Personnel Operations Program

Training Workbook

Personnel Calculations &Taxation

Participant's Guide

POP

Personnel Operations Program

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Last Revised
June 2005

CONTENTS

OVERVIEW 3

REFERENCES 4

USING CALCULATORS 5

Percentages 5
Rounding 5
Days, Hours and Minutes Calculations 6

COUNTING DAYS 9

FORMULAS 10

CALCULATING AN EMPLOYEE'S PAY 12

Overtime and Penalty rates 14

SUPERANNUATION 15

ComSuper Calculations (PSS / CSS) 15
EPSC 17
Other Schemes – EPSC only 17

LEAVE ACCRUALS 18

Annual Leave Accrual 18
Annual Leave Loading 18
Long Service Leave Accrual 19
Sick / Personal / Carer's Leave Accrual 20

TAXATION 21

Pay As You Go (PAYG) 21
Terminology 21
Rates of Tax 24
Individual Resident Income Tax Rates 24
Declarations 25
Tax File Number Guidelines 25
Withholding declarations 26
Taxing of Allowances 26
How much to withhold? 26
Rebates and Family Tax Benefit 27
Higher Education Loan Programme 27
Student Financial Supplement Scheme 29
Lump Sum Payment in Arrears 29
Annual Reporting 31

EXTENSION WORK 33

TAX ON TERMINATION PAYMENTS 34

Annual Leave 34
Long Service Leave 34
Annual Leave Loading 35

Other Issues 35
Calculating the Long Service Leave components 37
Normal termination *38*
Termination due to bona fide redundancy or invalidity *39*
Redundancy Pay and Notice Periods 40
What is a bona fide redundancy? 40
Eligible Termination Payment 41
Reasonable Benefit Limits 42

Note: The calculations in this module are based on a standard 7 hour 21 minute day (or 73 hours 30 minute fortnight). This may vary from agency to agency, depending on the particular Certified Agreements or AWA.

OVERVIEW

Objectives

The objective of this course is to provide participants with

- refresher on maths principles
- calculating employee entitlements
- information on the New Tax System and PAYG
- information on how to tax employee entitlements and termination payments.

Target Audience

This training course is suitable for new staff and staff who are required to calculate and tax employee's entitlements and termination payments.

Note

- The general conditions of employment contained in this workbook are based on the APS Award 1998 (the minimum award applying in the APS) and other relevant legislation.

- If an agency has displaced the APS Award in their Certified Agreement, then the only authority applying is the agency Certified Agreement (CA) and other relevant legislation (which cannot generally be displaced by a CA).

- Agencies whose employment arrangements come under the *Public Service Act 1999* may have their own determinations on pay and conditions matters.

- Is it important to know which provisions apply in your agency.

- The calculations in this module are based on a standard 7 hour 21 minute day (or 73 hours 30 minute fortnight). This may vary from agency to agency, depending on the particular Certified Agreement or AWA.

The notes in this workbook do not replace primary reference material.

REFERENCES

- Certified Agreement or Australian Workplace Agreement
- *Long Service Leave (Commonwealth Employees) Act 1976*
- APS Award 1998
- *Income Tax Assessment Act 1936 & 1997*

Tax references:

- PAYG Withholding Tax Tables
- ATO booklet "Unused Annual Leave and Long Service Leave – A guide for employers" dated 1 July 1999 (NAT 3032). This is a useful guide on how to split the LSL components for taxation purposes.
- ATO booklets "ETP - A Practical Guide for Employers in Meeting your Obligations to Employees who Stop Working for You" (NAT 2698) and "ETP - A Guide for Employers on Redundancy of an Employee" (NAT 2702).
- Taxation Ruling TR 94/12 – Income tax: approved early retirement scheme and bona fide redundancy payments

USING CALCULATORS

Calculators are one of the most commonly used pieces of office equipment in personnel/payroll areas. Some models can do time calculations and calculate periods in days.

Some software programs such as spreadsheets can also perform calculations, including quite complex calculations using formulas.

Percentages

Calculating a percentage of a number can be done in several ways

100 x 20% *or* 100 x 0.20 *or* 100 x 20/100 *or* 100 x 1/5

Using the % key on your calculator

15% of 80 =

80 x 15% = 12

or

80 x 0.15 = 12

Exercise 1

Find 15% of 90 ....13.5....

Find 23% of 365 ....83.95....

Rounding

Rounding is an important element in calculations. The general principle of rounding a number is if the value to the right of the number of decimal points you need is 0-4 you round down, and 5-9 you round up.

eg	27.153786	=	27.15	(2 decimal places)
		=	27.154	(3 decimal places)
		=	27.1538	(4 decimal places)
		=	27.15379	(5 decimal places)
	123.36952	=	123.37	(2 decimal places)
		=	123.370	(3 decimal places)
		=	123.3695	(4 decimal places)

When to round to a certain number of decimal places depends on the type of calculation.

The final result of most calculations is either 2 or 4 decimal places, or whole numbers, for example:

- round the result of currency (dollars and cents) to 2 decimal places
- round LSL and annual leave credit to 4 decimal places
- round tax to whole dollars where the tax file number has been provided and ignore any cents where tax file number has not been provided

To round the result of a time calculation from hours, minutes and seconds to hours and minutes, round the minutes down for 0-29 seconds and up for 30-59 seconds.

Note: when using a calculator rounding does not usually occur until the end of a calculation.

Exercise 2

Round the following	28.536475	= 28.54	(2 decimal places)
		= 28.536	(3 decimal places)
		= 28.5365	(4 decimal places)
		= 28.53648	(5 decimal places)

Days, Hours and Minutes Calculations

Calculating days, hours and minutes is one of the most common calculations in personnel. The process can vary between calculators, but is usually fairly similar.

Addition

3 [H] 27 [M] [+] 4 [H] 46 [M] [=] 8 hrs 13 mins 0 secs

Subtraction is similar

7 [H] 51 [M] [-] 3 [H] 57 [M] [=] 3 hrs 54 mins 0 secs

Multiplication

Most calculators will allow you to multiply a number of hours by a decimal and keep the answer in hours (or convert the answer with a hit to the [H] Key), for example:

7 [H] 21 [M] [x] 2 = 14 hrs 42 mins
OR = 14.7 [H] 14 hrs 42 mins

Division is the same:

25 [H] 40 [M] [÷] 3 = 8 hrs 33 mins 20 secs

Some calculators will also allow you to multiply and divide hours and minutes by hours and minutes. However, the answer comes up either, in hours, minutes and seconds, or in decimal format, for example:

36 [H] 45 [M] [÷] 7 [H] 21 [M] [=] 5 (days)

Some calculators might only count to 99 hrs 59 mins, with calculations greater than this converted to a decimal:

7 [H] 21 [M] [x] 15 = 110.25 (hours)

or 110 hrs 15 mins

To convert a decimal of hrs to minutes, multiply by 60, or use the minutes function on your calculator.

0.25 [x] 60 [M] = 15 minutes or

0.25 [H] = 15 minutes (using hrs function)

Remember: when performing calculations on your calculator be consistent with the units you are using, either decimal or hours/minutes, e.g. 7 hours 21 minutes (or 7:21 - the common convention to display hours and minutes) equals 7.35 as a decimal, not 7.21.

When doing a lengthy calculation you only need to hit the ' = ' key when changing between multiply/divide and add/subtract actions ie you can do a series of either multiply/divide steps or add/subtract steps without entering '= '.

