



TD 2007/18 - Income tax: consolidation: in applying the statutory cap in section 705-40 (tax cost setting amount for reset cost base assets held on revenue account) of the Income Tax Assessment Act 1997, does the definition of revenue asset in section 977-50 of that Act include any CGT asset, a hypothetical realisation of which would have an amount reflected in the joining entity's taxable income (disregarding the single entity rule), otherwise than solely as a capital gain or capital loss?

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Taxation Determination

Income tax: consolidation: in applying the statutory cap in section 705-40 (tax cost setting amount for reset cost base assets held on revenue account) of the *Income Tax Assessment Act 1997*, does the definition of revenue asset in section 977-50 of that Act include any CGT asset, a hypothetical realisation of which would have an amount reflected in the joining entity's taxable income (disregarding the single entity rule), otherwise than solely as a capital gain or capital loss?

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Ruling

1. Yes. The definition of revenue asset in section 977-50 of the *Income Tax Assessment Act 1997* (ITAA 1997)¹ as it applies in section 705-40, extends to all CGT assets (except trading stock and depreciating assets) where any profit or loss on realisation would be reflected in the joining entity's taxable income, otherwise than solely as a capital gain or capital loss.
2. A profit or loss would include a gain, receipt, loss or outgoing that would arise if that asset was realised.

¹ All references to legislative provisions in this Taxation Determination are to provisions of the ITAA 1997.

Example

3. *Sub X was an investment company, which held a significant number of assets. Predominantly the assets were shares held for investment purposes, cash and real property (offices) from which its business was conducted. Overall, the investment portfolio had doubled in value since acquisition, however the value of the office property, which was acquired at the height of a boom, was half what was paid to acquire it.*
4. *Sub X's investment strategy for its share portfolio was to maximise dividend yields. Where the dividend yield on investments fell, Sub X's strategy meant that those shares would be sold and the proceeds invested in other shares with a higher dividend yield. Sub X never acquired shares for the purpose of profit-making by sale, although it recognised that its investment strategy meant that shares would be sold from time to time. In times of rising share values but falling dividend yields, 'switching' between investments would be significant.*
5. *Head Co owned all the membership interests in Sub X, and the Head Co consolidated group was formed on 1 July 2006, with Head Co as the head company and Sub X as a member.*
6. *Head Co's business involved a number of activities, enterprises and undertakings, and it held a range of investments, some as revenue assets and some as long term investments that were clearly on capital account.*
7. *Although only a small proportion of the Sub X portfolio was ear-marked for imminent sale at any given time, it is considered that the entire Sub X investment portfolio constituted revenue assets in accordance with the definition in section 977-50. All the investments were held on the basis that, hypothetically, they could be sold as part of Sub X's normal business activity, and if sold at a profit would constitute ordinary income (per London Australia Investments Co Ltd v. FC of T (1977) 138 CLR 106; 77 ATC 4398; (1977) 7 ATR 757).*
8. *Section 977-50 requires a realisation of the assets to be hypothesised, such hypothesis being based on the assumption that the single entity rule would not apply (subsection 701-10(2)).*
9. *Because of Sub X's overvalued office property (which is not a revenue asset), the allocable cost amount (ACA) available to be allocated to Sub X's reset cost base investments under the tax cost setting process (applying item 1 of subsection 705-65(1), section 705-60 and paragraph 705-35(1)(c)), exceeded both the market and terminating values² for those assets.*
10. *The application of section 705-40 meant that the ACA relative to the overvalued office property could not be applied to the investment assets beyond those assets' market values or terminating values.*
11. *The ACA consequently not able to be applied to the investment assets would be reallocated among other reset cost base assets to the maximum extent possible (paragraph 705-40(3)(c)), and failing that, treated as a capital loss of Head Co in accordance with CGT event L8 (section 104-535).*

² Under section 705-30.

Date of effect

12. This Determination applies to CGT assets that are consumables,³ under arrangements begun to be carried out from its date of issue. For all other CGT assets, this Determination applies both before and after its date of issue.⁴ However, the Determination does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

13. From December 2003 until 3 May 2007, the Consolidation Reference Manual (CRM) contained a Note⁵ to a worked example dealing with consumables brought into a group. That Note said that a consumable is not a revenue asset 'since its cost rather than a net loss, is allowed as a deduction.' That Note has now been withdrawn from the CRM. There were (and are) no other references to revenue assets in the CRM.

