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GUIDE TO DEPRECIATION

2000–01

TAXPACK REFERRED PUBLICATION

AUSTRALIAN TAXATION OFFICE

www.ato.gov.au

How self-assessment affects most individuals

Self-assessment means the Australian Taxation Office (ATO) uses the information you give in your tax return to work out your refund or tax bill. You are required by law to make sure you have shown all your assessable income and claimed only the deductions and tax offsets to which you are entitled.

What are your responsibilities?

Even if someone else—including a tax agent—helps you to prepare your tax return, you are still legally responsible for the accuracy of the information.

What if you lodge an incorrect tax return?

Our computers continually check for missing or wrong information. We have audit programs designed to detect where taxpayers have not declared all of their assessable income or where they have incorrectly claimed deductions or tax offsets. If you become aware that your tax return is incorrect, you must contact us straightaway.

Initiatives to complement self-assessment

There are a number of initiatives administered by the ATO which complement self-assessment. Examples include:

- a change in penalty provisions so that if you take reasonable care with your tax affairs, you will not receive a penalty for honest mistakes—but please note that interest on omitted income or overclaimed deductions and tax offsets could still be payable
- the process for applying for a private ruling
- your entitlement to interest on early payment or overpayment of a tax debt
- the process for applying for an amendment if you find you left something out of your tax return.

Do you need to ask for a private ruling?

If you have a concern about the way tax law applies to your personal tax affairs, you may want to ask for a private ruling.

A private ruling will relate just to your situation. Write to the ATO describing your situation in detail and ask for advice. Include your tax file number. If you lodge your tax return before you receive your private ruling, be aware that the ruling may alter the accuracy of your return.

You can ask for a review of a private ruling decision if you disagree with it, even if you have not received your assessment. The ATO can give you more information about review procedures.

Copies of publications

To get a copy of any publication referred to in this book:

- visit our Internet site at **www.ato.gov.au**
- ring our Publications Distribution Service on **1300 720 092** for the cost of a local call or
- visit an ATO office.

Publications referred to in this book include:

- *Taxation Ruling IT 2308—Income tax: depreciation of plant acquired otherwise than by purchase*
- *Taxation Ruling IT 2685—Income tax: depreciation*
- *Taxation Ruling TR 2000/18—Income tax: depreciation effective life*
- *Taxation Ruling IT 26—Computers—depreciation, investment allowance*

Feedback

Reader feedback helps us to improve the information we provide. If you have any comments to make about this book, please write to:

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As this is a publications area only, any tax matters will be passed on to a technical area. Otherwise you can ring our Personal Tax Infoline on **13 2861** for help.

Guide to depreciation
2000–01

Australian Taxation Office
Canberra

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About this publication

This publication is available free from the Australian Taxation Office (ATO). The ATO prohibits any party from selling it. We regularly revise our publications to take account of changes to the law.

If you have an enquiry relating to your circumstances which this publication does not cover, ring the Personal Tax Infoline on **13 2861** or get help from a tax adviser.

As part of our commitment to produce accurate publications, taxpayers will not be subject to penalties if they can demonstrate that they based a tax claim on wrong information supplied by the ATO.

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What is depreciation?

Under income tax law, you are allowed to claim deductions for expenses incurred in earning assessable income—for example, recurring expenses such as rent, wages and electricity. Some expenses, such as the cost of acquiring capital assets, are not allowable. Capital assets are those which provide a benefit over a number of years—for example, motor cars and machinery.

The value of such assets gradually reduces over time as they approach the end of their effective lives. Assets which lose value in this way are said to depreciate. In recognition of this fact, the cost of capital assets used in producing assessable income can be written off over a period of time as tax deductions.

Under income tax law, the term 'depreciation' is applied to plant—for example, cars and machinery. The depreciation provisions also apply to expenditure on computer software. Software includes a licence to use it.

Under measures contained in *New Business Tax System (Capital Allowances) Act 1999*, the depreciation provisions also apply to expenditure on an indefeasible right to use an international telecommunications submarine cable system (IRU).

The general depreciation provisions that apply to plant are modified for software and IRUs. This publication first covers the general provisions and then outlines, on pages 14 and 15, the variations for software and IRUs.

Depreciation terms

Termination value usually arises when you dispose of an item of plant; it is the sale proceeds less any expenses reasonably attributed to the sale. The amount of any GST is excluded from the termination value if the plant is sold as a taxable supply. Special rules apply where:

- plant is disposed of under a non-arm's length transaction—termination value is its market value
- plant is lost or destroyed—termination value is the amount or value receivable under an insurance policy or otherwise
- plant is disposed of other than by sale for example, by gift, bequest or scrapping—termination value is its market value
- plant becomes trading stock—termination value can be its cost or market value
- a partial change in the ownership or quasi-ownership of plant occurs—termination value is its market value
- the plant is a car that is or has been affected by the luxury car lease provisions
- the plant is a car acquired at a discount under a scheme to avoid the car depreciation limit
- the plant is a car and its cost exceeds the car depreciation limit
- the plant is attached to land over which quasi-ownership rights are held and
- the taxpayer holding the plant that has become a fixture on the land as its quasi-owner, ceases to be its quasi-owner.

