INCOME TAXATION LAW

READING SUMMARIES: SAMPLE

VII GENERAL DEDUCTIONS

A Introduction

Taxpayers may be permitted to deduct form their assessable income losses and outgoings. This may be pursuant to the general deductions provisions,\(^1\) which focus on the income nature of the loss, or pursuant to the specific general deductions provisions,\(^2\) which specifically provide for the deduction of particular losses (see Week 8). However, losses and outgoings which satisfy these provisions are only deductible if they are not subject to any exclusions (see Week 9).

B General Deductions

A taxpayer may deduct from their assessable income any loss or outgoing which is incurred through either gaining assessable income or carrying on a business.\(^3\) However, it must not be capital, private and domestic nature, incurred in gaining exempt income or non-assessable non-exempt income or non-deductable under a provision of the Act.\(^4\) This may require apportionment of the loss, as it may be incurred for multiple purposes.\(^5\)

Thus, the following issues must be examined: (1) loss or outgoing; (2) incurred; (3) positive limbs; (4) negative limbs; (5) apportionment; and (6) deduction.

1. Loss or Outgoing

The taxpayer must incur a loss or outgoing.\(^6\) These terms are given their ordinary meaning. An outgoing occurs upon a form of payment or expenditure, such as payment of interest or a premium.\(^7\) A loss occurs upon diminishment of the taxpayer’s financial resources, such as theft of money or issuing bills/notes at a discount to the face value they are required to be redeemed at.\(^8\)

2. Incurred

The loss or outgoing must be incurred.\(^9\) The amount is deductible once the liability to make it arises, rather than upon the amount actually being paid.\(^10\)

This requires (a) present liability; and (b) properly referable.\(^11\)

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\(^1\) Income Taxation Assessment Act 1997 (Cth), s 8-1.
\(^2\) Income Taxation Assessment Act 1997 (Cth), s 8-5.
\(^3\) Income Taxation Assessment Act 1997 (Cth), s 8-1(1)(a)-(b).
\(^4\) Income Taxation Assessment Act 1997 (Cth), s 8-1(2)(a)-(d).
\(^5\) Ure v FCT ___ 81 ATC 4100 (Deane and Shappard JJ), 4108.
\(^6\) Income Taxation Assessment Act 1997 (Cth), s 8-5(1).
\(^7\) Charles Moore & Co (WA) Pty Ltd v FCT (1956) 95 CLR 344; FCT v La Rosa (2003) ATC 4510.
\(^8\) Coles Myer Finance Ltd v FCT ___ 93 ATC 4214; FCT v Energy Resources of Australia Ltd ___ 96 ATC 4536.
\(^9\) Income Taxation Assessment Act 1997 (Cth), s 8-5(1).
\(^10\) W Nevill & Co Ltd v FCT (1937) 56 CLR 290.
(a) Present Liability

The taxpayer must have completely subjected themselves to making the expenditure,\(^{12}\) in that they have a present liability to pay\(^ {13}\) and have definitely committed to discharging it.\(^ {14}\) Accordingly, it is insufficient that the expenditure will be payable due to a future liability which will arise (even if this is certain)\(^ {15}\) or where it is just a mere possibility that such a liability will arise.\(^ {16}\) A present liability may arise despite the precise date that the liability must be discharged being unknown.\(^ {17}\)

(b) Properly Referable

The amount of the expenditure which is properly referable to the relevant income year must be determined where it continues over multiple income years.\(^ {18}\) Thus, the amount will need to be apportioned between the years. This will likely only apply to financing costs (ie costs associated with the use of something over time, eg interest for use of principle sum\(^ {19}\) or rent and management fees for use of property\(^ {20}\)).\(^ {21}\)

3. Positive Limbs

The expenditure must be incurred in either (a) gaining or producing assessable income; or (b) carrying on a business for the purpose of gaining or producing assessable income.\(^ {22}\) Expenditure may fall under one of both of these limbs.