14. Although a general (and incorrect) reason was given in the Note as to why consumables were not considered to be revenue assets, the Note dealt only with the topic of consumables. Therefore taxpayers who relied on the Note in relation to consumables are entitled to adopt the position outlined in the CRM up until the date of issue of this Determination. Taxpayers with CGT assets other than consumables would not have been entitled to rely on the Note as representing the Commissioner's view of the law in relation to revenue assets generally and therefore the Determination applies to all CGT assets other than consumables, both before and after its date of issue.

Commissioner of Taxation30 May 2007

³ Consumables are assets that are destroyed or cease to exist as soon as they are used, such as fuel. They are not depreciating assets as defined in subsection 40-30(1). They are also distinguished from trading stock which includes raw materials and other assets, such as parts, that are incorporated into a final asset.

⁴ Taxation Ruling TR 2007/7 sets out the Commissioner's view about how Subdivision 705-E and section 104-525 apply to errors made in working out tax cost setting amounts of reset cost base assets. Such errors may include the mischaracterisation of assets for tax cost setting purposes.

⁵ First at C9-5-340, and then transferred to C9-5-341.

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.*

Explanation

Background and context

15. The definition of revenue asset in section 977-50 applies for the purposes of the consolidation provisions (Part 3-90, for example, section 705-40), as well as CGT roll-overs (for example, Division 615), loss integrity (Subdivisions 165-CC and 165-CD) and value shifting (Part 3-95) rules.

16. The meaning of the words of the definition is dependent on the context of the provisions in which the definition is used.⁶ Gibbs CJ in *Cooper Brookes (Wollongong) Pty Ltd v. FC of T (Cooper Brookes)*⁷ said:

It is only by considering the meaning of the words used by the legislature that the court can ascertain its intention ... Of course, no part of a statute can be considered in isolation from its context – the whole must be considered.

17. This Taxation Determination therefore only considers the meaning of the term revenue asset as it applies in the context of the consolidation provisions, in particular section 705-40.

18. The Explanatory Memorandum to the introduction of section 705-40 stated that it was designed to prevent unrealised capital losses being converted to revenue losses when an entity joins a consolidated group.⁸ It does this by capping the tax cost setting amount of a revenue asset at the greater of its market value, or the joining entity's terminating value. Any resulting reduction to the revenue asset's tax cost setting amount is allocated among the other reset cost base assets to the maximum extent possible, and failing that, is instead treated as a capital loss of the head company (paragraph 705-40(3)(c) and the note to subsection 705-40(2)).

19. Section 705-40 applies also to depreciating assets and trading stock.

20. Given that the stated purpose of the provision (as outlined in paragraph 18 of this Determination) is to prevent unrealised capital losses being converted to revenue losses, it is reasonable in this context to infer that the provision was intended by the legislature to have the broadest application necessary to achieve that purpose, rather than a narrower operation. However, that inference must be able to be drawn from the words of the provisions themselves before the provisions can be applied in that way.

⁶ Although there is a basic rule of statutory construction that a particular word or phrase should be interpreted consistently throughout the one statute, it is well-accepted that the rule is not a strict one, and context is paramount: see Gibbs CJ in *Clyne & Another v. DFC of T (NSW)* 81 ATC 4429 at 4433.

⁷ 81 ATC 4292 at 4296.

⁸ See paragraph 5.37 of the Explanatory Memorandum to the New Business Tax System (Consolidation) Bill (No. 1) 2002 (Act No. 68 of 2002).

21. It should be noted here that section 705-40 applies from the perspective of the joining entity, rather than that of the head company of the consolidated group. The object of section 701-10 is to recognise the cost to the head company of the assets of the joining entity as the amount reflecting the group's cost of acquiring the entity. Under subsection 701-10(4) the tax cost for each asset of the joining entity is set at the time it becomes a subsidiary member of the group, at its tax cost setting amount. Importantly, subsection 701-10(2) provides that the section applies in relation to each asset of the joining entity on the basis that the single entity rule in subsection 701-1(1) does not apply.

