Summary of tax depreciation measures

For the 2019-20 to 2022-23 income years

Numerous changes have been made to the tax depreciation measures since 12 March 2020. This bulletin sets out a summary of these new measures for the 30 June 2020 to 30 June 2023 income years.

The following is intended as an overview of the regimes governing the deductibility of costs incurred in acquiring and improving depreciating assets. As should be clear, there are significant differences between the regimes and their interaction requires a careful consideration of the date on which depreciating assets are first used or installed ready for use. Furthermore, this bulletin does not consider complex interactions with the tax consolidation regime.

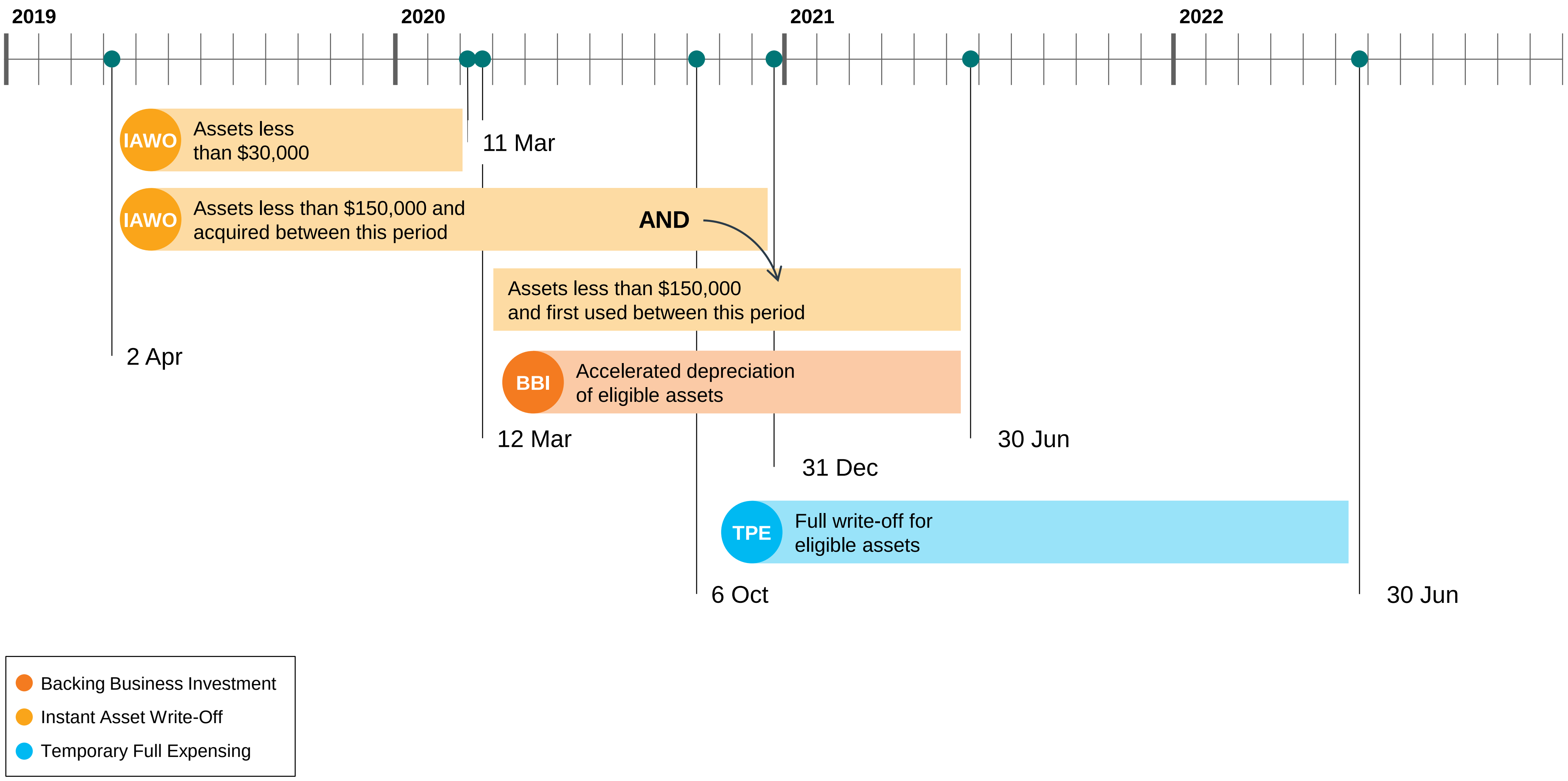
The tables provided and the more specific information about each measure have to be taken into consideration all together and not viewed in isolation.

