PCG 2022/1 - Non-commercial business losses - Commissioner's discretion regarding flood, bushfire or COVID-19

Practical Compliance Guideline

Non-commercial business losses – Commissioner’s discretion regarding flood, bushfire or COVID-19

Relying on this Guideline

This Practical Compliance Guideline sets out a practical administration approach to assist taxpayers in complying with relevant tax laws. Provided you follow this Guideline in good faith, the Commissioner will administer the law in accordance with this approach.

[Note: This is a consolidated version of this document. Refer to the Legal database (ato.gov.au/law) to check its currency and to view the details of all changes.]

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What this Guideline is about

1. Division 35 of the *Income Tax Assessment Act 1997* prevents an individual’s losses[1] from non-commercial business activities being offset against the individual’s other assessable income in the year the loss is incurred.[2]

2. All legislative references in this Guideline are to the *Income Tax Assessment Act 1997*.

[1] ‘Losses’ means the amount by which the allowable deductions attributable to a business activity exceed the assessable income from that activity (section 35-10).

[2] The individual’s losses can be incurred either alone or in partnership (section 35-10). The operation of Division 35 is modified for those losses incurred in partnership (section 35-25).

3. Division 35 operates in relation to the business activities carried on by a business, rather than the business itself. A business may be made up of more than one business activity.

4. Broadly, a loss from each business activity that an individual (alone or in partnership) carries on in a year is deferred to be offset against future income from the same business activity, unless:

- the individual meets the income requirement[3] and the business activity satisfies one of the 4 stipulated tests[4]
- the individual has a business activity that is eligible for an exception[5], or
- the Commissioner exercises the discretion in subsection 35-55 for the business activity for one or more income years.[6]

5. The discretion can be exercised in relation to a business activity for one or more income years if the Commissioner is satisfied that it would be unreasonable, by reference to the circumstances specified, to defer the losses.

6. One of the circumstances in which the discretion may be exercised is where the business activity was or will be affected by special circumstances outside the control of the operators of the business activity, including drought, flood, bushfire or some other natural disaster.[7]

7. This discretion is for situations where the business activity was or will be affected by special circumstances that caused it to fail to satisfy one of the 4 tests or make a profit in the relevant year.[8]

8. Special circumstances outside of the control of the operator of the business activity are those which are sufficiently different to distinguish them from the circumstances that occur in the normal course of conducting a business activity. Ordinary economic, weather or market fluctuations (which are expected to occur on a regular or recurrent basis and could reasonably be predicted to affect the business activity) will not normally be considered special circumstances.[9]

9. Ordinarily, special circumstances are those which have materially affected the business activity, causing it to not satisfy any of the 4 tests.[10] In addition to drought, flood and bushfire, examples of special circumstances (depending on the facts) may include government restrictions, explosions and disturbances to energy supplies.

10. In recent years, special circumstances such as flood, bushfire and COVID-19 impacts may have caused the non-commercial loss rules to apply to a taxpayer's business.

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[3] The income requirement (subsection 35-10(2E)) is met when, in a given income year, the sum of the individual's taxable income (disregarding any assessable first home super saver released amounts), reportable fringe benefits, reportable superannuation contributions and total net investment losses is less than $250,000.

[4] The assessable income test (section 35-30), the profits test (section 35-35), the real property test (section 35-40) or the other assets test (section 35-45).

[5] Concerning certain performing arts and primary production businesses (see subsection 35-10(4)).

[6] If a loss is not deferred, the individual cannot apply the loss carry back tax offset as this is not available to individuals (see paragraph 160-5(b) and section 160-25).

[7] As outlined in paragraph 35-55(1)(a).

[8] In the context of the Note to paragraph 35-55(1)(a) and consistent with the aim of the discretion, it is the Commissioner's view that the provision will apply in situations where the business activity would have satisfied one of the 4 tests if the special circumstances had not occurred (see paragraphs 59 to 66B and 105 to 108 of Taxation Ruling TR 2007/6 *Income tax: non-commercial business losses: Commissioner's discretion*).

[9] As outlined in paragraph 13 of TR 2007/6.

[10] Paragraph 13 of TR 2007/6. Note, for those individuals who do not satisfy the income requirement, the special circumstances must have caused the business to not make a tax profit in the relevant years (see paragraph 13A of TR 2007/6).

