Attachment A

TREATMENT OF LOSSES FROM NON-COMMERCIAL ACTIVITIES

The Government will tighten the extent to which individuals can offset losses from non-commercial activities against other income.

A deduction will remain allowable provided the activity from which the loss arises satisfies certain criteria. These tests will ensure that only losses arising from commercial business activities can be deducted from other income. They have been designed so that genuine business activities are not disadvantaged, and have been modelled on comparable provisions in other countries.

This is an important integrity measure that contributes to the fairness and equity of the tax law.

Key features

Losses from a business activity carried out by an individual taxpayer can be deducted from other income provided that at least one of the following tests is satisfied.

- The loss arises in relation to the rental of real property and to share (or similar) investments by individuals.

- The loss relates to an activity with assessable income greater than $20,000.

- Total assets of the particular activity exceed $500,000 in real property, or $100,000 of other assets excluding passenger motor vehicles. Under this test, the value to be used for the real property test is the greater of cost or market. The value test for other assets is to be the value for taxation purposes. These tests will enable taxpayers to use existing information to determine eligibility.

- The particular activity results in taxable income in 3 out of the last 5 years.

- The loss arises in circumstances outside the control of the taxpayer including natural disasters, or from an activity with a significant commercial purpose or character.

If a loss is unable to be offset against other income in the year that it arose, it can be offset in a future year when there is a profit from this, or a like, activity, or against other income when one of the criteria is satisfied.

Where special circumstances can be demonstrated that would warrant the recognition of — or make it unreasonable not to recognise — losses in the year they arose, the Commissioner of Taxation will have authority to recognise the losses in that year. The Australian Taxation Office will issue policies, guidelines and criteria for meeting the commercial purpose test.

- An example of where this authority might be exercised is where the activity is affected by circumstances outside the control of the taxpayer — such as prolonged drought, flood, bushfire or other natural disasters.

- Start-up expenditure, particularly in relation to an activity with a long lead-time, will also be considered under the safeguarding arrangement.

Commencement date

The commencement date is 1 July 2000.

Current arrangements

The existing tax law, using the concept of 'carrying-on a business', attempts to minimise the revenue leakage associated with non-commercial activities but has generally been unsuccessful.

Why change is needed

There is significant revenue leakage from unprofitable activities carried out by individual taxpayers claiming deductions for so-called business activities.

- Many of these activities are more like hobbies and/or lifestyle choices. Further, some of these activities have business like characteristics (according to the law), but are often unlikely ever to make a profit and do not have any particular commercial purpose.

The current tax law is complex and resource intensive to administer. The measure seeks to simplify current tax law, remove uncertainty and prevent a significant leakage of revenue from deductions of losses from non-commercial activities.