It is critical that clients review their fixed asset register and capital expenditure plans and consider how the rules apply, especially as part of their year-end tax planning. Clients should contact their Pitcher Partners representative to review their situation and determine what action is required.

We note that this summary assumes that the 12-month extension of the temporary full expensing measures (to 30 June 2023) announced in the May 2021 Federal Budget will become law.

Applying the tax depreciation measures

Depending on the business's aggregated turnover, eligible assets can qualify for one of the capital allowance incentives. If more than one incentive could apply, the order of application subject to opt out choices is (1) temporary full expensing (2) instant asset write-off (3) backing business investment. The table is timeline is based on date asset first used (or installed ready for use) for a taxable purpose.



Brief overview of eligibility of business based on aggregated turnover

Eligibility of the assets for the different measures has to fulfill all requirements for each measure to be considered accordingly. Exclusions or additional specific requirements may apply. Separate rules apply regarding eligibility of accelerated depreciation on second element costs. Alternative TFE for entities with over $5 billion aggregated turnover not covered.

<table>
<tr><th>Aggregated turnover
in current or prior year</th><th>BBI Backing business investment
Asset first used or installed in business between 12 Mar 2020 and 30 Jun 2021</th><th>IAWO Instant asset write-off
Asset first used or installed in business from 12 Mar 2020 to 30 Jun 2021</th><th>TPE Temporary full expensing
Asset first used or installed in business from 6 Oct 2020 to 30 Jun 2023</th></tr>
<tr><td>Less than $10m
Small business using simplified depreciation</td><td>57.5% deduction in year of allocation to pool
No cost restriction
Cannot opt out on asset-by-asset basis
Second-hand assets excluded</td><td>Full write-off
Asset cost < $150,000
Full write-off of small business pool if balance < $150,000 at 30 June 2020
Available for second-hand assets
Cannot opt out</td><td>Full write-off including the balance of a small business pool for 30 June 2021, 2022 & 2023
No cost restriction
Available for second-hand assets
Cannot opt out on asset-by-asset basis</td></tr>
<tr><td>Less than $10m
Small business not using simplified depreciation</td><td rowspan="3">Accelerated depreciation of 50%+ in first year
No cost restriction
Can opt out
Second-hand assets excluded
Exclusion for commitments entered into prior to 12 March 2020</td><td>Not eligible</td><td rowspan="2">Full write-off
No cost restriction
Available for second-hand assets
Can opt out on asset-by-asset basis</td></tr>
<tr><td>$10m to less than $50m
Medium business</td><td rowspan="2">Full write-off with asset cost < $150,000
Cannot opt out
Asset must be acquired between 2 April 2019 and 31 December 2020
Available for second-hand assets</td></tr>
<tr><td>$50m to less than $500m
Medium business</td><td rowspan="2">Full write-off
No cost restriction
Can opt out on asset-by-asset basis
Second-hand assets excluded
Exclusion for commitments entered into prior to 6 October 2020</td></tr>
<tr><td>$500m to less than $5b
Large business</td><td>Not eligible</td><td>Not eligible</td></tr>
</table>

Instant Asset Write Off (IAWO)

IAWO

Section 40-82 of the Income Tax Assessment Act 1997 contains the IAWO rules for medium sized businesses. This measure provides for a deduction of the entire cost of a depreciating asset provided certain requirements are met.

Date asset first used (or installed ready for use) for a taxable purpose

Asset must have been acquired between 7:30 pm on 2 April 2019 and 31 December 2020		
	Before 12 March 2020 if the following are satisfied	**Between 12 March 2020 and 30 June 2021 if the following are satisfied**
Entity's turnover	Between \$10 million and \$50 million	Between \$10 million and \$500 million
Asset's total cost	Less than \$30,000 as at 30 June 2020	Less than \$150,000 as at 31 December 2020

Business and turnover

Entity must carry on a business in the year of first taxable use.

No requirement that asset be used in the carrying on of a business but adjustment to deduction if asset not wholly used to produce assessable income.

Entity can use current year (i.e. year of seeking to claim IAWO) or previous year aggregated turnover to satisfy relevant turnover threshold.

SBE

Small business entities (aggregated turnover in the current or prior year of less than \$10 million) are excluded and must therefore use simplified depreciation rules to access IAWO.