To change large numbers of hours to weeks/days/hours/minutes first use your base weekly or fortnightly hours.

Examples

1. Total leave credit = 158.75 hrs (employee works 7:21/day)

   from 158.75 hrs, subtract 147 hrs (4 wks @ 36.75 hrs/wk)

   = 11.75 hrs [H] = 11 hrs 45 mins

   = 11 hrs 45 mins — 7 hrs 21 mins

   = 4 hrs 24 mins

therefore the total = 4 weeks, 1 day, 4 hours, 24 minutes

2. Divide 158.75 hrs by 7.35 (i.e., 7:21 as a decimal)

= 21.598639 (days)

subtract 21 to leave part of a day

= 0.598639 days

multiply by 7 $\boxed{H}$ 21 $\boxed{M}$ $\boxed{=}$ 4 hrs 24 mins

Exercise 3

a. An employee has 160.3 hours of accrued annual leave. How many weeks, days, hours and minutes is this? The employee works 7:21/day.

13·3hrs.

4 WEEKS

239 38·24 b. An employee has 239.64 hours of accrued annual leave. How many days, hours and minutes is this?

235·92

4·44

32 D

4 D 26 M

239·4 ÷ 7·35

32·604081 = 32D. 4H. 26M

COUNTING DAYS

Some calculations in personnel are based on working days of the week (Monday to Friday only), whilst others are based on calendar days (includes Saturday and Sunday). Most salary calculations are based on a 10 day fortnight, however there may be some allowances that are based on a 14 day fortnight.

Calculations for long service leave are based entirely on calendar days. Annual leave and personal sick/carers leave credits are deducted by working days but accrual calculations are based on calendar days service.

Examples

1. How many working and calendar days are there from Thursday 3 March 2005 to Monday 20 June 2005 (inclusive)? 171 - 62 + 1 = 110.

   Working days = 78
   Calendar days = 110

2. Defer an increment that was due on 7 February 2005 by 35 calendar days.

   Increment is payable from 14 March 2005.

Exercise 4

a. How many working and calendar days are there from Tuesday 3 May 2005 to Friday 3 June 2005 inclusive?

   WORKING
   CALENDAR

b. Defer an increment that was due on 5 May 2005 by 43 calendar days.

   17 JUN 2005

FORMULAS

There is a mathematical convention used to prioritise 'order of operations', easily remembered by the term **BODMAS**

Brackets
Of
Division
Multiplication
Addition
Subtraction

Exercise 5

a. Using the BODMAS rule work out the answer to the following:

$4 + 5 \times 9 \div 3 =$ $4+5\times3$ = $4+15$ = 19

If BODMAS wasn't used what other answers are possible:

, 27.

b. Use the BODMAS rule to work out the answer to the following to 3 decimal places:

$14 \div (9 \times 3) + 60 =$ $14 \div 27 + 60$ = 0.5185 = 60.5195

The same rule applies when using the formula for calculating the LSL components for taxation purposes

$$\frac{A}{B} \times \left[\frac{C\,(B + D)}{E} - F \right]$$

Note: *ignore fractions when working out the formula in the square brackets*

$\frac{C\,(B + D)}{E} - F$ *e.g. if answer is 117.88, use 117*

Exercise 6

Using the BODMAS rule, calculate the answer to the following:

$$\frac{46665}{278} \times \left[\frac{8073\ (278+30)}{12358} - 30 \right]$$

$$\frac{46665}{278} \times \left[\frac{8073 \times 308}{12358} - 30 \right]$$

$$167.86 \times [\quad 201.20 \quad - 30]$$

$$\$\,167.86 \times \quad 171.\cancel{2} = \$28{,}704.06$$

DAYS LSL.

CALCULATING AN EMPLOYEE'S PAY

An agency Certified Agreement (CA), Australian Workplace Agreement (AWA) or relevant Award contains:

- the salary rates
- the calculation of fortnightly salary
- the method of payment
- calculation of hourly rates for overtime, restriction duty, etc
- calculation of a part-time salary
- any allowances payable
- and other calculations relevant to the agency.

The most common formula used in the Commonwealth for calculating a fortnightly salary is:

Annual Salary x 12 ÷ 313 = Fortnightly Salary

Why use 12 and 313?

Every 12th year there are 27 pay periods in a financial year. 2004/05 is such a year. To take account of this extra payday a fortnightly salary is worked out over a 12 year cycle, i.e. in 12 years there are 313 paydays.

Example

$$\$52{,}500 \times \frac{12}{313} = \$2012.7795$$

$$= \$2012.78 \text{ (rounded)}$$

This formula can be amended easily to calculate other rates:

- weekly (÷ by 2)
- daily (÷ by 10)
- hourly (÷ by 73.5)
- minute (÷ by 73.5 ÷ 60)

Remember: when calculating figures, do not round until you reach the final figure:

i.e. just leave the full screen on your calculator.

Example

3.5 hrs salary @ $39,650 p.a.

=	$39,650 x 12 ÷ 313
=	$1520.1277 per fortnight
=	$1520.1277 ÷ 73.5 (= hourly rate)
=	$20.682009 per hour
=	$20.682009 x 3.5 hrs
=	$72.387031
=	$72.39 (to 2 decimal places)

You would not normally enter the = key until the end i.e.: 39650 x 12 ÷ 313 ÷ 73.5 x 3.5 = 72.397031

Exercise 7

a. What is the fortnightly salary for an employee receiving $65,000 per annum?

$2,492.01

b. What is the hourly rate for an employee earning $42,000 per annum?

$21.91

Overtime and Penalty rates

Generally, overtime is calculated on a 38 hr wk or 36¾ hr wk, depending on the day worked (unless otherwise prescribed in an agency Certified Agreement).

First find the person's hourly pay rate, using the appropriate "multiplier".

The multipliers are the two common 'hours per week' rates:

Monday - Saturday	= 38 hr/wk
Sunday, and Public Holidays after ordinary hours are worked	= 36¾ hr/wk

Examples

1. 3 hrs overtime for 36¾ week worker on $34,000 p.a. If worked on a weeknight, it's 3 hrs overtime @ 1½X:

$$\$34{,}000 \quad \times \quad \frac{12}{313} \quad = \quad \$1303.514376$$

÷	76 hrs	=	$17.151504 per hour (38 hrs/wk)
x	3 hrs	=	$51.454514 (for 3 hours)
x	1.5	=	$77.181772 (for OT @1½X)
		=	$77.18 (2 decimal places)

2. 6 hours Sunday duty for 36¾ wk worker on $26,300 p.a

$$\$26{,}300 \quad \times \quad \frac{12}{313} \quad = \quad \$1008.3067$$

÷	73.5 hrs	=	$13.718458 (for 36¾ wk divisor)
x	6 hrs	=	$82.310748 (for 6 hours)
x	2	=	$164.62149 (for OT @2X)
		=	$164.62 (2 decimal places)

SUPERANNUATION

ComSuper Calculations (PSS / CSS)

There are currently two contributory superannuation schemes operating in the Commonwealth public service, the Public Sector Superannuation Scheme (PSS) and the Commonwealth Superannuation Scheme (CSS). Generally, employees contribute 5% of their salary to superannuation. However, in the PSS employees may vary this between 2% and 10% and in the CSS between 5% and 10%. The employer also makes a contribution.