22. The effect of subsection 701-10(2) is that section 705-40 must be applied to each asset of the joining entity at the joining time as if the single entity rule was not in effect. Whether an asset is one to which section 705-40 applies will depend on the character of the asset of the joining entity at the joining time, on the basis that the operation of the single entity rule is excluded.⁹

Relevant provisions

23. Section 977-50 defines a 'revenue asset' as any CGT asset (where the asset is neither trading stock nor a depreciating asset) where:

the profit or loss on your disposing of the asset, ceasing to own it or otherwise realising it, would be taken into account in calculating your assessable income or tax loss, otherwise than as a capital gain or capital loss.¹⁰

24. The former definition of revenue asset was contained in subsection 705-40(2). It was in some respects narrower (for example, only covering disposals rather than other realisations) and in other respects broader (for example, covering all assets for consolidation purposes¹¹ rather than just CGT assets). In some respects the two definitions were simply different, for example in the former referring to taxable income rather than assessable income.

25. Section 705-40 was replaced by the same Act that introduced section 977-50. The replacement was stated in the Explanatory Memorandum¹² as being necessary to adopt the new definition in section 977-50, and also to cover trading stock and depreciating assets to 'preserve the class of assets presently covered by that rule'.

26. It would seem, therefore, that the replacement section 705-40 was intended to operate at least on a similar basis to that on which it previously operated. However, while the former definition applied on the hypothesis of a disposal by the head company, the amendment to subsection 701-10(2) (see paragraphs 21 and 22 of this Determination) means that it now applies on the hypothesis of a disposal by the joining entity.

⁹ This is not how the provisions were originally enacted. When section 977-50 was introduced in 2002, subsection 701-10(2) said that the cost to a head company of assets of a joining entity applied 'for each asset that becomes an asset of the head company because ... (the single entity rule) applies.' Subsection 701-10(2) was amended in 2004, retrospective to 1 July 2002, to recognise the cost to the head company of the assets of the joining entity on the basis that the operation of the single entity rule is excluded.

¹⁰ The Explanatory Memorandum to the New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Bill 2002, which introduced the definition, provides no further guidance. Paragraph 12.24 of the Explanatory Memorandum addresses what is a revenue asset solely in terms of the wording of its definition, together with what are realisation events for revenue assets (that is, where there is an actual, as opposed to hypothetical, realisation).

¹¹ See Taxation Ruling TR 2004/13 on the meaning of asset for the purposes of Part 3-90.

¹² Paragraph 1.29 of the Explanatory Memorandum to the New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Bill 2002.

27. Regardless of that background, as the new definition was introduced without exclusive reference to the consolidation measures, and in terms that materially differ from the old definition, it is not possible to draw any particular inference about the meaning of the term revenue asset in section 977-50 from the terminology of the former internal (consolidation) definition.

28. The definition in section 977-50 uses a combination of legal, economic/commercial and tax concepts. The way in which the provision addresses assets on which revenue gains would accrue is significantly defined by reference to those assets which would be excluded – that is, CGT assets (where realisation would only give rise to capital gains or losses), trading stock and depreciating assets.

29. It has been suggested that the terminology of the definition is sufficiently straightforward in that it is designed to encompass only those assets that would traditionally be regarded as being held on revenue account, the realisation of which would give rise to an amount of net profit to be included as ordinary income (see further on this throughout the Determination).

30. We consider that the intention of the provision cannot be to cover only those assets on which there is a single net result (profit or loss) if it was considered necessary to exclude from the application of the provision trading stock, on which profits or losses do not arise as a result of a single netting off.

31. The express exclusion of depreciating assets from the definition of revenue assets also suggests that a broader view should be adopted, because depreciating assets are generally held on capital account.

32. Before the definition in section 977-50 is considered in more detail, it is worth noting that, in the consolidation context, the heading to section 705-40 refers to assets 'held on revenue account'. This is important because subsection 950-100(1) makes it clear that headings of sections form part of the ITAA 1997.

33. The term 'on revenue account' is not defined in the ITAA 1997 but has a commonly understood meaning in tax law, being that which gives rise to ordinary income, as distinguished from assets held on capital account. According to Parsons, *Income Taxation in Australia*¹³ a revenue asset refers to:

an asset whose realisation is inherent in, or incidental to, the carrying on of a business [as distinct from] a 'structural asset', which forms part of the 'profit yielding subject' of the business.