The expenditure must be incurred in generating the taxpayer’s own assessable income and is not deductible if incurred in generating income for another. However, it is sufficient that a holding company incurs a loss to fund the activities of their wholly owned subsidiary with the purpose of generating profits for itself in the form of dividends.\(^ {23}\)

It is not required that assessable income is actually generated, however, only that it would have been from the relevant activities.\(^ {24}\) Further, it is not essential that a temporal connection exists between the

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\(^{11}\) Coles Myer Finance Ltd v FCT 93 ATC 4214.
\(^{12}\) FCT v James Flood Pty Ltd (1953) 88 CLR 492.
\(^{13}\) Nilsen Development Laboratories Pty Ltd v FCT 81 ATC 4031. Where TP’s employees entitled to leave payments but had not actually taken leave yet, Court held that the expenditure was not yet incurred b/c the TP had no present liability to pay. Irrelevant that it was certain that the amounts would be paid in the future.
\(^{14}\) Ogilvy & Mather Pty Ltd v FCT 90 ATC 4836. Where TP had entered agreement with advertising agency to purchase advert spots and the agreement had passed the cancellation period, the Court held that the TP had no yet incurred the expenditure – b/c TP became definitively committed (ie liable) to paying once the advert was published, not once the cancellation period lapsed.
\(^{15}\) Nilsen Development Laboratories Pty Ltd v FCT 81 ATC 4031. Where TP’s employees entitled to leave payments but had not actually taken leave yet, Court held that the expenditure was not yet incurred b/c the TP had no present liability to pay. Irrelevant that it was certain that the amounts would be paid in the future.
\(^{16}\) FCT v James Flood Pty Ltd (1953) 88 CLR 492; New Zealand Flax Investments Ltd v FCT (1938) 61 CLR 179 (Dixon J), 207.
\(^{17}\) FCT v Citylink Melbourne Ltd 2006 ATC 4404.
\(^{18}\) Coles Myer Finance Ltd v FCT 93 ATC 4214.
\(^{19}\) Coles Myer Finance Ltd v FCT 93 ATC 4214.
\(^{20}\) Merchant v FCT 99 ATC 4221.
\(^{21}\) FCT v Woolcombers (WA) Pty Ltd 93 ATC 5170.
\(^{22}\) Income Taxation Assessment Act 1997 (Cth), s 8-1(1)(a)-(b).
\(^{23}\) FCT v Total Holdings (Australia) Pty Ltd ___ 79 ATC 4279.
\(^{24}\) Robpibon Tin NL v FCT (1949) 78 CLR 47, 56-7.
loss and the gaining of assessable income.\textsuperscript{24} Thus, a loss which occurs in the year before the income may nevertheless be deducted. However, a temporal connection may be a relevant factor depending on the circumstances of the case.\textsuperscript{26}

(a) \textit{Assessable Income}

The expenditure must be incurred in generating assessable income,\textsuperscript{27} in that it is sufficiently connected to the activities of the taxpayer carried out for the production of income.\textsuperscript{28} This occurs where the expenditure is incidental and relevant to the activities/operations regularly carried on for the end of generating income,\textsuperscript{29} in that it has the essential character of a business expense.\textsuperscript{30} It must be one which has the objective complexion of money laid out in furtherance of a purpose of gaining income.\textsuperscript{31}

The character of the expenditure is a question of fact.\textsuperscript{32} It is unnecessary that it is frequent, expected or likely.\textsuperscript{33} Expenditure connected to activities which are prerequisites to earning income is insufficient, as the connection is too remote.\textsuperscript{34} This is so where the expenditure merely places the TP in the position to produce income (eg expenses for driving to work\textsuperscript{35} or eating extra food to make a football team\textsuperscript{36}).\textsuperscript{37} This is so even if the expenditure is required pursuant to a contract of employment, as it will still nevertheless have the character of a prerequisite rather than expenditure incurred \textit{in} the course of employment.\textsuperscript{38}

(b) \textit{Carrying on Business}

The expenditure must be necessarily incurred in carrying on a business for the purpose of generating assessable income,\textsuperscript{39} in that there is a sufficient connection between it and the activities of the business generally.\textsuperscript{40} This occurs where the expenditure is dictated by the business ends which form part or are incidental to the business.\textsuperscript{41} It does not have to be within the ordinary course of the business.\textsuperscript{42}