The employee superannuation contribution is calculated as follows:

(Annual Salary plus Allowances for Super) ÷ 26 x 0.05

- Round the result <u>up</u> to next 10¢ for CSS
- Round to the nearest cent for the PSS.

Note: When the PSS scheme started in 1990, the original advice from ComSuper was to round to the next 10¢ for the PSS (same as CSS) but later advice stated to round to two decimal places (i.e. nearest cent).

A short cut calculation is simply to divide the superannuation salary by 520 (i.e. 26 ÷ 0.05).

Examples

1. A 5% super contribution in the CSS.

5% on $31,500	=	$31,500	÷	26	x	0.05
	=	$60.57692				
	=	$60.60	(rounded up)			

2. A 5% super contribution in the PSS.

5% on $31,500	=	$31,500	÷	26	x	0.05
	=	$60.57692				
	=	$60.58	(rounded to nearest cent)			

PSSap

The PSSap opened to new APS employees on 1 July 2005.

Employer contributions - employers will contribute at least 15.4% of a member's superannuation salary to their PSSap account, subject to superannuation law.

Personal contributions - members will be able to build their PSSap super further with optional contributions (either before- or after-tax), transfers from other super funds and spouse contributions. Before-tax contributions, otherwise known as salary sacrifice contributions, are subject to individual employers allowing them.

Other Percentages

When an employee wishes to contribute a percentage other than 5% (or 10%), their contribution is first calculated on 5% (including the upward rounding if CSS), then reduced to 1%, then multiplied to take them to their new percentage. The final figure is not rounded.

1. An 8% CSS contribution

8% on $41,500	=	$41,500	÷	26	x	0.05
	=	$79.807692				
	=	$79.90	(rounded up to nearest 10¢)			
therefore 1%	=	$15.98	($79.90 ÷ 5)			
therefore 8%	=	$127.84	($15.98 x 8) (not rounded up to 10c)			

2. An 8% PSS contribution

8% on $41,500	=	$41,500	÷	26	x	0.05
	=	$79.807692	(not rounded up)			
1%	=	$15.961538	($79.807692 ÷ 5)			
8%	=	$127.69	($15.961538 x 8 normal rounding)			

Exercise 8

a. Calculate a 6% CSS contribution on a salary of $65,233

125.443076.
5% 125.50
1% 25.10
$150.60

b. Calculate a 2% PSS contribution on a salary of $43,950

$33.81

Part Percentage Rates

Members of the **CSS** can opt to pay part percentages between 5% and 10%. They can either nominate a percentage ie. 6.5 %, or they can nominate a fortnightly amount that is between 5% and 10% of their superannuation salary.

For example: If their superannuation salary was $41,500 they can elect to pay between $79.90 and $159.80 per fortnight (5% and 10%). They might opt to pay $85.00 per fortnight, which is approximately 5.32%.

EPSC

The Employer Productivity Superannuation Contribution (EPSC) rates that apply for the 2005/2006 financial year are $44.20 for a fortnightly salary of less than $1,473.33, 3% of the member's fortnightly superannuation salary if they earn more than $1,473.33 but less than $2,374.00, $71.22 if the employee's superannuation salary is $2,374.00 or more but less than $3,561.00, and 2% of salary if the employee's superannuation salary is $3,561.00 or more.

Other Schemes – EPSC only

All non-ongoing employees who do not elect to join the PSS or CSS are covered by the *Superannuation (Productivity Benefit) Act 1988.* Under this Act the employer pays Employer Productivity Superannuation Contribution (EPSC) to a fund nominated by the employee, thus complying with the Superannuation Guarantee legislation.

The conditions are generally administered by the ATO and DOFA and information is supplied by DOFA (currently in *Superannuation Circular No 2005/3 June 2005* – available at www.finance.gov.au/super).

For 2005-2006 the following employer contribution rates apply:

Weekly Rate of Salary	***Weekly Contribution***
Less than $150.33	$13.53
$150.33 to less than $2,593.85	9% of salary
$2,593.85 or more	$233.45

When an employee nominates a fund the following conditions must be met:

- the employee must already be a member of the fund
- the fund must agree to accept contributions from the agency, and
- the fund must be a complying superannuation fund under SIS legislation.

If non-ongoing employees do not already have membership in a complying fund then the default fund used is the Australian Government Employees Superannuation Trust (AGEST) which is managed by a corporate trustee Ausgest Pty Ltd. (For all administration enquiries call 1300 724 378; Internet:- www.agest.com.au). There is a list of other funds which may be joined.

An employee joining AGEST should be asked to complete an AGEST membership form on commencement. If no election is made or existing eligible fund information provided within a reasonable period (see agency guidelines) then start payments to AGEST. AGEST will need to be informed of the employee's name, date of birth, AGS number and address.

If contributions are late, interest should be paid at the prescribed rate, using the formula supplied in the DOFA *Superannuation Circular* No 2005/3.

LEAVE ACCRUALS

Leave types that have accruals are Annual/Recreation Leave, Long Service Leave, Personal/Sick Leave and War Service Sick Leave.

Annual Leave Accrual

Agency Certified Agreements contain a variety of accrual conditions. Under the APS Award 1998, the accrual for annual leave is:

$$\frac{A \times B \times C}{D}$$

A = number of hours per week for period
B = number of calendar days to count as service in the period
C = a basic annual leave credit of 4 weeks plus any additional credits for remote locality service as prescribed in APS Award 1998
D = number of actual calendar days in the year of service

Payment In Lieu

Employees are entitled to receive any unused annual leave and any pro-rata annual leave on ceasing APS employment as payment in lieu, calculated as follows:

AL accrued in hours (including pro-rata) x hourly rate using salary on cessation

Exercise 9

How much annual leave will an ongoing employee accrue for the period 1 January 2005 to 30 April 2005?

$$\frac{36.75 \times 120 \times 4}{365} = 48^{h}\ 20^{m}$$

Annual Leave Loading

From 2 January 1996 annual leave loading (ALL) ceased to accrue for most APS employees and was incorporated into base rates of pay. Under the APS Award 1998, only some shift workers and employees in remote localities continue to accrue ALL. The formula for ALL is:

$$\textbf{Annual Salary on 1 January} \times \frac{6}{313} \times 17.5\% \times \frac{\textbf{accrued leave hours on 1 Jan}}{36.75}$$

Long Service Leave Accrual

An employee must have 10 years qualifying service to be eligible for a grant of LSL. Under section 18 of the LSL Act, LSL accrues at the rate of 3/10 of a month for each year of service, represented by the following formula:

Completed years of qualifying service x 0.3

Pro-rata LSL

Where an employee with at least 1 year of service but less than 10 years of service ceases Commonwealth employment due to either minimum age retirement or retrenchment, they are eligible to take any pro-rata LSL which has accrued *or* receive payment in lieu, see subsection 17 (1) and (2) of the LSL Act.

Payment In Lieu

Employees ceasing Commonwealth employment after at least 10 years of service are entitled to receive payment in lieu for any unused LSL credits, see subsection 16 (4) of the LSL Act.

Pro-rata payment in lieu may be made after at least 1 year of service where the cessation is due to:

- age retirement (*minimum*)
- ill health
- death
- retrenchment

Payment in lieu is based on completed years and months of service and salary on cessation, represented by the following formula:

$$\frac{\textbf{Salary on cessation}}{\textbf{12}} \times \textbf{LSL credit}$$

Example

a. An employee has worked for 15 years.

