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AUSTRALIAN TAX ADVISER

2408 : APRIL 2024

The IFX Legal Tax Team

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SECTION 1 – PROFESSIONAL DEVELOPMENTS

CAPITAL/REVENUE DISTINCTION

Following the decision in *Bowerman v FC of T* discussed in a recent *Australian Tax Adviser*, the ATO has released a Decision Impact Statement ('DIS') outlining the Commissioner's view on the capital/revenue distinction as it affects both receipts and outgoings from property transactions. In order to better understand the logic of the DIS, some discussion of the rules surrounding the capital/revenue distinction would be appropriate. And I apologise to those readers for whom this is 'old hat'.

¶8.1 Taxability of receipts

Receipts will be *ordinary income* if they are 'income according to ordinary concepts' (in other words, it would be what a person on the 'Clapham omnibus'[1] would consider to be income). Unsurprisingly, given the vagueness of this provision, much of Australia's tax jurisprudence surrounding this topic is devoted to the interpretation of this concept.

Section 6-10(1) and (2) specifically includes *statutory income* in your assessable income. The term 'statutory income' refers to receipts that are not *ordinary income* but are included in a taxpayer's assessable income by virtue of a statutory provision – capital gains are a good example of receipts that are not assessable as ordinary income but are nonetheless assessable under the capital gains tax provisions in Chapter 3 of the ITAA97.

¶8.2 Deductibility of outgoings

A loss or outgoing will be deductible if it meets one or both of the conditions outlined in s 8-1(1)(a) or (b) and is not disqualified by any of the conditions outlined in s 8-1(2).[2] Significantly losses or outgoings of a capital nature are prohibited under s 8-1(2)(a), so only losses or outgoings of a revenue nature can be deducted. This is one of the core issues addressed by the statement.

¶8.3 Taxation of capital gains

Since gains from capital transactions are not 'income according to ordinary concepts', they are not taxable under s 6-5. So, to tax such receipts, legislators had to introduce specific measures to do it (which it did in 1985). As pointed out above, these measures are to be found in Chapter 3 of ITAA97. A taxable capital gain arises

1 The phrase 'Clapham omnibus' was reportedly first put to legal use in a judgment by Sir Richard Henn Collins MR in the English Court of Appeal libel case *McQuire v. Western Morning News* (1903) to denote an ordinary person.

2 Non-deductible items include:

(a) A loss of capital or of a capital nature;

(b) A loss of a private or domestic nature;

(c) A loss that relates to gaining exempt income;

(d) A loss that is made non-deductible by a provision in the Act.