Assets

Available for second-hand assets and assets used overseas.

IAWO not available for
Capital works, certain primary production assets or software development expenditure where the entity has existing software development pool.

Capital improvements to the asset (second element costs)

If incurred in year of first taxable use, the second element cost is included in the total cost that is measured against relevant cost threshold at relevant date.

If incurred in year after first taxable use only available where IAWO previously applied to the initial acquisition:

12 March 2020	31 December 2020	
Eligible for IAWO if second element cost was less than \$30,000, was incurred prior to 12 March 2020 and the acquisition previously eligible for IAWO.	**Eligible for IAWO if second element cost was less than \$150,000**, was incurred between 12 March 2020 and 31 December 2020 and the acquisition of the asset was eligible for IAWO in previous year (i.e. 2018-19 or 2019-20 income years).	

Opt-out of IAWO not available for any assets

Backing Business Investment (BBI)

BBI

Subdivision 40-BA of the Income Tax (Transitional Provisions) Act 1997 contains the rules for the BBI measure. This measure provides for a deduction of 50% of the asset's cost in the first year.

Date asset first held and first used (or installed ready for use) for a taxable purpose		
	12 March 2020 **30 June 2021**	
	Exclusion for commitments entered into before 12 March 2020 (e.g. existing contract to acquire asset or construction of asset already commenced). **Integrity rule** where pre-12 March 2020 commitment cancelled, and new commitment entered into after 12 March 2020 for identical or substantially similar asset.	

Business and turnover

Entity must carry on a business in the year of first taxable use.

Asset must be used for the principal purpose of carrying on a business.

Adjustment to deduction if asset not wholly used to produce assessable income.

Entity's aggregated turnover is less than $500 million (in the current or prior year).

SBE

Small business entities eligible (i.e. those with aggregated turnover in the current or prior year of less than $10 million), where they otherwise are not applying simplified depreciation rules.

Assets

No cost limit for asset to be eligible.

BBI not available for	
Second-hand assets or those principally used or located overseas	Capital works, certain primary production assets or software development expenditure where the entity has existing software development pool.

Calculation

50% of total cost at end of the income year (regardless of time of year asset first used).

Remaining 50% deductible under standard rules using effective life (prime cost or diminishing value) which includes days basis apportionment in first year based on time of first use.

Capital improvements to the asset (second element costs)

If incurred in year of first taxable use, then included in cost amount to which BBI applies.

BBI not available if second element costs incurred in year after first taxable use (but may qualify for TFE).

Ability to opt-out of BBI available on an asset-by-asset basis

Temporary Full Expensing (TFE)

TFE

Contained in Subdivision 40-BB of the Income Tax (Transitional Provisions) Act 1997. This measure provides for a deduction of the entire cost of a depreciating asset.

Date asset first held and first used (or installed ready for use) for a taxable purpose		
	7:30 pm on 6 October 2020	30 June 2023
	For entities with aggregated turnover (in current and prior year) of $50 million and over **Exclusion** for commitments entered into before 6 October 2020 (e.g. existing contract to acquire asset or construction of asset already commenced); **Integrity rule** where pre-6 October 2020 commitment cancelled, and new commitment entered into after 6 October for identical or substantially similar asset.	

Business and turnover

Entity must carry on a business in the year of first taxable use.

Asset must be used for the principal purpose of carrying on a business.

Adjustment to deduction if asset not wholly used to produce assessable income.

Balancing adjustment may apply to deem a disposal at market value if later use changes to principally overseas use or non-business use.

Entity has aggregated turnover of less than $5 billion (in the current or prior year).

Alternative test available for certain corporate tax entities with aggregated turnover of $5 billion and over.

SBE

Small business entities (i.e. those with aggregated turnover in the current or prior year of less than $10 million) are eligible where they otherwise are not applying simplified depreciation rules.

Assets

No cost limit for asset to be eligible.

TFE not available for			
Acquisition of (but not improvements to) second-hand assets unless aggregated turnover (in current or prior income year) is less than $50 million.	Assets principally used or located overseas	Capital works, certain primary production assets or software development expenditure where existing software development pool.	Where a balancing adjustment happens to the asset in first year (including change in partnership interests if entity is a partnership).

Capital improvements to the asset (second element costs)

TFE available for second element costs incurred between 6 October 2020 and 30 June 2023) including in respect of second-hand assets for all entities regardless of turnover (e.g. available for entities with over $50 million aggregated turnover even if excluded from TFE for initial acquisition).