If you are not sure of the termination value of plant for depreciation purposes, contact your professional tax adviser or ring the Australian Taxation Office (ATO).

Undeducted cost is the cost of the plant less the sum of your depreciation deductions and any further amounts that you could not deduct because you used the plant other than for producing assessable income—for example, private use of the plant or because a deduction is prevented by the income tax law such as for certain plant used for leisure facilities.

Written down value is generally the cost of the plant less the sum of your depreciation deductions.

Which items can you depreciate?

The depreciation provisions apply to plant that is used to produce assessable income or is installed ready for use to produce assessable income and is held in reserve. Plant includes:

- computers
- electric tools
- furniture and fittings
- furnishings—carpets and curtains
- manufacturing machinery
- motor vehicles.

In some situations, various other assets which are generally not regarded as plant are also depreciable under income tax. They include:

- working animals—for example, racehorses—not used in primary production
- structural improvements—for example, fences and dams—on land used in primary production and forest operations
- plumbing fixtures and fittings in premises principally for the use of employees or for the care of the children of employees
- software, including a licence to use it.

Buildings are not generally plant or included in plant but a deduction similar to depreciation may be available under the separate deduction provisions for capital works.

In most instances, it will be clear whether or not something is an item of plant. However, if you are not sure whether an item qualifies for depreciation, contact your professional tax adviser or ring the ATO.

Which items can't you depreciate?

There are a few items of plant on which you cannot claim depreciation. They are:

- plant where a deduction is available under the provisions for specific landcare operations or facilities to conserve or convey water
- research and development plant unless you have elected that the research and development provisions are not to apply to that plant
- leisure facilities and boats unless, at some time in the income year, their use constitutes a fringe benefit or you used them for certain specific business purposes.

Who can depreciate plant?

Only owners or quasi-owners can depreciate plant. You will be treated as the owner of the plant for depreciation purposes if you are the legal owner or you hold sufficient rights over the plant to characterise you as the owner in preference to any other person who also holds rights over the plant.

Quasi-ownership covers the situation where plant is attached to land that you do not own but have a right to use. This only applies where the land is owned by certain Australian and foreign government agencies. An example of quasi-ownership is where you have a Crown lease and have attached plant to that land after you acquired the lease.

Quasi-ownership also applies to plant which you have leased to a lessee and which has become a fixture on land that you do not own, provided certain conditions are met.

If there is a quasi-owner, only the quasi-owner can claim depreciation. If you are not sure whether you are the owner of the plant, contact your professional tax adviser or ring the ATO.

Luxury cars leased after 20 August 1996

Lessees of luxury cars, either new or second hand, which cost more than the depreciation cost limits given in the table on page 3 ($55 134 for the current income year) are subject to luxury car leasing rules. These rules apply to leases entered into after 20 August 1996, other than for short-term hiring agreements or for cars that are trading stock of the lessee.

Under these rules the lessee is treated as the owner of the luxury car. The actual lease payments made by the lessee are no longer allowable deductions. The lease payments are divided into their underlying capital component and their finance charge component. The lessee can then claim:

- the finance charge component reduced to reflect non-business use and
- depreciation based on the luxury car depreciation limit reduced to reflect non-business use.

Adjustments to cost for depreciation purposes

The calculation of depreciation is generally based on the cost of the plant to you. Cost includes:

- the original purchase price or construction cost
- transport costs
- installation costs
- customs duty
- relocation costs.

The cost for depreciation purposes may differ from the cost to you of the item of plant. The cost to you may be altered to arrive at a cost for depreciation in a number of circumstances. This occurs where:

- the cost of the car exceeds the depreciation cost limit for certain motor vehicles
- a car is acquired at a discount and plant (including a car) is traded in on the purchase of the car and the pre-discount price exceeds the car depreciation limit
- the plant is a car that is or has been affected by the luxury car lease provisions
- an inflated price is paid for the plant under a non-arm's length transaction
- a lessor who is treated as a quasi-owner acquires plant under a sale and lease-back arrangement
- part of the plant's cost is deductible under a provision other than the depreciation provisions
- another taxpayer has previously claimed depreciation deductions for the plant, in particular where the plant is acquired from an associate
- the plant is acquired by roll-over and
- trading stock becomes plant.