Their LSL credit is: 15 (years) x 0.3 (months) = 4.5 months

Their salary is $63,299. If they ceased Commonwealth employment they would be entitled to payment in lieu.

This amount is: $\frac{\$63{,}299}{12} \times 4.5 = \$23{,}737.12$

Exercise 10

Betty Croker is a non-ongoing employee in your agency. She commenced on 5/10/2004 as a full-time employee on a salary of $41,300 pa and her engagement contract is due to expire on 29/11/2005. Betty's dob is 14/9/1944 and she has no eligible prior service.

a) Calculate Betty's full annual leave accrual for 2005 and the payment in lieu (she has taken the leave she accrued in 2004).

$$\frac{365 \times 333 \times 4}{365} = 134.1123$$
$$= 134^{H}07^{M}$$

$$\$41,300 \times 12 \div 313 \div 73.5 \times 134^{H}07 = \$2889.14$$

b) Is Betty entitled to a payment in lieu of LSL? If so, calculate her LSL entitlement and payment in lieu.

$1 \div 12 = 0.08333$ .12 of YEAR

Service DATE Completed 1yr + 1mth

$= 1.0833 \times 0.3$

$= 0.325$ of a Month

$$\frac{41,300}{12} \times 0.325 = \$1118.54$$

Sick / Personal / Carer's Leave Accrual

These are generally included in a single accrual. The rate and time of accrual vary in agency CAs. The APS Award conditions are complex and are discussed in the Leave Workshop.

War Service Sick leave is also covered in the Leave Workshop.

TAXATION

Employers or payers are obliged to withhold tax from employee's pay and remit the money to the Commissioner of Taxation. All remuneration or rewards for personal services are income and must be included as assessable income. Income is assessed in the year of receipt (not necessarily in the year earned).

Pay As You Go (PAYG)

PAYG withholding is an integrated, comprehensive system that replaced all old withholding tax systems, including Pay As You Earn (PAYE), the Prescribed Payments System and the Reportable Payments System from 1 July 2000.

'Withholding' means the process by which payers deduct amounts from payments made to others (e.g. payees) and send these amounts to the Australian Taxation Office (ATO).

Under PAYG withholding, businesses and other enterprises must deduct amounts from certain payments they make to others, including:

- payments to employees, company directors and office holders
- payments under labour hire arrangements
- payments under voluntary agreements, and
- payments where an Australian Business Number (ABN) has not been quoted.

Terminology

The New Tax System changed certain terms to describe tax concepts and processes:

The New Tax System
Tax file number declaration *(marginal tax rate component)*
Withholding declaration *(family tax benefit or rebates component)*
Payer – a business or entity that makes a payment
Payee – can include a non-individual
Tax tables – various tax tables apply to different types of payments
Payment Summary – different payment summaries apply depending on the payment
Withholder – all government bodies have been determined by the ATO to be *large withholders*
ABN is the no. issued by the ATO identifying the payer

The amount to withhold from payments made to payees is determined mainly by the information provided on a *Tax file number declaration* and a *Withholding declaration* form.

The amount of tax to be withheld is set out in the PAYG Withholding Tax Tables produced by the ATO. The ATO also has a Statement of Formulae to use in computerised payroll systems.

Separate formulas apply to payees who:

- have claimed the tax free threshold and are eligible to receive a leave loading
- have claimed the tax free threshold and are NOT eligible to receive a leave loading
- have NOT claimed the tax free threshold
- have not provided their payers with a valid Tax File Number
- are foreign residents
- have a Higher Education Loan Program (HELP) debt
- have a Student Financial Supplement Scheme (SFSS) debt.

All tax withholding amounts are in whole dollars. Rounding of tax amounts is as follows:

- where the tax file number is provided, round to whole dollars
- where the tax file number is not provided, ignore any cents.

How to work out withholding (tax) amounts from the tax tables

1. Calculate the fortnightly income
2. From column 1 find the closest lower figure to the fortnightly income
3. Use the appropriate column to find the correct amount to be withheld

Example 1

Salary is: $36,127 per annum
$1,385.06 per fortnight

In column 1 locate the closest lower figure, ie $1,384

Tax free threshold with leave loading	$282.00
Tax free threshold no leave loading	$278.00
No tax free threshold	$406.00
No tax file number	$671.00

Therefore the net pay with No LL is:	Salary	$1,385.06
	Tax	$278.00
	Net	$1,107.06

Example 2

Salary is:	$42,058 per annum $1,612.45 per fortnight

In column 1 locate the closest lower figure, ie $1,612

Tax free threshold with leave loading	$354.00
Tax free threshold no leave loading	$350.00
No tax free threshold	$478.00
No tax file number	$782.00

Therefore a net pay is:	Salary	$1,612.45
	Tax (LL)	$354.00
	Net	$1,258.45

If the income is greater than the highest amount on the tax table i.e. greater than $3840 per fortnight, use the instructions at the bottom of page 9 of the tax table to calculate the tax amount.

Example

For Tax free threshold no leave loading

Salary:	$105,000 $4,025.56 per fortnight

In column 1 locate the closest lower figure, ie. $3,840

$3,840	$1,232.00
$4,025 - $3,840 = $185.00	
Tax on $185.00 @ $0.485	$89.73
Add =	$1,321.73
Tax rounded to the nearest dollar	$1,322.00

Therefore the net pay is	Salary	$4,025.56
	Tax	$1,322.00
	Net	$2,703.56

Rates of Tax

The amount to withhold from payments should be in accordance with the PAYG Withholding Tax Tables produced by the ATO. The ATO also provides a Statement of Formulae to use in computerised payroll systems.

The PAYG Withholding tax tables are:

Title	**ATO reference no.**	**Effective for payments from**
Fortnightly Rates* - incorporating Medicare levy with/without leave loading	NAT 1006	1 July 2005
Higher Education Contribution Scheme (HECS)	NAT 2185	1 July 2005
Student Financial Supplement Scheme (SFSS) including statement of formulas	NAT 3307	1 July 2005
Unused Leave Payments on Termination of Employment	NAT 3351	1 July 2000
Eligible Termination Payments	NAT 3349	1 July 2001
Tax table for back payments	NAT 3348	1 Nov 2004

** there are equivalent weekly, monthly and quarterly rates available*

All tax withholding amounts are in whole dollars. Rounding of tax amounts is as follows:

- where the tax file number is provided, round to whole dollars
- where the tax file number is not provided, ignore any cents.

Individual Resident Income Tax Rates

These rates apply to individuals who are residents of Australia for tax purposes.

Tax rates 2004-2005	
Taxable income	*Tax rate %*
\$0 - \$6000	0
\$6001 - \$21600	Nil + 15c for each dollar over \$6000
\$21,601 - \$63,000	\$2,340 + 30c for each dollar over \$21,600
\$63,001 - \$95,000	\$14,760 + 42c for each dollar over \$63,000
\$95,001 +	\$28,200 + 47c for each dollar over \$95,000

Medicare levy is 1.5% of taxable income. For individuals who do not have private hospital cover through private health insurance and taxable income is over \$50,000 (\$100,000 for couples and families), a 1% surcharge applies. The surcharge is calculated on lodgement of the individuals tax return.

