

**CORRECTION**

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**TAXATION LAWS AMENDMENT BILL (NO.3)  
1991**

**INCOME TAX (DEFERRED INTEREST  
SECURITIES)(TFN WITHHOLDING TAX) BILL  
1991**

**MEDICARE LEVY AMENDMENT BILL 1991**

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**EXPLANATORY MEMORANDUM**

Replace pages 150 to 154 inclusive to clarify the examples  
contained therein.

(circulated by authority of the Treasurer,  
the Hon. J. Kerin, M.P.)



**Step 2.** Calculate the amount that would have been deducted for non-quotation of a TFN if the deemed payment amount had been paid to the investor as money. This will be the TFN withholding tax payable jointly and severally by the investor and investment body for the eligible deferred interest investment. It is described in the Bill as the "undeducted TFN amount".

**14.29** When the income from an eligible deferred interest investment is actually paid at the end of the term of the investment, no deductions are required for failure to quote a TFN other than the amount that is included as assessable income under Division 16E for the final year and any periodic interest payment.

***What about Substituted Accounting Periods?***

**14.30** A taxpayer may be given leave to adopt an accounting period, for tax purposes, in place of the normal year of income (i.e. 1 July to 30 June).

**14.31** In calculating the deemed payment amount (step 1) any substituted accounting period that may apply to the investor is ignored. [*Clause 77 - new subsection 221YHZQ(2)*]

***An example of how TFN withholding tax is calculated***

**14.32** Kate invests in debentures with X Bank to the value of \$1,000 for a term of two years commencing on 1 July 1992 and ending on 30 June 1994. Interest will be paid on the debentures at 6% per 6 months compound when the term ends on 30 June 1994.

**14.33** This investment is an eligible deferred interest investment and will thus be subject to TFN withholding tax if a TFN is not quoted.

**14.34** The investment pays assessable income as follows.

<i>Date</i>	<i>Cash Flow(\$)</i>	<i>Written Up Value(\$)</i>	<i>Notional Accrual Amount(\$)</i>
01/07/92	-1,000.00	1,000.00	
31/12/92	0.00	1,060.00	60.00
30/06/93	0.00	1,123.60	63.60
31/12/93	0.00	1,191.02	67.42
30/06/94	1,262.47	1,262.47	71.45

**14.35** "Notional accrual amount" is the amount of accrued interest which must be included in Kate's assessable income under Division 16E.

**14.36** Kate fails to quote her TFN to X Bank. The TFN withholding tax rules are therefore applicable.

**14.37** For the year of income ending 30 June 1993, Kate is assessed on the accrued income earned on the debentures. The amount of income included in her assessment under section 159GQ of Division 16E for that year is \$123.60 (i.e. \$60.00 + \$63.60). Assuming a top tax rate plus medicare levy of 48.25%, the TFN withholding tax payable on the investment for 1992/93 is **\$59.35** (taking account of the rounding off provision in subsection 221YHZC(1C)).

**14.38** The normal TFN rules apply to the first \$138.87 (\$67.42 + \$71.45) of the final payment to the investor since that is the amount of accrued interest earned in the 1993/94 income year (i.e. the year in which the term ends).

**What happens if an investor gets periodic interest as well as deferred interest?**

**14.39** Some deferred interest investments pay income in two ways: by periodic interest and deferred interest:

- Periodic interest is payments of interest (usually by coupon) paid to the investor at intervals of 12 months or less;
- Deferred interest accrues over the term of the investment and is paid when the term ends.

**14.40** Payments of periodic interest are not caught by the TFN withholding tax rules. These payments are subject to the normal TFN arrangements. That is, if a TFN is not quoted by the investor, 48.25% of the periodic interest must be deducted and remitted to the Commissioner. The balance can be paid to the investor. [*Clause 75 - new subsection 221YHZA(2B)*]

**14.41** If a TFN is not quoted on the investment, the deferred interest for years other than the final year of the term is subject to TFN withholding tax.

***Example***

**14.42** Andrew deposits \$1,000 with Z Bank for a four year term commencing on 1 July 1992 and ending on 30 June 1996. The investment earns income by way of:

- periodic payments of interest of \$40 every 6 months; and
- accruing interest paid at the end of the term at 4% per 6 months compound.

**14.43** Andrew's yield to redemption on his investment is 7.53% compound per 6 months.

**14.44** This investment is an eligible deferred interest investment and will thus be subject to TFN withholding tax if a TFN is not quoted.

**14.45** The investment pays assessable income as follows:

<i>Date</i>	<i>Cash Flow(\$)</i>	<i>Written Up Value(\$)</i>	<i>Notional Accrual Amount(\$)</i>
01/07/92	-1,000.00	1,000.00	
31/12/92	40.00	1,035.25	35.25
30/06/93	40.00	1,073.15	37.90
31/12/93	40.00	1,113.91	40.76
30/06/94	40.00	1,157.73	43.82
31/12/94	40.00	1,204.85	47.12
30/06/95	40.00	1,255.51	50.66
31/12/95	40.00	1,309.99	54.48
30/06/96	1,408.57	1,368.57	<u>58.58</u>
			368.57

**14.46** "Cash flow" is the payments of periodic interest and the payment on 30/06/96 which represents \$40.00 periodic interest and \$1,368.57 accrued interest plus capital.

**14.47** "Notional accrual amount" is the amount of accrued interest which must be included in Andrew's assessable income under Division 16E.

**14.48** Andrew fails to quote his TFN to Z Bank. The TFN withholding tax rules are therefore applicable to the accrued interest for the 1992/93 to 1994/95 income years while the normal TFN rules apply to the periodic interest and the accrued interest for the 1995/96 income year.

***Periodic interest***

**14.49** Assuming a top rate of tax plus medicare levy of 48.25%, Z Bank is required to deduct **\$19.30** under the normal TFN rules from each payment of periodic interest when it is paid.

***Accrued interest for 1992/93 income year***

**14.50** For the year of income ending 30 June 1993, Andrew is assessed on the accrued income earned on the term deposit. The amount of income included in his assessment under Division 16E for that year is \$73.15 (i.e. \$35.25 + \$37.90) Assuming a top rate of tax plus medicare levy of 48.25%, the TFN withholding tax payable on the investment for 1992/93 is **\$35.20** (taking account of the rounding off provision in subsection 221YHZC(1C)).

**Who has to pay the TFN withholding tax?**

**14.51** This will depend on whether the investment body is an untaxable Commonwealth entity. Untaxable Commonwealth entities are defined in the Bill to be the Commonwealth or a Commonwealth authority that cannot, by a law of the Commonwealth, be made liable to pay Commonwealth tax [*Clause 77 - new section 221YHZP*]. An example of an untaxable Commonwealth entity is the Reserve Bank of Australia. An example of an investment body which is not an untaxable Commonwealth entity is a bank or building society.

**14.52** Where the investment body is not an untaxable Commonwealth entity, the investor and investment body are jointly and severally liable to pay TFN withholding tax. [*Clause 77 - new paragraph 221YHZT(b)*]

**14.53** Where the investment body is an untaxable Commonwealth entity, the investor is solely liable to pay TFN withholding tax [*Clause 77 - new paragraph 221YHZT(a)*]. In this case, the investor will be taken to have authorised the investment body to pay the tax on behalf of the investor.

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