If this happens and a taxpayer does not meet one of the other requirements for the loss to be offset against their other income, the taxpayer will need to seek the Commissioner's discretion to allow them to do so.

11. This Guideline outlines a safe harbour that, provided you satisfy the relevant conditions, allows you to manage your tax affairs as if the Commissioner had exercised the discretion in paragraph 35-55(1)(a). It does not, however, apply to amounts deferred in previous income tax years under the non-commercial loss rules. This Guideline also does not prevent you from applying for an exercise of the discretion in the usual way if your circumstances do not fall within the terms of the safe harbour.

12. This Guideline does not apply to the Commissioner's discretions in:

- paragraphs 35-55(1)(b) or (c) – the 'lead-time' limbs, or
- subsection 35-55(2) – the 'blackhole expenditure' limb.

Date of effect

13. This Guideline applies to the 2019–20, 2020–21, 2021–22, 2022–23, 2023–24 and 2024–25 income years.[11]

Safe harbour – compliance approach

14. If your circumstances satisfy the conditions listed in paragraph 16 of this Guideline, you can manage your tax affairs as if we had exercised the discretion. There is no need to apply for the discretion to be exercised.

15. If you choose to use this safe harbour and are subsequently selected for an ATO compliance check, we may seek to confirm that you satisfy the relevant safe harbour conditions.

Safe harbour – conditions

16. You qualify for the safe harbour if you satisfy all of criteria (a) to (f) listed in this paragraph in an income year and you made a tax profit from your business activity in the immediately preceding income year[12]:

(a) you satisfy the income requirement in subsection 35-10(2E)

(b) you made a loss from your business activity, excluding any amounts deferred from a previous income year under paragraph 35-10(2)(b)[13]

(c) your business activity was affected by one or more of the following events

  (i) flood (including where you received ATO flood support)

  (ii) bushfire (including where you qualified for an ATO bushfire lodgment and payment deferral), or

  (iii) a government-imposed lockdown, business closure or restriction due to COVID-19

[11] There are time limits on amending assessments for previous income years. Beyond these times, you will need to lodge an objection (see Time limits on tax return amendments).

[12] 'Tax profit' refers to the business activity producing assessable income for an income year that is greater than the deductions attributable to it for that year (apart from the operation of subsections 35-10(2) and (2C) – see paragraph 16 of TR 2007/6).

[13] See Example 6 of this Guideline.

(d) the event meant that

  (i) you were not able to carry on your business activity or unable to carry it on to the same scale as you usually carry on your business activity, or

  (ii) some or all of your customers were not able to access your business activity or access it in the same way as they usually did

(e) you have not applied for a private ruling requesting the Commissioner exercise the 'special circumstances' discretion in relation to your business activity in the relevant income year

(f) you have evidence to support that you are eligible for the safe harbour.

Examples

17. The following examples illustrate how the safe harbour can apply in various situations.

Example 1 – bushfire – eligible to use the safe harbour

18. *Ismoth operates an established beekeeping business. At the commencement of the 2019–20 income year, the business maintained 100 hives that provided pollination services to agricultural enterprises and produced honey for sale. The business had generated small tax profits in recent years, including in the 2018–19 income year.*

19. *In December 2019, the business activity was impacted by bushfire resulting in a loss of approximately half the hives. In previous years, the average loss of hives was approximately 5% per year.*

20. *Ismoth's other income remained stable and she met the income requirement in the 2019–20 income year.*

21. *Ismoth's beekeeping business returned a loss in the 2019–20 income year.*

22. *Ismoth maintains evidence of the loss of hives to demonstrate the impact of the bushfire on her business activity.*

23. *In this case, Ismoth is eligible to use the safe harbour.*

Example 2 – flood – not eligible to use the safe harbour

24. *Steve runs a coffee roasting business from the garage of his home. He has not made a profit in recent years, including in the 2019–20 income year. Steve meets the income requirement in the 2020–21 income year.*

25. *In the 2020–21 income year, the town where Steve lives was inundated with flood water and Steve closed his business for 3 months to undertake repairs to his garage, where the business activity was conducted.*

26. *Even though the flood would be a special circumstance, which impacted Steve's business activity, Steve did not make a tax profit in the income year before the event. In this case, Steve is not eligible to apply the safe harbour. However, Steve can apply for the exercise of the discretion in the usual way.*

Example 3 – COVID-19 – eligible to use the safe harbour for current year's loss only