The expenditure must be necessary to the taxpayer carrying on the business, in that it is appropriate and adapted for the ends of the business.\textsuperscript{43} Accordingly, it will depend on the interests of the taxpayer

\begin{footnotes}
\footnote{Steele v DFCT ___ 99 ATC 4242, 4251.}
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\footnote{Income Taxation Assessment Act 1997 (Cth), s 8-1(1)(a).}
\footnote{Amalgamated Zinc (De Bavay's) Ltd v FCT (1935) 54 CLR 295 (Dixon J), 309.}
\footnote{Ronpibon Tin NL v FCT (1949) 78 CLR 47, 56; W Nevill & Co Ltd v FCT (1937) 56 CLR 290 (Dixon J), 305.}
\footnote{Charles Moore & Co (WA) Pty Ltd v FCT (1956) 95 CLR 344, 351; Lunney v FCT (1958) 100 CLR 478,499-501.}
\footnote{FCT v Phillips ___ 78 ATC 4361 (Fisher J), 4368.}
\footnote{FCT v Phillips ___ 78 ATC 4361 (Fisher J), 4368.}
\footnote{Charles Moore & Co (WA) v FCT (1956) 95 CLR 344.}
\footnote{Lunney v FCT (1958) 100 CLR 478; FCT v Cooper (1991) 29 FCR 177.}
\footnote{Lunney and Hayley v FCT (1958) 100 CLR 478, 498-9.}
\footnote{FCT v Cooper ___ 91 ATC 4395 (Hill J), 4414.}
\footnote{Lunney and Hayley v FCT (1958) 100 CLR 478, 498-9.}
\footnote{FCT v Cooper ___ 91 ATC 4395 (Hill J), 4414.}
\footnote{Income Taxation Assessment Act 1997 (Cth), s 8-1(1)(a)-(b).a}
\footnote{Ronpibon Tin NL v FCT (1949) 78 CLR 47.}
\footnote{FCT v Snowden & Willson Pty Ltd (1958) 99 CLR 431, 436.}
\footnote{FCT v Visy Industries USA Pty Ltd 2012 ATC 20-340, [60].}
\footnote{Magna Alloys & Research Pty Ltd v FCT (1980) 33 ALR 213, (Deane and Fisher J).}
\end{footnotes}
and it does not have to be an unavoidable or essentially necessary.\textsuperscript{44} Logical necessity is not required.\textsuperscript{45}

(i) Prior Expenditure

Expenditure which occurs prior to the commencement of the business activities are insufficient, as they are merely preliminary activities and not incurred within the course of business.\textsuperscript{46} This occurs where the taxpayer has not committed or made a final decision as to business activities but is merely undertaking activities which are directed to deciding whether or not to pursue certain business activities (eg research into field).\textsuperscript{47}

(ii) Subsequent Expenditure

Expenditure which occurs subsequent to the cessation of business will nevertheless be sufficient where the occasion of the expenditure can be traced to the business operations formerly carried on.\textsuperscript{48} The occasion refers to the transaction through which the liability arose.\textsuperscript{49} A refinanced loan (ie one which is transferred into a “new” loan) will be sufficient, as it takes on the same characteristics as the original loan.\textsuperscript{50}

This is distinct from expenditure incurred upon disposal of business, which involves parting with the means through which to generate income and therefore cannot be expenditure incurred in generating income.\textsuperscript{51}

4. Negative Limbs

The expenditure must not non-deductible, in that it is (a) capital nature; (b) private or domestic nature; (c) incurred in generating exempt income or non-assessable non-exempt income; (d) prevented by the Act.\textsuperscript{52}

(a) Capital Nature

The expenditure must not be capital or of capital nature.\textsuperscript{53} This requires a common sense examination of the circumstances as a whole and multiple factors may indicate capital while others indicate revenue.\textsuperscript{54} There are multiple factors which must be considered in determining this.

(i) Factors

\textsuperscript{44} Magna Alloys & Research Pty Ltd v FCT (1980) 33 ALR 213, (Deane and Fisher JJ); FCT v Snowden & Willson Pty Ltd (1958) 99 CLR 431.

