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## Taxation Determination

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Income tax: is an outgoing incurred by a business taxpayer for a gift provided to a former or current client deductible under section 8-1 of the *Income Tax Assessment Act 1997*?

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This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

### Ruling

1. Yes, a taxpayer who carries on a business is entitled to a deduction under section 8-1 of the *Income Tax Assessment Act 1997* (ITAA 1997) for an outgoing incurred on a gift made to a former or current client if the gift is characterised as being made for the purpose of producing future assessable income.
2. The outgoing is not deductible where it is of a capital nature, relates to the gaining of exempt or non-assessable non-exempt income, or some other provision of the income tax law prevents it from being deductible.

### Example 1

3. *Sally is carrying on a renovation business. Sally gifts a bottle of champagne to a client who had a renovation completed within the preceding 12 months.*
4. *Sally expects the gift will either generate future business from the client or make them more inclined to refer others to her business. Although Sally got on well with her client, the gift was not made for personal reasons and is not of a private or domestic character.*

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5. *The outgoing Sally incurred for the champagne is not of a capital nature.*
6. *Sally is entitled to a deduction under section 8-1 of the ITAA 1997.*

## **Example 2**

7. *Bernard is carrying on a business of selling garden statues. Bernard sells a statue to his brother for \$200. Subsequently, Bernard gifts a bottle of champagne to his brother worth \$170. Apart from his transaction, Bernard provides gifts only to clients that had spent over \$2,500 over the last year.*
8. *The gift has been made for personal reasons, and is of a private or domestic character.*
9. *Bernard is not entitled to a deduction under sections 8-1 or 40-880 of the ITAA 1997.*

## **Date of effect**

10. This Determination applies to years of income commencing both before and after its date of issue. However, this Determination will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

## Appendix 1 – Explanation

**❶ This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.**

11. Section 8-1 of the ITAA 1997 allows a deduction for losses or outgoings to the extent that they are incurred in gaining or producing assessable income or are necessarily incurred in carrying on a business for that purpose. However to the extent that the losses or outgoings are of a capital, private or domestic nature, or relate to gaining or producing exempt income or non-assessable non-exempt income, they will not be deductible. In addition, losses or outgoings will be not deductible under section 8-1 of the ITAA 1997 to the extent that another provision prevents a taxpayer from deducting them.

12. Losses or outgoings are incurred in gaining or producing assessable income where they are 'incidental and relevant to that end' (*Ronpibon*).<sup>1</sup> Where a taxpayer is carrying on a business for the purpose of gaining or producing assessable income, voluntary expenditure incurred for business needs may be deductible. It is the taxpayer who decides whether the expenditure 'is dictated by the business ends to which it is directed' (*Snowden & Willson*).<sup>2</sup>

13. If a taxpayer provides a gift that is characterised as being made for the purpose of producing future assessable income, the outgoing incurred on the gift will be incidental and relevant to gaining or producing assessable income. The taxpayer's outgoing is 'dictated by the business ends to which it is directed' and is necessarily incurred in carrying on a business for the purpose of gaining or producing assessable income.

14. Section 40-880 (about unrecognised business-related expenditure) does not provide relief for expenditure of a private or domestic nature.<sup>3</sup>

15. Deductibility under section 8-1 of the ITAA 1997 is subject to there being no other provision in the tax law that affects the deduction. These situations include:

- where the gift is a bribe to a foreign official (section 26-52 of the ITAA 1997) or a public official (section 26-53 of the ITAA 1997)
- where the gift is the provision of entertainment (section 32-5 of the ITAA 1997)
- where the gift is within the prepayment rules (Subdivision H or Division 3 of Part III of the *Income Tax Assessment Act 1936*).

<sup>1</sup> *Ronpibon Tin NL & Tongkah Compound NL v. Federal Commissioner of Taxation* [1949] HCA 15 at [14]

<sup>2</sup> *Federal Commissioner of Taxation v. Snowden & Willson Pty Ltd* [1958] HCA 23; (1958) 99 CLR 431 at 437. See also *Re Magna Alloys & Research Pty Ltd v. Commissioner of Taxation of the Commonwealth of Australia* [1980] FCA 150; (1980) 49 FLR 183 in which the Court, citing *Ronpibon* and *Snowden and Willson*, stated:

The requirement that the claimed outgoing be "necessarily" incurred in carrying on the relevant business does not, in the context, mean that the outgoing must be either "unavoidable" or "essentially necessary". Nor does the word "necessarily" import a requisite of logical necessity. What is required is that the relevant expenditure be appropriate and adapted for the ends of the business carried on for the purpose of earning assessable income... For practical purposes and within the limits of reasonable human conduct, it is for the man who is carrying on the business to be the judge of what outgoings are necessarily to be incurred.

<sup>3</sup> See paragraph 40-880(5)(i).

## References

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*Previous draft:*

Not previously issued as a draft

*Related Rulings/Determinations:*

TR 2006/10

*Legislative references:*

- TAA 1953
- ITAA 1997
- ITAA 1997 8-1
- ITAA 1997 26-52
- ITAA 1997 26-53
- ITAA 1997 32-5
- ITAA 1997 40-880
- ITAA 1997 40-880(5)(i)

- ITAA 1997 Div 30

*Cases relied on:*

- Ronpibon Tin NL and Tongkah Compound NL v. Federal Commissioner of Taxation (1949) 78 CLR 47; [1949] HCA 15
- Magna Alloys & Research Pty Ltd v. Federal Commissioner of Taxation 80 ATC 4542; (1980) 11 ATR 276
- Federal Commissioner of Taxation v. Snowden & Willson Proprietary Limited (1958) 99 CLR 431; [1958] HCA 23

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ATO references

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