Declarations

What a payer needs to know about TFN declarations:

- A TFN declaration should be completed when a payee starts a relationship with a payer, such as starting a job or converting a superannuation entitlement to a pension.
- Payers must send a completed TFN declaration to the ATO within 14 days of the commencement of a payer/payee relationship (can be done electronically).
- If a payee does not provide an effective, complete TFN declaration within 14 days, the payer must complete a declaration with as much payee detail as is available and withhold tax from their salary at the top marginal rate (48.5%).
- For TFN declaration to be 'valid', all the information fields must be completed.
- If a payee has answered question 1 with a cross against "application made to the ATO for a new or existing TFN", then the payer can withhold an amount applicable to a TFN having been quoted. If a payer does not have the payees tax file number after 28 days, the top marginal rate must be withheld from future payments.
- If a payee wishes to vary their rate of tax, they will need to complete a Withholding declaration form, not a TFN declaration.
- A TFN declaration is valid for 12 months from the last payment made to the employee.

Tax File Number Guidelines

The Privacy Commissioner has issued Tax File Number Guidelines under section 17 of the *Privacy Act 1988*. The guidelines dated 21 December 1992 are legally binding and aim to restrict the use of tax file number information.

Unauthorised use or disclosure of tax file numbers is also an offence under the *Taxation Administration Act 1953*. The tax file number rules are also partly contained in the Income Tax Assessment Act 1936.

Storage of Tax File Number Declarations is also subject to these guidelines, and to comply, most agencies keep TFN Declarations in secure (locked) separate storage rather than on personal files.

The guidelines are available on the Privacy Commissioner's website at www.privacy.gov.au, under Privacy Act and Other Laws.

Withholding declarations

The Withholding declaration is a booklet which enables payees to advise their payer of any variations or changes to their tax circumstances.

Payees may complete the declaration for the following reasons:

- When starting a payer/payee relationship to claim an entitlement. A TFN declaration must be completed by the payee, quoting their tax file number (or exemption), before completing a Withholding declaration.
- An existing TFN declaration exists, and they;
  - cease to be an Australian resident for tax purposes
  - claim or discontinue claiming the tax free threshold
  - advise about a HELP debt or a SFSS debt, or changes to them
  - claim an entitlement or variation to an entitlement to the family tax benefit
  - claim an entitlement or variation to an entitlement to a dependant spouse, zone or special rebate.

The Withholding declaration is a 25 page booklet in which the payee completes the worksheets to calculate their entitlement and provides the payer with *only* the completed last page of the booklet. It is recommended that the payee keeps the worksheet calculations for their records.

The declaration should be retained by the payer and does not need to be sent to the ATO.

Taxing of Allowances

Allowances are separately identified payments made to a payee e.g. for working conditions, for qualifications or work related expenses. Payers should ensure allowances are taxed correctly.

For further information on taxing allowances refer to PAYG Bulletin no. 1 – Taxing of allowances for the 2000/01 and future income years, valid from 1 July 2000.

How much to withhold?

Once a payee has completed a TFN declaration and/or a Withholding declaration, the amount the payer must withhold depends on whether the payee:

- has claimed the tax free threshold and is eligible to receive a leave loading
- has claimed the tax free threshold and is NOT eligible to receive a leave loading
- has NOT claimed the tax free threshold
- has not provided a valid Tax File Number
- is a foreign resident
- has a HELP debt or a SFSS debt.

Section 15-15 variation

From 1 July 2000, Australian residents for tax purposes do not pay tax on the first $6000 of their yearly income, known as the tax free threshold.

Where there are 27 pays in a financial year, payees may request an additional amount to be withheld from their earnings to cover any shortfall in tax for the financial year. A table with the additional amount is in the Fortnightly rates tax table.

Where a payee has answered No to the question 'Are you an Australian for taxation purposes?', foreign resident tax rates apply. Details on how much to withhold are in the Fortnightly rates tax table.

Rebates and Family Tax Benefit

A payee must use a Withholding declaration form to advise the payer of their entitlement to a rebate or Family Tax Benefit (FTB). The declaration is effective from the first payday after the payee has provided the form.

If a payee is not claiming the tax free threshold *or* has not provided a tax file number, rebates do not apply (i.e. not allowed when using columns 4 and 5 of the tax table).

Use the Ready Reckoner on page 3 of the tax table to convert the payee's annual rebate or FTB figure to a fortnightly amount. Rebates and FTB reduce the amount in columns 2 and 3 of the tax table.

Example

For Tax free threshold with leave loading

Salary per annum	$43,576
Annual rebate claimed	$1,340

First calculate fortnightly rebate using the ready reckoner

1300 =	49.00
40 =	2.00
Total	$51.00

The ~~net~~ GROSS pay is Salary 1,670.65

tax	372.00
less rebate	51.00
Total tax	321.00
Net	1,349.65

Higher Education Loan Programme

From 1 January 2005 a new suite of loans called the Higher Education Loan Programme (HELP) was introduced. HELP offers Commonwealth loans to assist students to pay their eduction fees and to study overseas. HELP is for eligible students enrolled in Commonwealth supported places. FEE-HELP is a loan that will cover up to the full amount of tuition fees for eligible fee-paying students. OS-HELP is a loan to assist students in covering expenses such as accommodation and travel whilst studying overseas.

A payee who has provided a Tax file number declaration or a Withholding declaration form and has answered yes to the HELP question may need additional amounts withheld from their income.

If their fortnightly earnings are $1,380 or more (2005/2006 rates), use the PAYG Withholding HELP Tax Table to calculate the HELP component. The HELP component is added to the normal tax and increases the amount of tax payable.

Do not add a HELP or SFSS component when using column 5.

Examples

With tax free threshold no leave loading

Salary $36,127 per annum
$1,385.06 per fortnight

Using the HELP tax table find the appropriate income in column 1, i.e. $1,384
The HELP component is found in column 2, i.e. $56.00

The ~~net~~ GROSS pay is	Salary	1,385.06
	tax	278.00
	plus HELP	56.00
	Total tax	334.00
	Net	1,051.06

Salary $49,000 per annum
$1,878.59 per fortnight

Using the HELP tax table find the appropriate income in column 1, i.e. $1,878.
The HELP component is found on page 2, i.e. $112.00.

The ~~net~~ GROSS pay is	Salary	1,878.59
	tax	434.00
	plus HELP	104.00
	Total tax	538.00
	Net	1,340.59

Student Financial Supplement Scheme

The Student Financial Supplement Scheme (SFSS) is a voluntary loan scheme for tertiary students to help cover their expenses while they study. Five years after the loan is taken out the ATO becomes responsible for collecting the outstanding loan. At this stage the loan becomes an accumulated Financial Supplement debt. Compulsory repayments of accumulated Financial Supplement debts are made through the tax system when the person's taxable income reaches the minimum threshold.

If a payee has provided a Withholding declaration and has answered 'Yes' to question 7(b) 'Do you have an accumulated Financial Supplement debt?' and their fortnightly earnings are $1498 or more (2005/2006 rates), use the PAYG Withholding Student Financial Supplement Scheme (SFSS) Fortnightly Tax Table to calculate the SFSS component.

The SFSS component is to be withheld from all earnings, including taxable allowances, bonuses and commissions.

Do not withhold any amount for SFSS from lump sum termination payments.

Lump Sum Payment in Arrears

Where a payee receives a lump sum payment of assessable income, such as salary, wages or allowances (not payments for unused leave), that represents a back adjustment for work already performed, concessional tax treatment may apply.

