Calculation of PAYG

PAYG instalment rate

The Commissioner calculates a taxpayer's instalment rate (to two decimal places) using the following formula:

$$\frac{\text{notional tax}}{\text{base assessment instlament income}} \text{ x } 100$$

If either the notional tax or the base assessment instalment income is nil, the instalment rate is also nil.

Base assessment instalment income

The first step in determining the meaning of base assessment instalment income is to determine the taxpayer's “base year”. This is the latest income year for which an assessment has been made. However, if the Commissioner is satisfied that there is a later income year for which the taxpayer does not have a taxable income and therefore no assessment has been made, the base year will be that income year. This could occur where the taxpayer is in a loss position in that year.

➢ **Example 1**

At the time the Commissioner is determining the instalment rate for Enterprises Ltd, the company has lodged its 2014/15 return and has been assessed. The company has also lodged its 2015/16 return which disclosed an overall loss for that year. The Commissioner will determine that Enterprises Ltd's base year is the 2015/16 income year.

The “base assessment” is the assessment for the base year. If the base year is one in which an assessment has not been made (i.e. because the taxpayer was in a loss position), then the base assessment is the return or other information from which an assessment for that year would have been made.

The “base assessment instalment income” is so much of the taxpayer's assessable income taken into account for the base assessment as the Commissioner determines is instalment income.

➢ **Example 2**

Joan Smith's base year is 2015/16. In the assessment for that year, Joan derived $25,000 salary. S30,000 business income, $2,000 interest and incurred S10,000 in business expenses. Joan's base assessment instalment income is $32,000 (i.e. S30,000 + $2,000).

PAYG notional tax

A taxpayer's “notional tax” for the base year is calculated as follows:

$$\textit{adjusted tax on adjusted taxable income} \quad - \quad \textit{adjusted tax on adjusted withholding income}$$

Where a taxpayer's adjusted tax on adjusted withholding income is greater than the adjusted tax on adjusted taxable income for the base year, the notional tax is nil.

In working out a taxpayer's notional tax, the Commissioner may take account of:

- changes in the law that may reasonably be expected to apply to the year for which the Commissioner is calculating the instalment rate and which did not apply in the base year
- proposed changes in the law that, in the Commissioner's opinion, are likely to be enacted and have the effect of lowering the taxpayer's instalment rate

The calculation of superannuation or RSA provider's notional tax is modified to ensure that no-TFN contributions income and the tax offset for no-TFN contributions income are not taken into account.

However the contributions are still assessable contributions that are taken into account when working out the provider's notional tax rid base assessment instalment income.

Adjusted taxable income
A taxpayer's "adjusted taxable income" for the base year is the taxpayer's total assessable income for the base year, reduced by:

- any net capital gains included in assessable income (except if the taxpayer is a superannuation fund, an ADF, a PST or an FHSA trust)
- all deductions allowed for the base year, except tax losses
- if the taxpayer is a company or it is a head company that had tax losses transferred to it, the lesser of:
  ~ any tax loss to the extent that it can be carried forward to the next income year, and
  ~ the deduction for tax losses claimed in the base year, and
- if the taxpayer is neither a company nor a head company that had tax losses transferred to it, any tax loss to the extent that it can be carried forward to the next income year.

Adjusted withholding income
A taxpayer's "adjusted withholding income" for the base year is the amount of assessable income from which PAYG withholding has been, or should have been, made for the base year (except for amounts that have been subject to PAYG withholding because the taxpayer did not quote a TFN or an ABN), reduced by the deductions allowed for the base year to the extent that they reasonably relate to those amounts.

There is no legislative guidance as to what deductions reasonably relate to the amounts from which PAYG withholding has been, or should have been, made. There is also no mention of how such deductions are to be allocated where they do not fully relate to PAYG withholding income.

Adjusted tax
Calculation of the adjusted tax on either the adjusted taxable income or the adjusted withholding income is a four-step process.

Step 1: Calculate the income tax payable on the adjusted taxable income or the adjusted withholding income (as relevant). The following tax offsets are disregarded:

- private health insurance offset
- tax offset arising from franking deficit tax liabilities
- low income tax offset
- offset for superannuation contributions made on behalf of the taxpayer's spouse
- offset for Medicare levy surcharge (lump sum payments in arrears)

Step 2: Calculate the Medicare levy payable on the adjusted taxable income or the adjusted withholding income (as the case may be), disregarding the Medicare levy surcharge.

Step 3: Calculate the amount of any HELP debt and/or FS assessment debt that would have been repayable for the base year on the assumption that the taxpayer's taxable income was equal to the adjusted taxable income or the adjusted withholding income (as the case may be).