\textsuperscript{45} FCT v Snowden & Willson Pty Ltd (1958) 99 CLR 431, 436.

\textsuperscript{46} Softwood Pulp and Paper Ltd v FCT 76 ATC 4439 (Menhennitt J), 4450.

\textsuperscript{47} Goodman Fielder Wattle Ltd v FCT 91 ATC 4438 (Hill J), referring to Softwood Pulp and Paper Ltd v FCT 76 ATC 4439 (Menhennitt J), 4450; Griffin Coal Mining Company Ltd v FCT 90 ATC 4870.

\textsuperscript{48} Placer Pacific Management Pty Ltd v FCT 95 ATC 4459, following AGC (Advances) Ltd v FCT 75 ATC 4057 (Mason J), 4071-2; FCT v Brown 99 ATC 4600.

\textsuperscript{49} AGC (Advances) Ltd v FCT 75 ATC 4057 (Mason J), 4071-2.

\textsuperscript{50} FCT v Jones 2002 ATC 4135.

\textsuperscript{51} Peyton v FCT (1963) 109 CLR 315 (Kitto, Taylor and Owen JJ), 321.

\textsuperscript{52} Income Taxation Assessment Act 1997 (Cth), s 8-1(2)(a)-(d).

\textsuperscript{53} Income Taxation Assessment Act 1997 (Cth), s 8-1(2)(a).

\textsuperscript{54} BPAustralia Ltd  FCT (1965) 112 CLR 386 (Lord Pearce), 397.
An expenditure which is “once and for all” is usually of capital nature, as opposed to reoccurring and regular expenditure which is usually of revenue nature.\footnote{Vallambrosa Rubber Co Ltd v Farmer (1910) 5 TC 529 (Lord Cullen), 536.} Further, expenditure which is incurred in bringing into existence an enduring benefit will usually be of capital nature (eg creation of an asset).\footnote{British Insulated \& Helsby Cables Ltd v Atherton [1926] AC 205 (Viscount Cave), 213.}

Expenditure incurred in relation to business entity is usually of capital nature, as it relates to the structure of the entity which enables it to generate profit rather than the operation of business to actually generate that profit.\footnote{Sun Newspapers Ltd v FCT (1938) 61 CLR 337 (Dixon J); Hallstroms Pty Ltd v FCT (1946) 72 CLR 634 (Dixon J), 647.} This includes expenditure relating to establishing, organising, enlarging, extending or protecting the entity (such as acquisition of a rival newspaper to preserve the TP’s business in the area\footnote{Sun Newspapers Ltd v FCT (1938) 61 CLR 337.}). The following factors must be examined to determine the nature of the expenditure: (i) character of advantage sought; (ii) manner to be used, relied upon or enjoyed; and (iii) means adopted in obtaining it.\footnote{Income Taxation Assessment Act 1997 (Cth), s 8-1(2)(b).}

(ii) \textit{Examples}

- REPAIRS

(b) \textit{Private or Domestic}

The expenditure must not be of private or domestic nature,\footnote{Lodge v FCT 72 ATC 4174; Martin v FCT 84 ATC 4513; Hyde v FCT 88 ATC 4748; Jayatilake v FCT 91 ATC 4516.} in that it is of personal nature or concerns household affairs. This will depend on the essential character of the expenditure and expenditure which is merely a prerequisite to generating income is insufficient (eg childcare costs so that parent can work\footnote{Lodge v FCT 72 ATC 4174.} or moving costs where job relocated\footnote{Mansfield v FCT 96 ATC 4001.}).\footnote{Mansfield v FCT 96 ATC 4001, 4008.}

(i) \textit{Clothing}

Expenditure in relation to acquiring clothing is usually of private and domestic nature and therefore non-deductable.\footnote{Mansfield v FCT 96 ATC 4001, 4008.} This is because the mere fact that a taxpayer is required to dress appropriately at their profession is not sufficient to render such expenses of a business nature.\footnote{Lodge v FCT 72 ATC 4174.}

Further facts may render clothing expenditure of a business nature, however, rather than private or domestic. This is so where the taxpayer is required to frequently change clothes throughout the day.
within their job, where clothing with special features is required due to the job conditions, and where work-related protective clothing is required (eg helmets by construction workers).