27. *Mary operates a food truck and meets the income requirement in the 2019–20 income year.*

28. *The business activity made a loss of $15,000 in the 2017–18 income year. Mary was not eligible to use the losses and they were deferred. The business generated a tax profit of $10,000 in the 2018–19 income year. Mary offset $10,000 of her carried forward losses against that income; however, the remaining $5,000 was deferred and carried forward.*

29. *A government-imposed lockdown in response to COVID-19 meant that Mary could not operate her business from March to June 2020. In the 2019–20 income year, the business made a loss of $7,000. Mary maintains evidence of the lockdown's impact on her business.*

30. *In this case, Mary is eligible to use the safe harbour to offset the $7,000 loss from the 2019–20 income year against her other income but cannot use the safe harbour to offset the $5,000 loss previously deferred.*

Example 4 – COVID-19 – income requirement – not eligible to use the safe harbour

31. *Virat operates a successful boutique clothing design and manufacture business, which supplies several independent retail stores across Australia. In recent income years, the business has made tax profits.*

32. *During a number of months in the 2020–21 income year, a series of government-imposed COVID-19 restrictions limited Virat's ability to manufacture and supply clothes to his customers. Virat's business activity made a loss in that year.*

33. *Virat's other taxable income and net investment losses were greater than the income requirement of $250,000.*

34. *In this case, while Virat's business activity was affected by special circumstances outside his control and the business made a loss, he is not eligible to apply the safe harbour because he did not meet the income requirement. However, Virat can apply for the exercise of the discretion in the usual way.*

Example 5 – COVID-19 – able to carry on the business activity – not eligible to use the safe harbour

35. *Bert conducts a share trading business activity, which has made a tax profit in the last income year. The share trading business activity is for his own benefit.*

36. *In the 2020–21 income year, the values of Bert's holdings fluctuated and he made a loss from his share trading activity. The area where Bert lived was subject to extended periods in government-imposed lockdown due to COVID-19 but this did not prevent Bert from conducting his share trading business activity as normal. Bert meets the income requirement in the 2020–21 income year.*

37. *Bert was able to continue his share trading business activity as normal despite COVID-19 and therefore is not eligible to apply the safe harbour.*

Example 6 – calculating if a business activity has made a loss – not eligible to use the safe harbour

38. *Jana carries on a 3D-printing business activity from home. In the 2019–20 income year, she made a loss of $20,000, which was deferred under the non-commercial loss rules.*

39. *In the 2020–21 income year, Jana's business activity made a profit of $5,000. Jana used part of the loss from the 2019–20 income year to offset this profit. Jana does not satisfy Division 35 to offset the remaining $15,000 against her other income and that amount continues to be deferred.*

40. *In the 2021–22 income year, Jana's home was inundated by flood water causing her to cease her business activity for 3 months and therefore the profit from her business activity reduced to $3,500. Jana can offset $3,500 of her deferred losses against this profit.*

41. *However, Jana does not qualify to use the safe harbour in the 2021–22 income year because she cannot include the remaining $11,500 in calculating whether her business activity made a loss in that year.*

42. *Jana did not make a loss in the 2021–22 income year and therefore is not eligible to apply the safe harbour to offset the remaining $11,500 of losses against her other income in that year.*

Commissioner of Taxation
14 September 2022

Amendment history

16 July 2025

Part	Comment
Paragraph 13	Updated to include 2024–25 income year.

8 November 2023

Part	Comment
Paragraph 13	Updated to include 2023–24 income year.

References

Previous draft:

PCG 2022/D2

Related rulings and determinations:

TR 2007/6

Legislative references:

- ITAA 1997 Div 35
- ITAA 1997 35-10
- ITAA 1997 35-10(2)
- ITAA 1997 35-10(2)(b)
- ITAA 1997 35-10(4)
- ITAA 1997 35-10(2C)
- ITAA 1997 35-10(2E)
- ITAA 1997 35-25
- ITAA 1997 35-30
- ITAA 1997 35-35
- ITAA 1997 35-40
- ITAA 1997 35-45
- ITAA 1997 35-55
- ITAA 1997 35-55(1)(a)
- ITAA 1997 35-55(1)(b)
- ITAA 1997 35-55(1)(c)
- ITAA 1997 35-55(2)
- ITAA 1997 160-5(b)
- ITAA 1997 160-25

Other references:

Time limits on tax return amendments

ATO references

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