34. Although the ordinary meaning of the term 'on revenue account' would equate with Parsons' 'revenue asset', in fact the ambit of the definition in section 977-50 indicates that the meaning of the term 'on revenue account' used in the heading to section 705-40 must embrace a far broader range of assets than those traditionally regarded as being on revenue account.¹⁴

35. This conclusion appears inevitable given the use of the words 'in calculating your assessable income' used in paragraph 977-50(a). Although the concept of assessable income is addressed in more detail later in this Determination, it is clear that assessable income includes, not just ordinary income (that which arises where assets are realised as an incident of a business), but also statutory income, where amounts are included in assessable income irrespective of whether assets are held on what would traditionally be regarded as 'revenue account'.

¹³ Parsons, RW 1985, *Income Taxation in Australia*, The Law Book Company Limited, p.155. See also Taxation Ruling TR 96/4 on valuing shares acquired as revenue assets.

¹⁴ Given that section 705-40 applies to depreciating assets, this is, at least to some extent, self-evident.

36. The role of headings in statutory interpretation has been explained in a number of cases.¹⁵ The rules have been summarised as:¹⁶

- If the language of the section is clear and is actually inconsistent with the heading, the heading must give way.
- If the language of the section is clear, but, although more general, is not inconsistent with the heading, the section must be read subject to the heading.
- If the language of the section is doubtful or ambiguous, the meaning which is consistent with the heading must be adopted.

37. Given that a court is obligated to give effect to the words actually used in the law, and not dismiss as otiose words which appear to be inconvenient, we regard the specific use of the term 'assessable income' (embracing as it does statutory income) compels the conclusion that, to the extent that the heading to section 705-40 uses a term ('on revenue account') traditionally associated only with ordinary income, it is inconsistent with the clear language of the words of the definition in paragraph 977-50(a) and therefore must give way to those words.

38. Therefore, although there is a significant body of case law dealing with transactions 'on revenue account', we do not think that the heading to section 705-40 can provide a simple answer to what is a 'revenue asset' for the purposes of that section.

39. As to when a realisation would be taken into account in calculating a joining entity's assessable income or tax loss (otherwise than solely as a capital gain or capital loss), the key factors in the definition are:

- profit and loss;
- disposing, ceasing to own or otherwise realising;
- 'would be taken into account'; and
- calculating your assessable income or tax loss.

Profit and loss

40. The tax law does not define 'profit or loss'. The concept has a technical meaning in commerce and usually involves a netting of receipts and outlays, although certain gains or losses on realisation of an asset may be accounted for separately as revenue and expenses.

41. Consistent with the notion of netting receipts and outlays, it has been suggested that the concept of profit referred to in the definition reflects the commercial meaning of the word, and should be limited to (net) profits arising from business or commercial transactions or where some plan, method or process has been adopted to generate the amount. In this way, 'profit' would be a narrower concept than 'gain'. A similar interpretation would apply to losses. A profit or loss arising in these circumstances would be calculated by comparing the gross proceeds on realisation with the total outlays. The net result would constitute either ordinary income or allowable deductions.

¹⁵ See, for example, *Silk Bros Pty Ltd v. State Electricity Commission (Vic)* (1943) 67 CLR 1, *Saunders v. Borthistle* (1904) 1 CLR 379 and *Ragless v. District Council of Prospect* [1922] SASR 299.

¹⁶ Refer Murray, CJ in *Ragless v. District Council of Prospect* [1922] SASR 299.