(ii) **Home Office**

Expenditure incurred in relation to a home office which is a place of business is of business nature and not private or domestic. This is an area of the taxpayer’s home which is the base of their business operations, in that they do not have an office elsewhere outside their home. Expenditure in relation to both occupancy (eg rent, interest, rates and insurance premiums) and running (eg heating, cooling, lighting and depreciation) are deductible in this case.

Expenditure in relation to a home office which is not a place of business, but merely used in connection with business activities, is not of business nature and is private and domestic. This is so where the taxpayer does have an office elsewhere outside their home and use the home office due to convenience. Expenditure in relation to occupancy is not deductible, although the taxpayer may still deduct running expenses.

(iii) **Commuting**

Expenditure incurred in relation to commuting may be of private and domestic nature or business nature. This will depend on the facts and special rules apply to the calculation of deductions for expensing involving the use of a car.

(A) **During Work**

Expenditure for commuting while the taxpayer is working is of business nature, as it is incurred in the course of generating income and thus deductible. This often occurs where commuting is part of the taxpayer’s job, such as a travelling salesman.

(B) **Between Home and Work**

Expenditure for commuting from home to work and vice versa is of private and domestic nature, as it is not incurred in the course of generating income but in putting the taxpayer in the position to earn income. However, this is subject to some exceptions, where the taxpayer is: (i) an itinerant worker who is required to regularly work at different locations; (ii) a “stand-by” or “on-call” worker; (iii) 

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67 *FCT v Edwards* 94 ATC 4255.
68 *Mansfield v FCT* 2002 ATC 4004. Where flight attendant allowed deduction for expenditure on shoes and stockings, as shoes had to be a bigger size due to air pressure and stockings frequently laddered due to confined spaces in workplace.
69 *Morris v FCT* 2002 ATC 4004. Where taxpayer with outdoor occupation allowed deduction for sunhats, sunglasses and sunscreen.
70 *Swinford v FCT* 84 ATC 4803, 4806.
71 *Swinford v FCT* 84 ATC 4803, 4806, distinguishing *Handley v FCT* 81 ATC 4165, 4173 and *FCT v Forsyth* 81 ATC 4157.
72 Tax Ruling 93/30.
73 *Handley v FCT* 81 ATC 4165, 4173 and *FCT v Forsyth* 81 ATC 4157.
74 *Handley v FCT* 81 ATC 4165, 4173 and *FCT v Forsyth* 81 ATC 4157.
75 Tax Ruling 93/30; *FCT v Faichney* 72 ATC 4245.
77 *Lunney and Hayley v FCT* (1958) 100 CLR 478.
78 *FCT v Wiener* 78 ATC 4006, 4010.
79 *FCT v Collings* 76 ATC 4254; *Owen v Pook* [1970] AC 244.
transporting bulky goods (e.g., musical instruments);\textsuperscript{80} or (iv) a part-time professional athlete required to travel in own vehicle to produce their ‘best form’ at training/matches.\textsuperscript{81}

(B) Between Unrelated Jobs

Expenditure for commuting between unrelated jobs is of private and domestic nature, as it is not incurred while the taxpayer is engaged in income generating activities of either job.\textsuperscript{82}

**BUT see specific deduction for travel between workplaces: s 25-100.**

(C) Obtaining New Work

Expenditure for commuting to obtain new clientele is of business nature and thus deductible. This would occur where the taxpayer is a self-employed builder who commutes to potential clients’ homes and provides quotes for work. In contrast, expenditure for commuting to obtain potential future employment is of private/domestic nature, as it is not incurred in income generating activities but rather in obtaining employment.\textsuperscript{83}

(iv) Travel

Expenditure for travel for business purposes is of business nature and thus deductible.\textsuperscript{84} This is so where the taxpayer devoted the majority of time to business purposes, rather than recreational purposes, and where their motive in travelling is to obtain knowledge to advance their career.\textsuperscript{85} This is particularly so where the travel is undertaken at the request of the taxpayer’s employer.\textsuperscript{86}

(c) Exempt & Non-Exempt Non-Assessable

The expenditure must not be incurred in relation to generate exempt income or non-assessable non-exempt income.\textsuperscript{87}

