




# ***PS LA 2006/1 (GA) - Calculating the cost base of a CGT asset where there is insufficient information to determine any capital works deduction under Division 43 of the ITAA 1997***

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## Calculating the cost base of a CGT asset where there is insufficient information to determine any capital works deduction under Division 43 of the ITAA 1997

This Practice Statement outlines when a taxpayer is not required to reduce an asset's cost base and reduced cost base for Division 43 capital works expenditure.

*This Practice Statement is an internal ATO document and an instruction to ATO staff.*

*Taxpayers can rely on this Practice Statement to provide them with protection from interest and penalties in the following way. If a statement turns out to be incorrect and taxpayers underpay their tax as a result, they will not have to pay a penalty, nor will they have to pay interest on the underpayment provided they reasonably relied on this Practice Statement in good faith. However, even if they do not have to pay a penalty or interest, taxpayers will have to pay the correct amount of tax provided the time limits under the law allow it.*

### 1. What is this Practice Statement about

Division 43 of the *Income Tax Assessment Act 1997* (ITAA 1997) allows a taxpayer to deduct construction expenditure (incurred by the taxpayer or a previous owner) in respect of certain income-producing buildings and structural improvements (capital works).

All legislative references in this Practice Statement are to the ITAA 1997, unless otherwise indicated.

The construction expenditure is written off over 25 or 40 years, depending on when it was incurred and the use of the capital works.

Where a taxpayer has deducted or can deduct expenditure in an income year under Division 43, it does not form part of the cost base or reduced cost base of a capital gains tax (CGT) asset (subsections 110-45(2) and 110-50(2)).

This Practice Statement outlines the circumstances where we will accept that a taxpayer cannot deduct an amount under Division 43 for a CGT asset and is therefore not required to reduce the asset's cost base or reduced cost base.

### 2. When will the ATO accept that a deduction cannot be made

We will accept that a taxpayer cannot deduct an amount under Division 43, and so is not required to reduce their cost base and reduced cost base, where the taxpayer:

- does not (as a question of fact) have sufficient information to determine the amount and nature of the construction expenditure for an asset, and
- does not seek to deduct any amount in relation to the construction expenditure under Division 43 (or any other provision).

**Note:** This only has relevance to CGT assets acquired after 7:30 pm (AEST) on 13 May 1997, although it may apply to expenditure on land or a building acquired

before that time, provided the expenditure is incurred after 30 June 1999 and forms part of the fourth element of the cost base of the asset (subsections 110-45(1A) and 110-50(1A)).

### 3. When would a taxpayer not have sufficient information

There are some circumstances where a taxpayer may not have sufficient information to deduct amounts under Division 43.

#### *Where the previous owner does not supply details of the construction expenditure*

Subsection 262A(4AJA) of the *Income Tax Assessment Act 1936* (ITAA 1936) requires the previous owner of capital works to provide the new owner with a notice containing the information necessary for the new owner to work out how Division 43 applies to them. However, this information may not be available in some circumstances and the taxpayer therefore may not have sufficient information to deduct amounts under Division 43.

#### *Where the previous owner was not entitled to a deduction under Division 43 but the new owner will be*

The notice requirement in subsection 262A(4AJA) of the ITAA 1936 only applies if the previous owner has deducted an amount under Division 43. However, there are some circumstances when the new owner will be entitled to a deduction under Division 43 even though the previous owner was not – for example, if the capital works were acquired from a speculative builder or a previous owner who used the capital works as a private residence. The new owner therefore may not have the information necessary to work out how Division 43 applies to them.

### **Where a taxpayer has difficulty in calculating what they have spent**

Even where the construction expenditure was incurred by the taxpayer themselves, they still may have difficulty in ascertaining the exact amount that qualifies for deduction under Division 43.

*Taxation Ruling TR 97/25 Income tax: property development: deduction for capital expenditure on construction of income producing capital works, including buildings and structural improvements* recognises that where there is difficulty in determining construction expenditure, a building cost estimate provided by an appropriately qualified person can be used.

However, the cost of obtaining such an estimate can impose a significant burden on taxpayers, which is why we allow the exception outlined in section 2 of this Practice Statement. It is consistent with the broad policy underpinning the CGT cost base reduction rules, being that an amount should either be allowed as a deduction or included in the asset's cost base or reduced cost base, but not both.

## **4. Examples**

### **Example 1**

*Angie purchased a rental property on 1 August 2001. Marty, the previous owner, incurred construction expenditure on the property in the 1997–98 income year. Marty deducted amounts under Division 43 in relation to this expenditure. When Angie purchased the property, she became entitled to claim deductions under Division 43 for the capital works undertaken by Marty.*

*At the time Angie purchased the property, Marty did not provide her with the information she would need to calculate her deductions under Division 43. Marty said he could not find the information Angie needed and moved overseas a few months after selling the property to Angie. Angie tried without success to contact Marty.*

*As Angie did not have the information she needed to deduct an amount under Division 43, she did not claim deductions. On 1 May 2004, Angie sold the property to Daniel and made a capital gain.*

**ATO's position:** *We will accept that Angie cannot deduct an amount under Division 43. She will not have to adjust the cost base of her rental property.*

### **Example 2**

*Courtney purchased a property from Anthony in August 2002 and occupied it as his main residence.*

*Anthony had previously undertaken capital works on the property and deducted amounts for the construction expenditure under Division 43. However, he did not provide Courtney with information that would enable him to work out how Division 43 might apply to him.*

*In February 2005, Courtney moved interstate and decided to rent out the dwelling. When he came to prepare his tax return for the 2004–05 income year, Courtney's tax agent told him that he was entitled to deduct amounts under Division 43 for the construction expenditure Anthony incurred.*

*Courtney did not contact Anthony to get information on the construction expenditure and did not engage a quantity surveyor to provide him with an estimate of the building costs. He did not deduct the amounts under Division 43 to which he was entitled.*

**ATO's position:** *We will accept that Courtney cannot deduct an amount under Division 43 and so will not require him to adjust the cost base of the property.*

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## Amendment history

### 11 April 2024

Part	Comment
All	Updated to apply current ATO style and accessibility guides.
Section 3	Updated to improve grammar and layout.
Throughout	Minor changes in wording.

### 15 October 2015

Part	Comment
All	Updated to new LAPS format and style.

### 17 April 2014

Part	Comment
Contact details	Updated.

### 9 October 2012

Part	Comment
Contact details	Updated.

### 24 February 2012

Part	Comment
Generally	Updated to current publication style.
Paragraph 1	Inserted footnote 1.
Paragraph 13	Added title for TR 97/25.

### 6 August 2008

Part	Comment
Paragraphs 10 and 12	Minor changes in wording.
Contact details	Business line to Law & Practice.

## References

<b>Legislative references</b>	ITAA 1936 262A(4AJA) ITAA 1997 Div 43 ITAA 1997 110-45(1A) ITAA 1997 110-45(2) ITAA 1997 110-50(1A) ITAA 1997 110-50(2)
<b>File references</b>	06/2449
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