The tax table for back payments (NAT 3348) issued in November 2004 replaces the previous tax tables on lump sum payments in arrears and bonuses and similar payments. Included in this table are three methods for calculating amounts to be withheld depending on when the payment accrued.

Method A is used when the payment has accrued in the current financial year. Using this method tax is withheld as if the payment had been made in the pay periods to which it relates.

When the payment accrued in a prior financial year but the payment occurs less than 12 months after this use Method B to calculate the withholding amount:

1. Use the relevant tax tables to work out the amount to withhold on the payee's normal earnings for the current pay period
2. Divide the back payment by the number of pay periods over which it accrued
3. Add this figure (disregarding any cents) to the current normal earnings
4. Use the same tax table as previously to determine the amount to withhold on the combined payment amount
5. ~~Subtract the amount worked out in step 1 from the amount worked out in step 4~~
6. Multiply the result by the number of normal pay periods over which the amount accrued to obtain the total amount to withhold from the back payment.

Method C is used to calculate the amount to withhold from back payments of salary or wages that were accrued more than 12 months before the payment date, and all other amounts that accrued in a prior financial year. Method C uses the payee's marginal rate. The steps to calculate this are outlined on page 36.

Lump sum payments for work performed 12 months (or longer) prior to the date of payment which is in excess of $400, must be shown on Label E of the payee's payment summary.

A letter detailing the back payment should also be provided to the payee for inclusion in their tax return. This letter should:

- state the payer's PAYG withholding details including name and address
- state the payee's details including their name, address, and TFN
- provide separate details of each back payment showing the amount accrued, the amount withheld from this payment, and the period to which the payment relates

For further information refer to the *PAYG Withholding Tax table for back payments (NAT 3348).*

Payment Summary

The payment summary records the total payments made, total tax withheld and certain other information about the payee.

There are several different types of payment summaries:

- Payment Summary – Individual Non Business
- Payment Summary – Labour Hire and Other Specified Payments
- Payment Summary – Voluntary Agreement
- Payment Summary - Withholding where ABN not Quoted
- ETP Payment Summary

At the end of each financial year (the period 1 July to 30 June), a payer who has withheld tax from payments made to others must complete a payment summary for each payee and give it to the payee. The payment summary must be given to the payee by 14 July after the financial year.

If a payee ceases employment during the financial year, a payee can request a payment summary at any time. However, the payer should not provide a mid-year payment summary if they provided reportable fringe benefits to the payee. This is because the reportable fringe benefits amount cannot be completed until the end of the financial year.

Annual Reporting

By 14 August after the end of each financial year, the payer must provide a report to the ATO about payments from which they withheld amounts (including nil amounts) if the payments were of the following types:

- salaries, wages, allowances, bonuses or commissions paid to an employee
- payments to company directors
- payments to office holders
- return to work payments
- pensions or annuities
- eligible termination payments
- payments for unused leave
- compensation, sickness or accident payments
- payments under a voluntary agreement, and
- payments under a labour hire arrangement.

Payers can report to the ATO on the approved form or provide copies of all payment summaries issued to payees for the financial year, together with a statement that totals all the amounts from the payment summaries.

Additional Exercises

Working in personnel/payroll, there will be many circumstances when you will be required to manually calculate an employee's salary, tax and other pay adjustments. The documents you have received, e.g. tax tables and payroll calendars are the first of many documents you will need to keep close at hand. These documents will form your own personal reference material.

Using these documents and the previous examples, calculate the following net pays, i.e. the net pay is the fortnightly salary less tax, superannuation and deductions.

1.	Salary	APS2 $36,325 pa	$ 1392.65
	Tax	With tax free threshold no LL	$ 282-00
	Superannuation	CSS 5% contribution	$ 69.90
	Deductions	$55.50 pf life insurance	$ 55.50
		$100.00 pf savings account	$ 100.00
	Total Net Pay		**$** 885.75
2.	Salary	APS6 $57,588 pa	$ 2,207.85
	Tax	With tax free threshold no LL, HELP	$ 538+154
	Superannuation	PSS 5% contribution	$
	Deductions	$75.80 pf health insurance	$
	Total Net Pay		**$**
3.	Salary	APS4 $45,188 pa	$
	Overtime	3 hrs on a Tuesday	$
	Gross	Tax payable on this amount	$
	Tax	No tax file number	$
	Superannuation	PSS 2% contribution	$
	Deductions	$12.50 pf insurance	$
	Total Net Pay		**$**
4.	Salary	APS3 $40,292 pa	$
	Tax	With tax free threshold with LL with rebate of $1,600	$
	Superannuation	CSS 10% contribution	$
	Total Net Pay		**$**
5.	Salary	APS5 $46,426 pa	$
	Tax	With tax free threshold no LL	$
	Superannuation	5% PSS contribution	$
	Deductions	$75.00 pf to credit union	$
		$185.00 pf mortgage	$
		$45.60 pf health insurance	$
	Total Net Pay		**$**

EXTENSION WORK

The following pages detail more advanced aspects of personnel calculations for those already familiar with personnel calculations.

TAX ON TERMINATION PAYMENTS

Annual Leave

On normal termination (e.g. resignation):

- annual leave accrued pre-18 August 1993 is taxed at 31.5% (includes Medicare levy)
  - this is recorded against the Payment Summary Label 'A' and is commonly referred to as Lump Sum A.
- annual leave accrued post-17 August 1993 is taxed at the employee's marginal rate (i.e. the rate of tax applied to the highest rate of salary)
  - this is included in gross payments on the Payment Summary.

Termination due to bona fide redundancy or invalidity retirement:

- all annual leave is taxed at 31.5% (includes Medicare levy)
  - this is recorded against the Payment Summary Label 'A'.

Long Service Leave

On normal termination (e.g. resignation):

- LSL accrued pre-16 August 1978 - 5% of the gross is taxed at the employee's marginal rate.
  - this is recorded against the Payment Summary Label 'B' and is commonly referred to as Lump Sum B.
- LSL accrued from 16 August 1978 to 17 August 1993 (inclusively) is taxed at 31.5% (includes Medicare levy).
  - this is recorded against the Payment Summary Label 'A' and is commonly referred to as Lump Sum A.
- LSL accrued post-17 August 1993 is taxed at the employee's marginal rate (for calculating tax, add this to other components taxed at employee's marginal rate to form one total).
  - this is included in gross payments on the Payment Summary.

Termination due to bona fide redundancy or invalidity retirement:

- LSL accrued pre-16 August 1978 - 5% of the gross is taxed at the employee's marginal rate.
  - this is recorded against the Payment Summary Label 'B' and is commonly ~~referred to as Lump Sum B.~~
- LSL accrued post-15 August 1978 is taxed at 31.5% (includes Medicare levy).
  - this is recorded against the Payment Summary Label 'A' and is commonly referred to as Lump Sum A.

Annual Leave Loading

From 2 January 1996, employees in the APS no longer accrue annual leave loading, with the exception of those in remote localities and shift workers. Employees who continue to accrue a loading are entitled to receive the first $320 of their loading in each financial year untaxed, if they pay tax at the *with leave loading* rate during the year.

The tax rates that apply to loadings are the same as the annual leave tax rates above.

