpayer's compliance with one or more taxation laws. An investigation is completed when the SRO has provided a taxpayer with formal acknowledgement that the SRO has completed the investigation.

This Revenue Ruling applies to a tax default that occurs on or after 25 July 2007.

Please note that rulings do not have the force of law. Each decision made by the State Revenue Office is made on the merits of each individual case having regard to any relevant ruling. All rulings must be read subject to Revenue Ruling GEN.001.



July 2007

Commissioner of State Revenue