TD 93/D92 - 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 of gold miners?

This document has been finalised by TD 93/127.

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Draft 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 of gold miners?

1. Some gold producers have on hand at balance date stocks of gold bearing ore, whose gold content is below the cut off grade for processing, but have been stockpiled for processing at a later date if the price of gold rises and/or costs fall. These stocks may have been valued under subsection 31(2) at a lower than market or nil value.

2. 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.

3. As indicated by Taxation Ruling TR 93/3, the notional market value of gold ore is calculated by taking the spot price of gold, less the estimated future costs, less the profit margin of the purchaser. Although not unknown, it would be a rare situation where low grade ore is actually purchased on the market.

4. The application of subsection 31(2) is limited in the case of low grade ore stocks which represent the early stages of work in progress, and have a largely notional market value. Fluctuations in gold prices cause the market valuation of these stocks to vary, and the market value may fall below cost. These fluctuations are a normal occurrence with all metals, including gold, and do not constitute special circumstances for the purpose of subsection 31(2).

5. If a notional market value is capable of reasonable estimation, it must be applied before subsection 31(2) is considered. However, if there is no prospect of the trading stock having any future market value, and the producer has no intention of further processing these stocks, a nil value may be justified in terms of subsection 31(2).

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 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 30% = $75

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

If spot price of gold falls to $400
b) *MSV = $75*

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

Only in part c) of the example above should subsection 31(2) be applied, and only where :
. there is no prospect of the gold price rising above $325 before the end of the life of the mine, and
. the producer has made a decision not to process these stocks further during the life of the mine.

Commissioner of Taxation
15/04/93

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