42. There is no doubt that a profit or loss arising from the realisation of an asset in these circumstances is intended to fall within the meaning of revenue asset.
43. However, case law refers to the need to apply the 'natural and ordinary sense of the language'¹⁷ and there is nothing inherently within the words of the definition (or the context in which it is to be applied) that suggests the words 'profit or loss' should be restricted to their narrow commercial meaning.
44. In particular, section 70-5 on trading stock, in bringing gross outgoings and earnings to account for the disposal of trading stock, refers to such commercial profits as 'net profits'. The use of the word 'profit' in section 977-50 therefore suggests something broader than simply commercial or net profits.
45. The ordinary meaning of **profit** is defined as:
- Macquarie Dictionary:* 1. The pecuniary gain resulting from the employment of capital in any transaction ... b. net profit, amount remaining after deducting all costs from gross receipts,...2. returns, proceeds or revenue, as from property or investments.
- Shorter Oxford Dictionary:* 4. That which is derived from or produced by some source of revenue; proceeds, returns. 5. The pecuniary gain in any transaction, the excess of returns over the outlay of capital. ... Phrase **P. and loss**, an inclusive expression for the gain and loss made in a series of transactions, and the gain or loss made in one transaction...
46. 'Loss' is defined to mean:
- Macquarie Dictionary:* ...11. Commerce failure to recover the costs of a transaction or the like, in the form of benefits derived.
- Shorter Oxford Dictionary:* '5. Detriment or disadvantage resulting from deprivation or change of conditions; an instance of this. (opp. to gain)
47. In contrast, 'gain' is defined in the Macquarie Dictionary to mean:
1. to obtain; secure (something desired); acquire: *gain time*. 2. to win; get in competition: *gain the prize*. ... 4. to obtain as a profit: *he gained ten dollars by that transaction*. noun 8. profit; advantage. 9. (*plural*) profits; winnings. 10. an increase or advance. 11. the act of gaining; acquisition.
48. Given that the ITAA 1997 (in section 70-5) has specifically used the term 'net profits' to describe the commercial notion of profit, it could reasonably be concluded that the words 'profit or loss' are used in this context simply to describe any financial gain or loss on a transaction. This gain or loss might be revenue or capital in nature. It might also represent the difference between two amounts (a net amount) or extend to the case where a gross receipt itself represents a financial gain (or the gross outlay a financial loss).
49. Perhaps a stronger indication that profit or loss is intended to be read more broadly is the requirement that the profit or loss would be taken into account in tax calculations 'otherwise than as a capital gain or capital loss'. A revenue asset must be a CGT asset and it will therefore always be necessary to calculate a capital gain or loss on its realisation. The operation of the CGT anti-overlap rules in section 118-20 to any profit or loss made from the asset's realisation must therefore be implicit in the definition. The CGT anti-overlap rule applies to reduce a capital gain to the extent an amount is included in the taxpayer's assessable income. As assessable income includes both ordinary and statutory income¹⁸ the profit referred to in the definition of revenue asset should cover all profits that are included in ordinary income or statutory income.

¹⁷ See Mason and Wilson JJ in *Cooper Brookes* at pp 4305-6.

¹⁸ See further explanation at paragraphs 58 to 69 of this Determination.

Disposing, ceasing to own or otherwise realising

50. Section 977-50 requires that the profit or loss arise from a (hypothetical) disposal, cessation of ownership or other realisation. A summary of the meaning of the words 'dispose', 'cease' and 'realise' from the Shorter Oxford and Macquarie dictionaries is as follows:

- Dispose – to assign; to order, control, direct; to bestow; to make over or part with (property), as by gift or sale; transfer; to get rid of'.
- Cease – to stop, give over, discontinue, desist; to come to or be at an end.
- Realise – to be sold for (a specified sum); to convert (assets, etc) into cash or money.

51. The words 'disposing of, ceasing to own or otherwise realising' are hence broad enough to cover any way in which a revenue asset can be realised.

52. That a profit or loss on realisation 'would' be taken into account supports the view that the realisation referred to in the definition is purely hypothetical and actual realisation is not necessary. In fact, the question is looked at when there is no realisation (that is, when an entity joins a consolidated group).

53. The words do not suggest that any particular form of realisation, or type of profit or loss needs to be anticipated, simply that if the asset was realised in the taxpayer's operations, any profit or loss would be taken into account for the purposes of the taxpayer's income tax calculations, otherwise than solely as a capital gain or loss.

Would be taken into account

54. The ordinary meaning of the term 'taken into account' suggests a looser relationship between the profit or loss and assessable income, than a term such as 'forms part of' or 'is included in'.

55. The use of the term 'taken into account' varies throughout the ITAA 1997. While the term is used to represent direct inclusions in, or exclusions from, income or losses,¹⁹ it is also used to refer to matters that are covered by other provisions,²⁰ suggesting a less strict use of the term.

56. Specifically in Part 3-90, the term is used, for example, to refer to membership interests that would be taken into account in working out a reduction in a tax cost setting amount.²¹ In a similar approach to that referred to in the previous paragraph the term is also used in relation to assets that are 'not taken into account' when applying paragraph 705-35(1)(c).²²

¹⁹ For example, exempt income may be 'taken into account in working out the amount of a tax loss' – refer to the Note to subsection 6-15(2).