Note - *There would only be a very small number of employees who would have annual leave and leave loading accrued before 18/8/93.*

Other Issues

- If the total post-17/8/93 lump sum payment from normal termination is less than $300, withhold the lesser of:
  - ➢ the amount worked out using the above rates, or
  - ➢ 35.5% of the payment.
- HELP and SFSS is not deducted from lump sum termination payments.
- If the employee has not provided their tax file number and is a resident, the rate of tax must be 48.5% of the lump sum payment (non-resident is taxed at 47%).
- Any tax file number declaration a payee has provided to a payer is effective for the period they were working and for a period of 12 months after the last payment made to them.
- Rounding of tax calculated is as follows:
  - ➢ where tax file number provided, round to whole dollars
  - ➢ where tax file number not provided, ignore any cents.

Calculating the Marginal Rate

There are several steps to calculating the marginal rate tax for the relevant components i.e. the total of 5% of LSL pre-16/8/78, post-17/8/93 LSL, annual leave and leave loadings. The total is treated as if it had been included in each pay over a 12 month period, i.e. over 26 equal parts for fortnightly pays.

1. Total the relevant components and divide by 26
2. Add this amount (the 1/26) to the employee's normal gross earnings* (i.e. fortnightly salary) for the pay period, this becomes the notional gross
3. Work out the amount of tax on the figure obtained in step 2, i.e. notional gross
4. Work out the amount of tax on the normal gross earnings
5. Work out the difference between the tax payable amounts obtained at steps 3 and 4
6. Multiply the difference by 26, this is the tax payable at employee's marginal rate.

***Note:**

Normal Gross Earnings are all payments, except those relating to termination payments, received in the last full week of employment (this includes taxable allowances, overtime, bonuses, etc).

Therefore, an employee's 'normal gross earnings' should be taken to be the earnings relating to the last full pay period worked.

When an employee's pay fluctuates significantly over a number of pay periods, the ATO will accept an average of gross taxable earnings for the financial year to date over the number of pays received.

Where the employee terminates employment after receiving only one full pay in the financial year, the 'normal' pay should be taken to be that pay.

Where no full pay has been received for the financial year, the normal pay should be taken to be the pay received for the last full pay period the employee worked in the previous financial year.

Refer to the ATO booklet "Unused Annual Leave and Long Service Leave – A guide for employers" dated 1 July 1999 (NAT 3032).

Exercise 11

Calculate the amount of tax John Smith needs to pay on the total of $6,504.76. John's annual salary is $30,042 (no leave loading, tax free threshold claimed and TFN quoted).

1. Total components and divide by 26	.... ÷ 26	
2. Add step 1. to the employee's normal gross earnings	.... + ...	
3. Work out the amount of tax on the figure obtained in step 2, i.e. notional gross	tax on	
4. Work out the amount of tax on the normal gross earnings	tax on	
5. Work out the difference between the tax payable amounts obtained at step 3 & 4	.... −	
6. Multiply by 26, becomes the amount of tax payable at employee's marginal rate	.... x 26	

Calculating the Long Service Leave components

Special tax treatment applies to lump sums relating to long service leave. For taxation purposes, the period over which long service leave has accrued to an employee is known as the "**eligible service period**" or ESP. This includes service recognised from previous employment and adjustments made for any breaks in service or leave without pay not to count as service.

The amount of tax an employee needs to pay on a lump sum payment in lieu of long service leave depends on a number of factors. This includes:

- the reason for terminating
- date the eligible service period (ESP) started
- whether any long service leave has already been taken

Note: the eligible service period for taxation purposes is not necessarily the same as the entire period of employment. The eligible service period is the period, or the aggregate of the periods, of employment to which the relevant lump sum termination payment relates; in the case of LSL it's the completed years and months of service, taking into account any leave without pay not to count as service.

Example

Kate commenced on 4 February 1988 and ceased on 11 July 2003. She took LWOP from 1/9/88 – 3/10/88 (33 calendar days), her LSL entitlement is calculated as follows:

period of employment: 4/2/88 – 11/7/03

calculate new LSL date (deferred by the period of lwop): 4/2/88 + 33 days = 8/3/88

completed years and months of service for LSL: 8/3/88 – 7/7/03 = 15 years 4 months (or 15.3333 years)

LSL entitlement: 15.3333 x 0.3 = 4.6000 months

When calculating Kate's eligible service period the dates 4/2/88 to 7/7/03 are used, taking LWOP into account as appropriate.

Normal termination

Where the employee's eligible service period (ESP) started after 15 August 1978, the whole lump sum relates to post-15 August 1978 and post- 17 August 1993 service.

Where the eligible service period (ESP) of the payment started before 16 August 1978, the following information is needed to calculate the post-15 August 1978 and pre-16 August 1978 components:

A	the lump sum amount (i.e. the total amount being paid for unused LSL)
B	the number of whole days of unused LSL
C	the number of whole days in the eligible service period after 15/8/78
D	the number of whole days of LSL used in the eligible service period
E	the number of whole days in the eligible service period and
F	the lesser of the number of days of LSL used after 15/8/78 and the amount calculated by the formula C (B + D) ÷ E

Formula for calculating post-15/8/78 component & post-17/8/1993 component.

$$\frac{A}{B} \times \left[\frac{C\,(B + D)}{E} - F \right]$$

(remember BODMAS when applying the formula)

Steps in applying the formula:

1. calculate the amount of the lump sum that accrued post-15/8/78
2. calculate the pre-16/8/78 by deducting the post-15/8/78 component worked out from the total lump sum
3. calculate the post-17/8/93 by applying the formula again and substituting the reference in C and F from 15/8/78 to 17/8/93
4. recalculate the post-15/8/78 component by deducting the post-17/8/93 worked out from the amount of the post-15/8/78 previously calculated

Note:

- the formula is applied **twice** only when there is pre-16 August 1978 service
- for post 1993 component substitute 15/8/78 with 17/8/93 in C & F of the formula
- when calculating part C of the formula, deduct any relevant LWOPNTCAS that applies to that component
- when calculating part E of the formula (whole days in eligible service period), use the eligible service period as explained in the previous section of the workbook (completed years and months of service)
- ignore fractions when working out the formula in the square brackets

  $$\frac{C\,(B + D)}{E} - F$$ *e.g. if result is 117.88 then use 117*
- if the result is a negative after applying the full formula, then the post-15 August 1978 or the post-17 August 1993 component of the lump sum will be NIL
- for taxation purposes, the formula applies a last in first out method of long service leave taken, so leave accrued last (most recently) is taken to have been used up first. This allows the employee to protect leave accrued in earlier periods of service which is subject to more favourable concessional tax treatment.

Termination due to bona fide redundancy or invalidity

Where the employee's eligible service period (ESP) started after 15 August 1978, the whole lump sum relates to post-15 August 1978 service.

Where the eligible service period (ESP) of the payment started before 16 August 1978, the following information is needed to calculate the post-15 August 1978 and pre-16 August 1978 components:

A	the lump sum amount (the total amount being paid for unused LSL)
B	the number of whole days of unused LSL
C	the number of whole days in the eligible service period after 15/8/78
D	the number of whole days of LSL used in the eligible service period
E	the number of whole days in the eligible service period and
F	the lesser of the number of days of LSL used after 15/8/78 and the amount calculated by the formula $C(B + D) \div E$

Formula for calculating the post-15/8/78 component.

$$\frac{A}{B} \times \left[\frac{C\,(B + D)}{E} - F \right]$$

(remember BODMAS when applying the formula)

Steps in applying the formula:

1. calculate the amount of the lump sum that accrued post-15/8/78
2. calculate the pre-16/8/78 by deducting the post-15/8/78 component worked out from the total lump sum

Note:

- when calculating part C of the formula, deduct any relevant LWOPNTCAS that applies to that component
- when calculating part E of the formula (whole days in eligible service period), use the eligible service period as explained in the previous section of the workbook (completed years and months of service)
- ignore fractions when working out the formula in the square brackets

  $\frac{C\,(B + D)}{E} - F$ *e.g. if result is 117.88 then use 117*
- if the result is a negative after applying the full formula, then the post-15 August 1978 component of the lump sum will be NIL
- for taxation purposes, the formula applies a last in first out method of long service leave taken, so leave accrued last (most recently) is taken to have been used up first. ~~This allows the employee to protect leave accrued in earlier periods of service which~~ is subject to more favourable concessional tax treatment.