(d) Act

The expenditure must not be non-deductable pursuant to another provision of either the 1936 or 1997 Acts.\textsuperscript{88}

5. Apportionment

The loss or outgoing is deductible only to the extent that it satisfies the requirements.\textsuperscript{89} A loss which is partly for the required purposes and partly not will only be partly deductible and will require

\textsuperscript{80} FCT v Vogt 75 ATC 4073.
\textsuperscript{81} FCT v Ballesty 77 ATC 4181, 4184.
\textsuperscript{82} FCT v Payne 2001 ATC 4027.
\textsuperscript{83} FCT v Maddalena 71 ATC 4161, 4163.
\textsuperscript{84} FCT v Finn (1961) 106 CLR 60.
\textsuperscript{85} FCT v Finn (1961) 106 CLR 60.
\textsuperscript{86} FCT v Finn (1961) 106 CLR 60.
\textsuperscript{87} Income Taxation Assessment Act 1997 (Cth), s 8-1(2)(c).
\textsuperscript{88} Income Taxation Assessment Act 1997 (Cth), s 8-1(2)(d).
\textsuperscript{89} Income Taxation Assessment Act 1997 (Cth), s 8-1.
apportionment to determine the portion of the loss which may be deducted. This cannot be an arbitrary figure.

There are two kinds of losses which will require apportionment. Firstly, a single expenditure which consists of undivided items for distinct and severable things. This will require division of the sum in accordance with the extent it was applied for gaining income/etc and the extent it was applied for some other purpose. Secondly, a single expenditure which consists of one item but which was applied for something which simultaneously generated income/etc and achieved some other purpose. This cannot be divided arithmetically but requires a fair and reasonable assessment of the extent to which it was applied to generate assessable income/etc.

There is a presumption that expenditure is only for real and genuine income purposes where services are rendered from a related party and the relevant charges were commercially realistic. Alternatively, it is presumed that the expenditure was not wholly for income purposes where the relevant charges were grossly excessive.

6. Deduction

C Case Law


(a) Court
Full High Court
Dixon, Kitto and Windeyer JJ

(b) Procedural history

(c) Material facts
- R senior architect in Public Works Department of WA – responsible for building designs;
- R intended to use combined long service leave and recreation leave to travel overseas and study architectural trends;
- R’s employer requested that he extend travels to South America – extended R’s leave and paid for return fare from England to South America;

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90 *Ure v FCT* __ 81 ATC 4100 (Deane and Shappard JJ), 4108.
91 *Ronpibon Tin NL v FCT* (1949) 78 CLR 47.
92 *Ronpibon Tin NL v FCT* (1949) 78 CLR 47.
93 *Ronpibon Tin NL v FCT* (1949) 78 CLR 47.
94 *Ronpibon Tin NL v FCT* (1949) 78 CLR 47.
95 *Ronpibon Tin NL v FCT* (1949) 78 CLR 47.
96 *Ronpibon Tin NL v FCT* (1949) 78 CLR 47.
97 *FCT v Phillips* __ 78 ATC 4361 (Fisher J), 4368.
98 *FCT v Phillips* __ 78 ATC 4361 (Fisher J), 4368.
- R took leave and travelled – undisputed evidence that he used entire leave to study architecture overseas – kept written record of buildings visited and took a lot of notes and photos, made a lot of sketches and wrote reports;

- R claimed travel expenses as deductions;

- ATO denied deductions on basis that they were not incurred in generating income

(d) Issues

Whether R’s travel expenditure incurred in generating assessable income and thus deductible?

(e) Holdings

Yes

(f) Law

- Information within a person’s professional is not of capital nature -

(g) Application

- R obtaining knowledge made advancement in profession more certain (ie through promotion) -

- R’s motive in travelling and obtaining that knowledge was to advance grade and salary;

- R’s employers treated his desire to increase knowledge as a distinct advantage to their work but also of real importance to at least one project under way;

- Expenditure incidental and relevant to his employed, as it was incurred while R employed, earning a salary, acting in accordance with conditions of his service, and in accordance with the request of his employer;

(h) Order