

JOINT SUBMISSION BY

**The Tax Institute, Chartered Accountants Australia and New Zealand, CPA
Australia, Institute of Public Accountants and Taxpayers Australia**

**Taxation Ruling TR 2016/D1 – Income tax: deductibility of expenditure on a
commercial website**

Date: 20 May 2016

Thank you for the opportunity to comment on Taxation Ruling TR 2016/D1 (“the draft Ruling”) which deals with the deductibility of expenditure on a commercial website.

GENERAL COMMENTS

1. Overall, the joint bodies consider that the draft Ruling adequately addresses the issues. We are pleased to see the inclusion of multiple practical examples that should assist users of the Ruling.

SPECIFIC COMMENTS

1. We suggest that the Ruling could provide some additional direction regarding the income tax treatment for the following two issues:
 - a. data and content available on or incorporated into a commercial website that has independent value to the business (‘not considered part of a commercial website’ at paragraph 8). Furthermore, content on a website that is not incidental to the website and having value separate from the website, may not be in-house software under sub-paragraph 40(c); and
 - b. software associated with a commercial website, that does not meet the requirements of the definition of ‘in-house software’. Paragraph 43 flags potential capital gains tax (CGT) or s.40-880 treatment. However, potential treatment as copyright (as an item of intellectual property) under Division 40 is not discussed.

Definitions

2. We note that the draft Ruling defines a ‘commercial website’ in paragraph 5, but that term is only used occasionally throughout the remainder of the draft Ruling. The term ‘website’ is used on its own frequently throughout the draft Ruling (e.g. in paragraphs 20-27 and 29-37). We suggest that the term ‘commercial website’ should be used consistently throughout where relevant.
3. We suggest that the definition of ‘website’ in paragraph 6 also refer to associated content on the website, for consistency with sub-paragraph 40(c).
4. We suggest that paragraph 6 would be better placed before paragraph 5. Specifically, it may be useful to firstly define a ‘website’ (currently paragraph 6), and then identify the business nexus that makes it a ‘commercial website’ (currently paragraph 5).
5. We suggest that ‘data and’ be inserted before ‘content’ in the third dot point of paragraph 8, for consistency with paragraph 39.

6. We suggest that some examples be provided of data and/or content which have an independent value to the business as mentioned in paragraph 8. Examples might include photographs displayed on the website of a photography business or a customer email list. Another example may be electronic copies of the business's publications which can only be accessed by subscribers who have paid a fee for that access. The electronic copies of the publications may otherwise be purchased by non-subscribers for a set price (ie. they have independent value to the business).
7. We suggest that paragraph 8 would be better placed before paragraph 7.
8. We suggest that paragraph 11 would be better placed between paragraphs 44 and 45, given that the concept of 'depreciating asset' (mentioned in paragraph 11) is covered in paragraphs 37-44. Also, paragraph 11 and example 2 should make it clear that the relevant dividing line between deductible and non-deductible, for this purpose, is taxable purpose, not "business" per se. See paragraph 134 which correctly references taxable purpose; as paragraph 134 is not in the binding section of the Ruling, we recommend that the taxable purpose reference is replicated in paragraph 11. We also suggest that example 2 contains wording to the effect that the depreciable portion is determined by reference to the taxable purpose.

Types of Expenditure

9. We query whether the ATO considers that on-costs are a part of employee expenses, in the context of the first dot point of paragraph 12 and the coverage of 'salary and wages' in paragraphs 144-148. If so, we suggest that:
 - a. 'including on-costs' be appended to the first dot point of paragraph 12; and
 - b. the meaning of 'on-costs', including examples, be covered in paragraph 145 and/or 147.
10. We suggest that reference be made to website hosting fees in paragraph 18, given that such fees are stated to be revenue in nature in Examples 2, 4, 17 and 18.

Maintaining a website

11. It would be helpful to have an example of the type of modification covered in paragraph 22.
12. We suggest that in paragraph 23:
 - a. Example 8 be linked to the end of the first sentence;
 - b. 'significant' be inserted before 'new functionality' in the second sentence, in order to differentiate from adding minor functionality, as referred to in the first sentence.
 - c. a reference be made after the second sentence: '(see paragraphs 25-32 of the draft Ruling), in order to link this paragraph to the commentary on modifications, rather than leaving the paragraph ending with the less-helpful 'is capital'.
13. Given the trend towards businesses which operate purely online but are not themselves IT businesses, we suggest that at least two further examples of the capital vs revenue distinction (upgrade vs routine maintenance) be provided in the context of non-IT businesses with which most readers of the Ruling would be familiar, such as:
 - a. redesign of an insurance product comparison website, and
 - b. constant refreshing of a home decorating website from which the business makes money from advertisements displayed on the site.

14. We recommend that the term 'day-today' should be removed from paragraph 27 as this narrows the catchment of an operational cost. Paragraph 21 explicitly states that responding to an unexpected event would generally be regarded as maintenance (ie. revenue/deductible). Clearly, dealing with an infrequent website breakdown is not a day-to-day operation.