Redundancy Pay and Notice Periods

For taxation purposes, the payments received as a result of a redundancy, i.e. redundancy pay and period of notice are combined and treated as bona fide redundancy payments.

Bona fide redundancy payments are tax-free up to a limit calculated according to the years of service of the employee. The limit is indexed each year on 1 July in line with movements in Average Weekly Ordinary Time Earnings (AWOTE).

The ATO issues a taxation determination each year (around May/June) advising of the new rates for the financial year. The latest determination is TD2005/21.

If a bona fide redundancy payment is more than the tax-free limit for the employee, the excess part of the payment is taxed as an *Eligible Termination Payment.*

Note: some payments such as payment in lieu of notice (for separations other than due to redundancy) and compensation for loss of job are paid as an Eligible Termination Payment, not as a bona fide redundancy.

The tax free limit for 2005/06 is $6491 + $3246 for each completed year of service

The tax free amount is shown at label D of the payment summary.

Note:

- although a redundancy payment is limited to a maximum payment of 48 weeks (or 24 years of service), the actual years of service are used in the above formula.
- for part-time employees, the tax-free limit is worked out on the total years of service at the f/t salary rate at date of termination i.e. there is no adjustment for p/t service.

What is a bona fide redundancy?

Under the *Income Tax Assessment Act 1936* (s27F), payments made as a result of a bona fide redundancy qualify for concessional tax treatment. For taxation purposes a genuine or 'bona fide' redundancy is where the:

- employee is dismissed from a job, not left voluntarily
- employee is made redundant (the work has ceased or reduced or the workplace has relocated)
- the termination is before the time retirement or termination would ordinarily have occurred (and in any event before the employee turns 65)
- there is no agreement to employ the person later.

According to Taxation Ruling 94/12, payments made under redundancy packages will qualify for concessional treatment under s27F of the *Income Taxation Assessment Act 1936*, if an employee is dismissed by reason of his or her bona fide redundancy. However, to qualify as a 'bona fide redundancy payment' under s27F, certain conditions must be met, one being that the 'termination time', that is retirement or termination of employment, occurs before the employee turns 65 years.

Therefore there are implications for employees aged 65 years and over who receive redundancy packages. These payments do not meet the definition of a 'bona fide redundancy payment'. Based on verbal advice from the ATO, such payments are treated as an 'eligible termination payment'.

Eligible Termination Payment

Certain lump sum payments paid by employers on termination of employment are Eligible Termination Payments (ETPs). They include lump sum payments made upon resignation, retirement or death, but do not include payments for unused annual leave or long service leave. An ETP can be made up of different tax components, and the process can be involved.

The Australian Taxation Office has produced several publications to assist employers, including:

- PAYG Withholding Tax Table on Eligible Termination Payments
- ETP - A Practical Guide for Employers in Meeting your Obligations to Employees who Stop Working for You
- ETP - A Guide for Employers on Redundancy of an Employee.

There are several steps in the ETP process which are fully detailed in the above publications. Briefly the steps are:

1. Decide if any part of the lump sum payment is an ETP
   only certain payments paid to an employee on termination are ETPs
2. Calculate the ETP components
   use the eligible service period to correctly work out the ETP components
3. Give the employee a payment choice
   before you pay an ETP, you can give the employee the opportunity to roll-over the ETP into a roll-over fund for their retirement or to be paid in cash
4. Paying the ETP to a roll-over fund
   certain procedures need to be followed to roll-over an ETP
5. Paying the ETP in cash
   when paying an ETP in cash you need to apply the correct tax rates to the different ETP components, and issue an ETP Payment Summary
6. Reporting information to the ATO
   cash payments need to be reported, this can be done electronically
7. Record keeping
   records must be kept for 5 years, this can be done electronically

Note: *The amount rolled-over is not taxed at the time of payment; it is only the amounts taken as cash which are taxed on payment.*

Reasonable Benefit Limits

Reasonable Benefit Limits (RBLs) are the maximum amount of retirement and termination of employment benefits that individuals can receive over their lifetime at concessional (reduced) tax rates. Amounts over this limit are taxed at higher rates when a person lodges their income tax return. The ATO advises a person when any ETP or other retirement payments they receive are over their RBL.

There are two types of RBLs - a lump sum RBL and a pension RBL. For the financial year 2005/06 the lump sum RBL is $648,946 and the pension RBL is $1,297,886.

The upper limit for the post-June 1983 component of an ETP is $129,751 for the 2005/06 financial year.

The limit is indexed each year on 1 July in line with movements in AWOTE. The ATO issues a taxation determination each year (around May/June) advising of the new rates for the financial year.

An employer must report cash payments of more than $5000 gross, to the ATO on a RBL form. Only cash payments are reported, not roll-over payments.

The RBL form is to be lodged by the employer before the 14th day of the month after the month in which the ETP was paid. For example, an ETP paid on 26 July 2005 must be reported by 14 August 2005.

A copy of the information reported to the ATO must be given to the employee for their records.

Exercise 12

Sarah Lee commenced in the APS on Monday 3 August 1971. Sarah is excess to requirements and is terminated on Friday 24 June 2005 (without the required period of notice). Sarah's salary on cessation is $44,350 and her date of birth is 3/3/51.

Under the APS Award 1998;

Redundancy pay is based on 2 weeks salary for each completed year of continuous service, plus a pro-rata payment for completed months of service since the last completed year of service. The minimum sum payable is 4 weeks salary and the maximum payment is 48 weeks salary.

Where an excess employee is terminated, the period of notice is 4 weeks. In the case of an employee over 45 years of age with at least 5 years continuous service the period of notice is 5 weeks. Where the Agency head directs, or the employee requests, a termination date within the notice period, the employee's employment will terminate on that date. The employee will be paid compensation instead of notice for the unexpired portion of the notice period.

a) Calculate Sarah's redundancy pay.

b) Calculate the payment in lieu of notice.

c) Calculate the tax free component.

Exercise 13

Dave Jones started in the Department of Fine Arts on 15 November 1993. Dave is excess to requirements and is terminated on 31 August 2005 (without the required period of notice). Dave's salary on cessation is $82,139 and his date of birth is 5/6/65.

a) Calculate Dave's redundancy pay and payment in lieu of notice.

b) Calculate the tax free component.

c) How much of this is an Eligible Termination Payment?

d) Dave wishes to take the ETP as cash, what rate of tax is payable?

Note: Normally, employer/payer type ETPs fall into the category of Post June-83 untaxed component. An exception is the occasional ETP related to the lieu of notice period on retirement due to illness. Refer to the PAYG Withholding tax table on Eligible Termination Payments for the tax rates.

e) What must be issued to Dave, as a consequence of the ETP?