²⁰ See subsection 35-45(4) which excludes from the operation of section 35-45 'assets ... that are taken into account ... under section 35-40'.

²¹ See the Note to section 705-240.

²² See the table to paragraph 705-59(3)(b).

57. The requirement in section 977-50 that the profit or loss would be 'taken into account, in calculating your assessable income ... otherwise than as a capital gain or capital loss' also suggests this looser relationship between the profit or loss and the assessable income. In the case of a capital loss, it could never be (directly) taken into account in calculating a taxpayer's assessable income. At most, a capital loss is only taken into account in working out the taxpayer's net capital gain, which is then included in the taxpayer's assessable income. A profit or loss that would be taken into account would also include a profit or loss taken into account in part, or where the profit or loss would be calculated under some different methodology other than a simple (net) profit calculation.

Calculating your assessable income or tax loss

Assessable income

58. Under sections 6-5 and 6-10 'assessable income' includes ordinary income and statutory income, that is, every sort of profit, gain or receipt that will be assessed under the ITAA 1997.

Ordinary income

59. Assessable income includes gross income as well as net profits derived as ordinary income. In *Commercial & General Acceptance Ltd v. FC of T*,²³ Mason J said:

No doubt in the context of the Act (gross) income is to be ascertained in the first instance by reference to the gross income receipts of the taxpayer, but in my view it also includes a net amount which is income according to ordinary concepts and usages of mankind, when the net amount alone has that character, not being derived from gross receipts that are revenue receipts.

60. This meaning of ordinary income is consistent with the broader view taken of the meaning of the word 'profit' as it appears in the earlier part of the definition, each applying, where appropriate, to both gross and net receipts.

61. It is beyond the scope of this Taxation Determination to address the range of realisations that could give rise to ordinary income. However, it is worth noting that in *FC of T v. Myer Emporium Ltd*²⁴ (*Myer Emporium*) it was made clear that:

- profits from transactions made in the ordinary course of a taxpayer's business would be income;
- profits made in the course of the taxpayer's business where there was an intention to make a profit would also be income; and
- profits made outside the ordinary course of the taxpayer's business would still be income where there was an intention to make a profit and the transaction was entered into and the profit made in carrying out a business operation or commercial transaction.

²³ (1977) 137 CLR 373 at 382-3; 77 ATC 4375 at 4380; (1977) 7 ATR 716 at 722.

²⁴ (1987) 163 CLR 199; 87 ATC 4363; (1987) 18 ATR 693. See also Taxation Ruling TR 92/3 on whether profits on isolated transactions are income.

62. Assets otherwise traditionally regarded as not being held on revenue account, could be ventured into a business or profit-making venture (for example, *White v. FC of T*²⁵ and *FC of T v. Whitfords Beach Pty Ltd*²⁶) and thus become 'revenue assets'. In discussing the difference between a 'mere realisation' and the implementation of a profit-making intention, the court in *Myer Emporium* said that:²⁷

Then, if the asset be not a revenue asset *on other grounds*, the profit made is capital because it proceeds from a mere realisation.' [Emphasis added]

This strongly suggests that assets which, subsequent to acquisition, are ventured into a profit-making undertaking, will become 'revenue assets', even if they were not acquired as such.

63. Hence for a joining entity, assets that would be:

- realised in the course of its business;
- realised in association with the carrying on of its business; or
- capital assets that would be realised in circumstances other than a 'mere realisation',

would be assets which, if realised at a profit, would be taken into account in calculating the entity's assessable income.²⁸

Statutory income

64. The fact that the definition of revenue asset refers to assessable income (rather than just ordinary income) requires a consideration of statutory income.

65. Statutory income is assessable income that is not ordinary income (section 6-10). A summary of provisions dealing with statutory income is provided at section 10-5.

66. Amounts included in statutory income may also be included in ordinary income. Subsection 6-25(2) says that:

Unless the contrary intention appears, the provisions of this Act (outside this Part) prevail over the rules about ordinary income.

One provision that evidences such contrary intention is the CGT anti-overlap rule in section 118-20. As the capital gain is reduced to the extent an amount is included in assessable income, it is considered that the effect of this anti-overlap rule is that the assessability under ordinary income provisions 'prevails' over capital gains.