Modifying a website

15. It might be useful to have a section above 'Content migration' with the subheading 'Data and content' and to explain what is meant by these two terms. Further in this regard we suggest that:
- a. paragraph 34 be moved under the subheading 'Data and content'; and
 - b. an example be provided of content that has independent value (also see above comment above regarding paragraph 8).
16. In relation to paragraphs 33 and 35, we suggest that clarification be added regarding whether the initial uploading of content is to be similarly treated. Migration suggests moving from another website or format, whereas uploading may not involve any previous website or format, e.g. where a photography business requires initial and ongoing uploads of photos which are not migrated from another format or website.
17. We suggest the first sentence of paragraph 35 be changed to read 'If content is migrated as part of establishing a new commercial website or upgrade that significantly enhances or replaces the commercial website, the cost is a capital expense.' This change is necessary given the next sentence suggests that migrating as part of a non-significant upgrade is revenue.
18. If clarification is added to paragraph 33 that uploading of content is to be treated similarly to migration of content, then similar clarification should also be added in paragraph 35, e.g. 'If content is migrated or uploaded...' at the beginning of each sentence.
19. In relation to paragraph 36, we suggest that:
- a. clarification be added regarding whether the costs of establishing the presence are in-house software or some other type of asset - such clarification could be inserted into paragraph 36 or in paragraph 40 or 41-43; and
 - b. Example 16 be expanded to cover costs of establishing a presence.
20. We suggest that the ATO includes commentary in relation to micro-sites that have a related but distinct identity and domain name from the main business website. For example, a business may create a micro-site dedicated to a new product, rather than simply uploading a webpage with the details of the product amongst all of its other product description pages. While website updates relating to routine product changes and announcements is likely to be maintenance, would the creation of a separate micro-site be considered to be a modification of a capital nature?

In-house software

21. In relation to paragraph 40, we suggest that:
- a. sub-paragraph (a) include clarification that such software which is used to enable further interaction with the user may itself be in-house software, but is separate from the commercial website in-house software;
 - b. Example 18 be expanded to explain what is meant by 'providing it mainly for the user's own benefit';
 - c. 'data and' be inserted before 'Content' at the beginning of sub-paragraph (c) for consistency with paragraph 39;

- d. sub-paragraph (c) clarify whether the migration of data and content which is capital in nature is also 'in-house software'; and
 - e. a link be provided between sub-paragraph (c) and the suggested examples mentioned above in respect of paragraph 8.
22. In relation to both paragraphs 41 and 42, we suggest that clarification be added that the application software is also likely to be 'in-house software', albeit separate from the commercial website 'in-house software'.
23. We suggest that paragraph 43 include reference to software being potentially copyright if it is not 'in-house software'. The income tax treatment of copyright should then be covered in the Ruling (e.g. between paragraphs 207 and 208) unless scoped out (see earlier comment).

CGT

24. In relation to paragraph 45:
- a. it appears that the word 'not' is missing from the second sentence - it seems the sentence should read '... and does not constitute...'; and
 - b. it would be useful to have an example of such an asset which is not in-house software but which would be a CGT asset – perhaps a trademark would fall into this category?

Section 40-880

25. We consider that paragraph 46 misleadingly suggests that the two alternatives are section 40-880 and software development pool. We recommend replacing the second sentence with: 'Section 40-880 will generally not apply to commercial websites because capital expenditure on software development will usually be 'in-house software' and, if not, it would likely in any case be part of the cost base of a CGT asset'.
26. We suggest that paragraph 47 clarify whether the ATO accepts that every two years is 'periodic', given this seems to be the common domain name renewal requirement.
27. We suggest that the first sentence of paragraph 48 clarify whether 'An amount paid once-and-for-all to secure the right to use a domain name' refers to the initial registration of the domain name, which is when the first two-yearly fee is paid.

Examples

28. We suggest that Example 21 would be better referenced at the end of paragraph 49 as the example does not contain a nil amount scenario.
29. We suggest that paragraph 84 (Example 9) clarify what is meant by 'annual expenditure' – does it mean the sum of several years' spend on maintenance (revenue)?
30. In the first dot point of paragraph 97 (Example 13), it is unclear why the creation of website software is not stated to be 'in-house software'. If the ATO considers that it is in-house software the example should state that. If not, then for the purposes of this example, we suggest that the words 'create website software that' could be removed to make the point more clearly about this option being expenditure on the existing commercial website.

31. In relation to paragraph 100 (Example 14), the placement of the words 'acquiring newly released handsets and operating systems' suggests that these costs would also be revenue costs. Is that the ATO's intention? If the ATO does not intend that these costs are revenue, then it would be useful to clarify that these items are hardware (hence, outside the scope of the Ruling). If the ATO does intend that these costs are revenue, we suggest that:
 - a. such items be included in an extra point in paragraph 12; and
 - b. a further section be added about such costs after paragraph 14.

32. We suggest that Example 16 be expanded to cover the income tax treatment of labour costs involved in establishing the social media profile, in order to show how this differs from the maintenance of the profile.

33. In relation to Example 18:
 - a. It is unclear why reference is made to two versions of the website-building tool. Does the ATO intend that the versions be treated differently? If so, this is not clear from the Example. Paragraphs 114 and 117 would benefit from clarification.
 - b. In the first sentence of paragraph 115, it would be helpful to clarify the reference to the 'application' - which version is intended to be referenced?
 - c. In the second sentence of paragraph 115, it is not clear what is meant by 'the software' – is this the application software or the website? Clarification would assist the reader.
 - d. In paragraph 118, it may be helpful to clarify that the 'website-building application' is the fully featured version, given that SitesAtWork only charges a fee for the fully featured version.

34. We suggest that paragraph 124 (Example 20) conclude by clarifying how to treat the costs of developing the Nebula software, i.e. is it 'in-house software' but separate from the commercial website 'in-house software'?