IT 88 - Income Tax: Trading Stock - Commonwealth securities held by authorised dealers in the short term money market.

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TAXATION RULING NO. IT 88

TRADING STOCK - COMMONWEALTH SECURITIES HELD BY AUTHORISED DEALERS IN THE SHORT TERM MONEY MARKET

F.O.I. EMBARGO: May be released

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REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:
I 1101293	TRADING STOCK	6
	COMMONWEALTH SECURITIES	31(1)
	SHORT TERM MONEY MARKET	

PREAMBLE It was directed in paragraph 13 of CITCM No. 811 that securities held by dealers in the short term money market should not be treated as trading stock. The question has now been raised whether this approach can still be maintained having regard to the judgments given in the case of Investment & Merchant Finance Corporation v FC of T (1971) 125 CLR 249.

2. Although the view was expressed in the Modern Permanent Building Society case (1958) CLR 187 that trading stock does not include choses in action, it was indicated in the CITCM that this general statement did not automatically prevent shares and debentures in companies from being treated as trading stock in appropriate circumstances. It was nevertheless considered at the time that the nature of other kinds of choses in action prevented their acceptance as trading stock.

3. In his judgment in the IMF case, Walsh J., did not regard the Modern Permanent Building Society decision as establishing any general proposition to the effect that trading stock cannot include choses in action. The test applied in the I.M.F. case was whether shares purchased and sold satisfied the definition of "trading stock" in section 6. If the same reasoning is applied to bonds held by authorised dealers in the short term money market, it is necessary to determine whether bonds are capable of being treated as trading stock having regard to the manner in which the taxpayer's business is conducted.

FACTS 4. An authorised dealer in the short term money market is required to operate under a formal agreement with the Reserve Bank. The dealer's only business is the borrowing of money and investing and trading in certain government bonds and commercial bills. All funds accepted by a dealer are to be invested in money market securities maturing within three years, commercial bills which have been endorsed by a bank and such other securities as the Reserve Bank may from time to time approve. the dealer must be ready and able to engage actively in buying and selling money market securities.

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5. Although a dealer receives interest falling due on bonds held, the income from this source is absorbed by interest paid on borrowings from clients and trading in bonds is an integral and essential part of the business carried on. In the circumstances, it has been decided to accept that securities held by an official dealer in the short term money market constitute trading stock. This decision is consistent with one given by a former Second Commissioner in 1966 when it was held that bonds acquired by an unofficial dealer in the short term money market fell within the definition of trading stock.

6. Bonds and other securities held by banks and insurance companies should continue to be treated as indicated in paragraph 14 of CITCM No. 811.

COMMISSIONER OF TAXATION