67. The introduction to section 10-5 says that the provisions set out in the table include both amounts that are not ordinary income, and 'vary or replace rules that would otherwise apply for certain kinds of ordinary income.' It is clear from the note to subsection 6-10(2) that the provisions in the summary in section 10-5 about 'ordinary income ... do not change its character as ordinary income'.

68. Section 10-5 refers to a large number of provisions, including those on capital allowances, capital gains and foreign exchange gains.

²⁵ (1968) 120 CLR 191; (1968) 15 ATD 173.

²⁶ (1982) 150 CLR 355; 82 ATC 4031; (1982) 12 ATR 692.

²⁷ At (1987) 163 CLR 199 at 213.

²⁸ Ignoring the effect of the single entity rule, in accordance with subsection 701-10(2).

69. It is therefore apparent that a significant number of transactions relating to assets can have recognition in assessable income while not in any way giving rise to ordinary income.

Tax loss

70. Tax loss is defined in section 995-1 to include a tax loss worked out under sections 36-10, 165-70, 175-35 or 701-30.

71. For the purposes of working out the meaning of the term revenue asset, the most relevant provision is section 36-10 which deals with current year losses (that is, the excess of deductions over assessable income and net exempt income).

72. The reference to assessable income or tax loss in section 977-50 does not specifically address deductions. Deductions can arise on a realisation of an asset, either where the taxpayer sustains a net loss on realisation, or incurs a gross outlay as a deduction.

73. Where a taxpayer incurs these deductions, but is not in an overall loss situation, the taxpayer has not sustained a tax loss, as defined. Similarly, while the deductions are allowable against assessable income (in the calculation of taxable income – section 4-15), they will not generally be taken into account in calculating a taxpayer's assessable income.

74. Does this mean that losses or outgoings on the hypothesised realisation of assets that only give rise to deductions against assessable income (rather than tax losses) cannot be relevant in considering the meaning of the term revenue asset? For a range of reasons, we do not agree that any omission of a specific reference to deductions leads to that conclusion.

75. Deductions are an inherent component in the calculation of tax losses (for example, for section 36-10 current year losses, the loss arises from an excess of deductions over assessable and net exempt income). Even if there is no tax loss (because the taxpayer's position is, overall, profitable), the role of deductions in potentially bringing about a tax loss cannot be overlooked.

76. However, it must be remembered that the definition in section 977-50 deals with a hypothesised realisation (or range of possible realisations). Such realisations can be assumed to be, on balance, as likely as not to give rise to an amount of assessable income, rather than allowable deductions or a tax loss.

77. Making predictions about whether a joining entity is likely to be in an overall profitable situation (so that a loss on a hypothetical realisation of an asset would give rise to a deduction against assessable income, rather than a tax loss, as defined) is irrelevant in considering whether an asset of the joining entity is a revenue asset in accordance with the definition in section 977-50, as that term is to be applied in section 705-40.

78. As the legislature was concerned only with the characterisation of particular assets, it must be assumed that the law was enacted based on assumptions or predictions about those assets, in isolation from the joining entity's other income or deductions. That is, the general likelihood of whether the joining entity would be in an overall profit or loss situation, is not to the point in considering the characterisation of a particular asset held.

79. To construe the definition of 'revenue asset' as not applying to CGT assets where a net loss (claimed as a general deduction) might arise on realisation, would be to make a nonsense of the definition, and it is to be expected that the courts will generally support a construction of the law that is available from the words of the provision, which makes sense, over the alternative.²⁹

Conclusion

80. For any CGT asset of a joining entity (other than trading stock or a depreciating asset), where a profit or loss on realisation, if the asset were to be realised, would be reflected in their income tax calculations, otherwise than solely as a capital gain or loss, then that asset is the sort of asset that should be expected to meet the definition of revenue asset.

²⁹ Per Gibbs CJ in *Cooper Brooks*: at 81 ATC 4292 at 4296 '... if two constructions are open, the court will obviously prefer that which will avoid what it considers to be inconvenience or injustice'.

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- capital gains
- capital losses
- CGT assets
- CGT events L1-L8 consolidated and MEC groups
- consolidation assets
- consolidation formation
- consolidation joining
- consolidation market value
- depreciating assets
- disposal of assets
- general value shifting regime
- head company
- income
- income vs capital
- joining entity
- losses
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