TD 93/127 - Income tax: trading stock of gold miners: what is the application of subsection 31(2) of the Income Tax Assessment Act 1936 to the low grade ore stocks where the notional market selling value is below cost?

This ruling contains references to repealed provisions, some of which may have been rewritten. The ruling still has effect. Paragraph 32 in TR 2006/10 provides further guidance on the status and binding effect of public rulings where the law has been repealed or repealed and rewritten. The legislative references at the end of the ruling indicate the repealed provisions and, where applicable, the rewritten provisions.

This document has changed over time. This is a consolidated version of the ruling which was published on *29 November 2006*

Taxation Determination

Income tax: trading stock of gold miners: what is the application of subsection 31(2) of the *Income Tax Assessment Act 1936* to the low grade ore stocks where the notional market selling value is below cost?

1. Some gold producers have on hand at balance date stocks of gold bearing ore, with gold content below the cut off grade for processing, which have been stockpiled for processing at a later date if the price of gold rises and/or costs fall .

2. Subsection 31(1) gives the taxpayer the option to value trading stock at cost, replacement price, or market selling value. As indicated by Taxation Ruling TR 93/3, a notional market selling value of gold ore may be calculated where no actual market sales are readily comparable. This may be applied to low grade ore even though it is rarely sold on the market. The notional market selling value may be calculated by taking the spot price of gold, less a reasonable estimate of future costs of the hypothetical purchaser, less a reasonable profit margin of the hypothetical purchaser (not the hypothetical vendor). A reasonable estimate of the cost to the taxpayer of producing refined gold from the low grade ore may be an acceptable estimate of a hypothetical purchaser's costs.

3. Subsection 31(2) gives the Commissioner a discretion to determine a fair and reasonable value of trading stock, that by reason of obsolescence , or any other special circumstances relating to the trading stock, is less than the lowest value that could be applied under subsection 31(1). It is intended to apply particularly where taxpayers would be disadvantaged in valuing stock under the existing bases provided in subsection 31(1), for example in the case of articles of trading stock such as discontinued lines, obsolete items and spare parts for which there may only be a sporadic market.

4. The lowest value that could be applied under subsection 31(1) for low grade gold ore may be the notional market value. Fluctuations in gold prices cause the notional market selling values of low grade ore to vary. These values may fall below cost, and may even be zero in some cases, although no lower value than zero can be given. These price fluctuations are a normal occurrence with all metals, and do not alone constitute special circumstances for the purpose of subsection 31(2). Instead, they are taken into account by the use of a notional market selling value under subsection 31(1), where it is capable of reasonable estimation.

Example

Low grade ore is mined at a grade of .9 gm/tonne, when the cut off that year was 1.1 gm/tonne higher grade primary ore. Costs and profit margin are assumed to be fixed for this example.

Costs incurred in mining and stockpiling $190/oz gold
Spot price of gold = $500/oz
Further costs estimated at $250/oz gold
Purchaser's profit margin is $75/oz

a) Market selling value = 500 - 250 - 75 = $175
MSV has fallen below cost

If spot price of gold falls to $325 or below
b) MSV = 0

5. The very nature of a notional market selling value of low grade ore stocks would normally make a subsection 31(2) election unnecessary as the value is derived from quantifiable data (costs, spot price, profit margin, and ounces of gold/tonne), rather than being determined by actual market forces. The isolation of gold mines and their different cost structures are taken into account by these values which are not uniform across the industry.

6. In exceptional circumstances there may be special criteria, other than price fluctuations alone, where taxpayers could be disadvantaged by the application of subsection 31(1), and the Commissioner may exercise his discretion under subsection 31(2) to produce a lower or nil value. These special criteria may include :

. Continual stockpiling of large quantities of low grade ore
. Minimal amounts previously processed
. Processing costs are unlikely to fall substantially
. Stocks are being used for rehabilitation

This list is not meant to be exhaustive and each case must be decided on its merits.

Commissioner of Taxation
1/7/93

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