Step 4: Add up the amounts determined for steps 1, 2 and 3. From that amount deduct what would have been the taxpayer's family tax benefit (if any) for the base year if the taxpayer's taxable income for the base year had been the adjusted taxable income or the adjusted withholding income (as the case may be). The Commissioner does not reduce the adjusted tax for the taxpayer's family tax benefit.

➢ Example 1: Corporate taxpayer

ABC Ltd derived the following assessable income during the base year:

Gross sales	$120,000
Interest	$10,000
Royalties	$25,000

It incurred the following deductions during the base year:

Cost of sales	$50,000
Tax agent's fees	$2,000

ABC Ltd did not quote its TFN in relation to the interest income and, consequently, $4,650 tax was withheld. On the assumption that the corporate tax rate is 30% for the year for which the instalment rate is calculated, Happy Toys Ltd's instalment rate is calculated as follows:

ABC Ltd's adjusted taxable income	=	assessable income of base year	-	Net capital gains of base year	-	allowable deductions (except tax losses) of base year	-	Tax losses carried forward from base year

ABC Ltd's adjusted withholding income Adjusted tax on adjusted taxable income	=	nil, since amounts subject to PAYG withholding due to the non-quotation of either the taxpayer's TFN or ABN do not count

Adjusted tax on adjusted taxable income

Step 1:	=	Income tax payable on $103,000
	=	30% x $103,000
	=	$30,900
Step 2:		Not applicable
Step 3		Not applicable
Step 4		Add Steps 1 to 3
	=	$30,900 + $0 + $0 - $0
	=	$30,900

ABC Ltd's notional tax is therefore $30,900.

ABC Ltd's base assessment instalment income equals so much of its assessable income for the base year that is instalment income. This would be $155,000 (i.e. $120,000 + $10,000 + $25,000).

$$\text{ABC Ltd's instalment rate} = \frac{\text{ABC Ltd's notional tax}}{\text{Happy Toys Ltd's base assessment instalment income}} \times 100$$

$$= \frac{\$30{,}900}{\$155{,}000} \times 100$$

$$= 19.94\% \text{ (rounded to two decimal places)}$$

➢ Example 2: Individual taxpayer

Mary derived the following assessable income during the year ended 30 June 2016 (the base year):

Salary	$30,000
Net capital gain	$12,000
Interest	$8,000
Dividends (fully franked)	$2,000
Dividend gross-up amount ($2,000 x 30/70)	$857
Total	**$52,857**

She incurred the following deductions during the base year:

Work-related expenses	$800
Interest and dividend deductions	$200

Mary did not quote her TFN in relation to the interest income and, consequently, $3,720 tax was withheld. Further, on her assessment for the year ended 30 June 2016, Mary was allowed a rebate for a superannuation contribution she made on behalf of her spouse, Herbert. Mary does not have an HELP debt or an FS assessment debt and is not entitled to the Family Tax Benefit. Using the personal tax rates for the year ending 30 June 2016, Mary's instalment rate is calculated as follows:

Mary’s adjusted taxable income	=	assessable income of base year	-	Net capital gains of base year	-	allowable deductions (except tax losses) of base year	-	Tax losses carried forward from base year
	=	$52,857 - $12,000 - $1,000 - $0						
	=	$39,857						
Mary’s adjusted taxable income	=	$30,000 - $800						
	=	$29,200						

The interest subject to PAYG withholding due to the fact that Mary did not quote her TFN does not count as adjusted withholding income.

Adjusted tax on adjusted taxable income

Step 1:	=	Income tax payable on $39,857
	=	Tax on $39,857 using 2015/16 rates - franking credit of S857
		$4,500.52 - $857
	=	$3,643.52
Step 2:	=	Medicare levy on $39,857
	=	$39,857 x 2%
	=	$797.14
Step 3:		Not applicable
Step 4:		Add steps Ito 3 and deduct the amount of any family tax benefit
	=	$3,643.52 + $797.14 + $0 - $0
	=	$4,440.66

Adjusted tax on adjusted withholding income

Step 1:	Income tax payable on $29,200
	Tax on $29,200 using 2015/16 rates = $2,090
	$2,090
Step 2:	Medicare levy on $29,200
	$29,200 x 2%
	$584
Step 3:	Not applicable
Step 4:	Add steps 1 to 3 and deduct the amount of any family tax benefit
	$2,090 + $584 + $0 - $0
	$ 2,674

Mary's notional tax is therefore $1,766.66 (i.e. $4,440.66 - $2,674.00).