Ability to opt-out of TFE available on an asset-by-asset basis

Things to keep in mind

Overlap and priority

The above measures have the potential to overlap in respect of the same asset.

Hierarchy of application

1. **Temporary Full Expensing**
TFE

2. **Instant Asset Write-Off**
IAWO

3. **Backing Business Investment**
BBI

Opting-out of the **TFE** measure may result in one of the other measures operating:

- If the asset also meets the **IAWO** criteria, opting-out of TFE is of no practical consequence as the full cost may be deductible under **IAWO** in any case (e.g. assets costing less than $150,000 acquired before 31 December 2020 that were first used or installed between 6 October 2020 and 30 June 2021 could qualify for both TFE and IAWO such that opt-out of TFE does not change the outcome).
- If the asset also meets the **BBI** criteria, opting-out of both TFE and BBI is required if the entity wishes to depreciate for tax purposes using standard effective lives.
- If opt-out of TFE or BBI was chosen for the initial acquisition of the assets, opt-out may need to be **chosen again** for any second element costs incurred in a later year to improve the asset that would be eligible for TFE.

Other considerations

Key dates	Hardwired into the legislation and not adjusted for entities with substituted accounting periods.
R&D	Depreciation calculated under IAWO/BBI/TFE can count towards an eligible corporate tax entity's R&D tax offset where asset used for R&D purposes.
Assets	Measures apply to both tangible and intangible assets (e.g. in-house software).
Luxury car limit	IAWO/BBI/TFE for cars is limited to the luxury car limit ($57,581 for the 2019-20 income year, $59,136 for the 2020-21 income year and $60,733 for the 2021-22 income year).
Additional interaction provisions	Must be considered where assets are brought into a tax consolidated group as a result of a joining event.

Small Business Entities (SBEs)

An entity is an SBE for an income year if it carries on a business that year and has aggregated turnover of less than $10 million in the current or prior year. SBEs may use simplified depreciation under Subdivision 328-D of the Income Tax Assessment Act 1997.

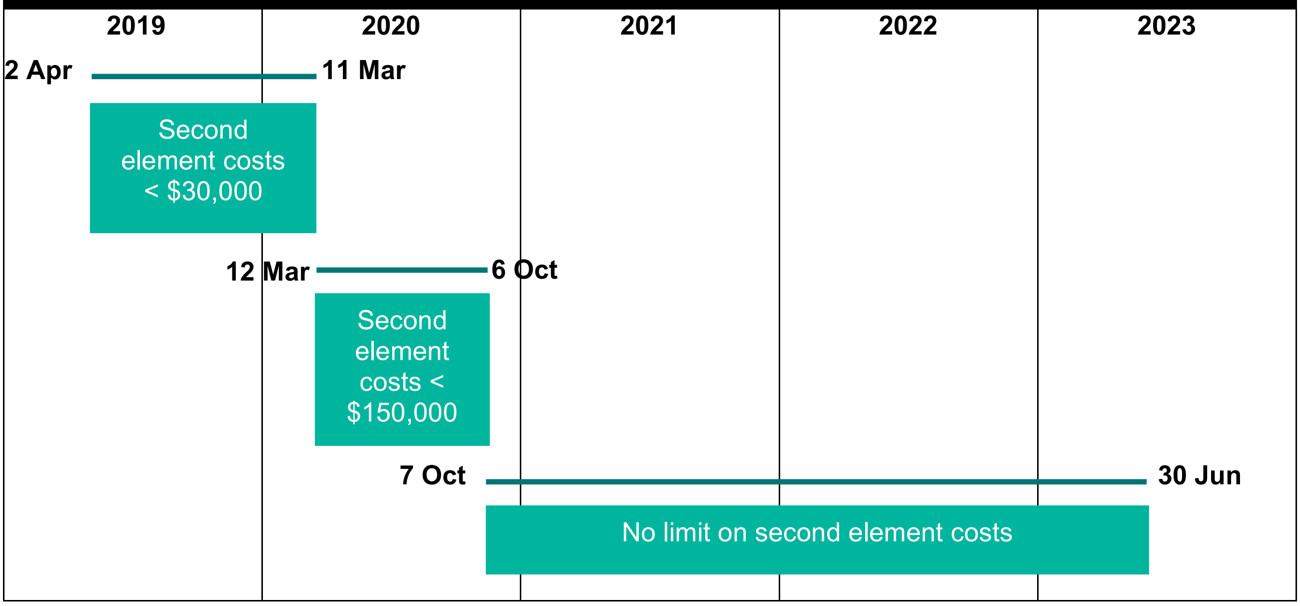
IAWO for SBEs using simplified depreciation