Mary's base assessment instalment income equals so much of her assessable income for the base year that is instalment income. This would be $10,000 (i.e. $8,000 + $2,000). The dividend gross-up amount is not instalment income as it is statutory income.

$$\text{Mary's instalment rate} = \frac{\text{Mary's notional tax}}{\text{Mary's base assessment instalment income's}}$$

$$= \frac{1{,}766.66 \text{ x } 100}{\$10{,}000}$$

= 17.67% (rounded to two decimal places)

Special rules provide a methodology for the Commissioner to work out one or more instalment rates for a trustee who has more than one PAYG instalment liability in respect of:

- a beneficiary under a legal disability
- a beneficiary that has a vested and indefeasible interest in the trust income but cannot require the trustee to pay that amount to them, and
- income to which no beneficiary is entitled.

GDP-adjusted notional tax

The Commissioner calculates GDP-adjusted notional tax in much the same way as notional tax is calculated. However, the adjusted taxable income for the base year is increased by the GDP adjustment and the adjusted tax is calculated based on this increased adjusted taxable income. Further, the adjusted withholding income for the base year is also increased by the GDP adjustment and the adjusted tax is calculated based on this increased adjusted withholding income.

The GDP adjustment that applies in 2016/17 is 2%. This has no effect if the taxpayer chooses to work out their own instalments (using the 'rate' method) or to pay annually, because the GDP adjustment factor is not applied to the instalments

Benchmark tax and benchmark instalment rate

The calculations of benchmark tax and the benchmark instalment rate are used to determine a taxpayer's liability to penalties where the taxpayer has varied the PAYG instalment rate.

Benchmark tax

Benchmark tax is calculated as follows:

$$\begin{array}{c} \text{adjusted assessed tax on} \\ \text{adjusted assessed taxable income} \end{array} - \begin{array}{c} \text{PAYG} \\ \text{withholding credits} \end{array}$$

If the amount of PAYG withholding credits is greater than the adjusted gross tax on adjusted assessed taxable income, then the benchmark tax is nil (i.e. the above formula cannot produce a negative amount). PAYG withholding credits cover: (a) credits for amounts withheld from withholding payments to the taxpayer during the variation year; and (b) credits for amounts of personal services income included in the taxpayer's assessable income for amounts paid.

A taxpayer's “adjusted assessed taxable income” for a particular income year is the taxpayer's taxable income for that year, reduced by any net capital gains (except if the taxpayer is a superannuation fund, an ADF, a PST or an FHSA trust).

Calculation of the “adjusted assessed tax” on adjusted assessed taxable income for a particular year is a four-step process.

Step 1: Calculate the income tax payable on the adjusted assessed taxable income. The following tax offsets are disregarded:

- private health insurance offset
- tax offset arising from franking deficit tax liabilities
- low income tax offset

- rebate for superannuation contributions made on behalf of the taxpayer's spouse
- offset for Medicare levy surcharge (lump sum payments in arrears)

Step 2: Calculate the Medicare levy payable on the adjusted assessed taxable income, disregarding the Medicare levy surcharge.

Step 3: Calculate the amount of any HELP debt and/or FS assessment debt that would have been repayable for the particular income year on the assumption that the taxpayer's taxable income was equal to the adjusted assessed taxable income.

Step 4: Add up the amounts determined for steps 1, 2 and 3. From that amount deduct what would have been the taxpayer's family tax benefit (if any) for the particular income year if the taxpayer's taxable income for that year had been equal to the taxpayer's adjusted assessed taxable income. The Commissioner does not reduce the benchmark tax for the taxpayer's family tax benefit.

Benchmark instalment rate

A taxpayer's benchmark instalment rate for an income year is calculated using the following formula (calculated to two decimal places, rounded up if the third decimal place is five or more):

$$\frac{\text{taxpayer's benchmark tax for the income year x 100}}{\text{instalment income for that income year}}$$

The “instalment income for that income year” is so much of the taxpayer's assessable income for that income year that the Commissioner determines is instalment income for that year.

➢ **Example**

XYZ Pty Ltd was assessed on the following income during the 2015/16 income year:

Gross sales	$120,000
Interest	$7,500
Net capital gain	$3,500

It also incurred S48,000 in expenses.

XYZ Pty Ltd's adjusted assessed taxable income is $79,500 (i.e. $120,000 + $7,500 - $48,000). The $3,500 capital gain is not taken into account.

XYZ Pty Ltd's adjusted assessed tax on adjusted assessed taxable income, calculated on a 30% company tax rate, is $23,850 (i.e. $79,500 x 30%). Steps 2, 3 and 4 above are not relevant for a non-individual taxpayer.

Accordingly, XYZ Pty Ltd's benchmark tax is $23,850.

XYZ Pty Ltd's instalment income for the 2015/16 income year is $127,500 (i.e. $120,000 + $7,500). The capital gain of $3,500 is not included.
Accordingly, XYZ Pty Ltd's benchmark instalment rate:

$$\frac{\$23{,}850}{\$127{,}500} = 18.71\% \text{ (rounded to two decimal places)}$$