An SBE is entitled to an immediate deduction of the cost of eligible depreciating assets if:
The asset is first acquired after **7:30 pm on 2 April 2015**
The asset's cost at year end is **less than $30,000** if **first used (or installed ready for use)** for a taxable purpose **prior to 12 March 2020**
The asset's cost at year end is **less than $150,000** if **first used (or installed ready for use)** for a taxable purpose **between 12 March 2020 and 6 October 2020**
If the asset was **first used (or installed ready for use)** for a taxable purpose between **6 October 2020 and 30 June 2023** • No cost limit applies
IAWO for cars acquired by an SBE is limited to the **luxury car limit** • $57,581 for the 2019-20 income year • $59,136 for the 2020-21 income year • $60,733 for the 2021-22 income year
Available for second-hand or overseas assets and no exclusion for "pre-commitments".
Adjustments required where asset not wholly used to produce assessable income

Capital improvements to the asset (second element costs)

If incurred in year of first taxable use, included in the total cost and measured against relevant cost threshold at relevant date.

If incurred in year after first taxable use, only available where IAWO for SBEs also applied to the initial acquisition of the asset and



Choice to use simplified deprecation

Where simplified depreciation is not chosen, the IAWO, BBI and TFE rules may apply as above, noting that the IAWO is not available for SBEs. Choosing not to apply the simplified depreciation rules for an income year may result in an SBE being temporarily "locked-out" of the rules if the entity had previously used those rules.

Using the simplified depreciation rules for SBEs results in those rules applying to all eligible depreciating assets (other than excluded assets covered below) rather than on an asset-by-asset basis. SBEs using the rules will therefore be required to apply both the general small business pooling rules as well as having access to the IAWO for SBEs. A choice to use simplified depreciation for SBEs should be evidenced in the tax return by completing the labels relating to simplified depreciation.

Exclusions
Certain assets are also excluded from simplified depreciation for SBEs including certain primary production assets (unless the SBE chooses otherwise), horticultural plants, assets that the entity predominantly leases out and second-hand assets used in residential property.

General small business pool

SBEs choosing to use simplified depreciation must also use the general small business pool for all eligible depreciating assets.

No opt-out on an asset-by-asset basis available.

General rules

Deduction equal to 15% of cost of asset in year added to the pool as well as 15% deduction of second element costs in year incurred.

Deduction of 30% of the opening pool balance each year.

When first electing into simplified depreciation, all eligible depreciating assets are brought into the pool as part of the opening balance at their tax written down values.

Pooling continues to apply even if the entity stops being a SBE or stops using simplified depreciation.

Pool balance written-off once below $1,000.

Temporary modifications for 30 June 2020 to 30 June 2023 income years

IAWO — Assets only added to pool if not written off in full under IAWO for SBEs.

BBI — Assets that would qualify for BBI in the 30 June 2020 income year (new business assets first held and used for a taxable purpose between 12 March 2020 and 30 June 2020) are eligible for 57.5% deduction in the year they are added to the pool.

Pool balance is written-off for 30 June 2020 if less than $150,000.

Pool balance is written-off for 30 June 2021, 30 June 2022 and 30 June 2023 income years regardless of balance.

Sale of assets

Sale of pool asset results in a reduction of the pool balance by sale price with any excess over the pool balance brought to account as assessable income.

IAWO — Sale price of asset previously claimed under IAWO for SBEs is fully assessable.

What are the next steps?

The above is intended as an overview of the regimes governing the deductibility of costs incurred in acquiring and improving depreciating assets.

As should be clear, there are significant differences between the regimes and their interaction requires a careful consideration of the date on which depreciating assets are first used or installed ready for use.

It is critical that clients review their fixed asset register and capital expenditure plans and consider how the rules apply. Clients should contact their Pitcher Partners representative to review their situation and determine what action is required.

Contact us

Alexis Kokkinos
Partner

p. +61 3 8610 5170
e. alexis.kokkinos@pitcher.com.au

Peter Gillies
Client Director

p. +61 3 8610 5361
e. peter.gillies@pitcher.com.au

Leo Gouzenfiter
Senior Manager

p. +61 3 8612 9674
e. leo.gouzenfiter@pitcher.com.au