If you acquire an item of plant either wholly or partly for a creditable purpose, the amount of the GST input credits allowable on that acquisition is excluded when calculating the cost for depreciation purposes.

Where plant is acquired by way of inheritance, gift or prize, its cost for depreciation purposes is its depreciated value immediately before the date of acquisition. See *Taxation Ruling IT 2308—Income tax: depreciation of plant acquired otherwise than by purchase.*

In addition, measures contained in Division 58 of ITAA 97 affect the way in which depreciation deductions and balancing adjustments are calculated in respect of depreciable plant previously owned by a tax exempt entity which enters the tax net on or after 4 August 1997 by way of:

- an entity sale—plant continues to be owned by the exempt entity that becomes taxable or
- an asset sale—plant is acquired by a taxable purchaser from a tax exempt entity in connection with the acquisition of a business.

If you are not sure of the cost of an item of plant for depreciation purposes, contact your professional tax adviser or ring the ATO.

Depreciation cost limit for certain motor vehicles

Motor cars and station wagons, including four-wheel drive versions, are subject to a depreciation cost limit. This means you cannot depreciate any part of the cost of such a vehicle that is more than the limit for the year in which you first used it.

Depreciation cost limits for the last 6 years

1995–96	$52 912	1998–99	$55 134
1996–97	$55 134	1999–2000	$55 134
1997–98	$55 134	2000–01	$55 134

Plant previously used only for private purposes

If you use an item of plant for private purposes before you first use it for income-producing purposes—motor vehicles are a common example—you would work out depreciation from the time you first use the plant for private purposes. However, you could claim deductions only for the years you use it to produce assessable income.

If you use the diminishing value method, deductions in the first year of income-producing use would be based on the plant's undeducted cost at that time.

If you use the prime cost method, you can claim deductions based only on the plant's cost.

Plant owned for only part of a year

When you acquire a depreciable item of plant, you can depreciate it only for the part of the year that you owned it. For example, if you purchased an item 3 months before the end of an income year, you would be entitled to 25 per cent of a full year's deduction for depreciation.

If your plant was sold, lost or destroyed during an income year, you are allowed a partial depreciation deduction for the time in that year that you owned the plant. Refer to page 10 to find out what happens if you no longer own an item of plant.

Purchase of a second-hand item of plant

You can generally claim depreciation based on the cost of the item to you. However, as indicated on page 2 in the section **Adjustments to cost for depreciation purposes**, the Commissioner may limit this cost for working out depreciation having regard to certain matters—for example, whether the seller and purchaser are associated parties and the market value of the plant.

Depreciated items included in the sale of other property

If the depreciated item is included with the sale of other property—for example, real estate—and a separate value is not specified in the sale agreement, you can claim depreciation based on the part of the overall cost that can reasonably be attributed to the item. The ATO generally accepts independent valuations as a basis for this attribution. However, if there is no independent valuation, you may need to demonstrate that your estimate provided a reasonable value. Considerations would include the market value of the plant itself, compared to the total purchase price of the property.

Limited recourse debt terminations

Under proposed legislation contained in Taxation Law Amendment Bill (No. 5) 1999, when plant is acquired under a limited recourse debt arrangement—including hire purchase—which terminates after 27 February 1998 and part of the hire purchase or debt principal remains unpaid, an adjustment to assessable income may be required.

The adjustment is equal to the amount by which the total amount of the deductions allowed for the plant under the depreciation provisions exceeds the total amount of the deductions which would be allowable if based on actual outlays. If you are not sure how to work out your adjustment to assessable income contact your professional tax adviser or ring the ATO.

Commercial debt forgiveness

Generally, an amount which you owe is a commercial debt if you can claim a deduction for the interest paid on the debt or you would have been able to claim a deduction for interest if it had been charged. The amount of the commercial debt includes any unpaid interest.

If your commercial debts are forgiven, you may choose or be required to reduce the base amount used in working out depreciation on an item of plant you acquired before the year of income in which your commercial debts were forgiven. The amount used to reduce the base amount is taken to be an amount you have deducted for depreciation of the plant as at the first day of the same income year in which your debts were forgiven.

If you use the prime cost method, the base amount—that is, the cost—is reduced by the amount forgiven before you work out depreciation for the year in which the debt is forgiven.

If you use the diminishing value method, the undeducted cost of the plant at the start of the year in which the debt is forgiven is reduced by the amount forgiven before you work out depreciation for that year.

How are depreciation deductions calculated?

Before 21 September 1999, depreciation deductions were calculated by applying a 'depreciation rate' fixed by reference to the effective life of an item of plant to either the cost or opening undeducted cost of that plant. After 21 September 1999, the legislation with the exception of small business taxpayers and certain specific items does not provide for a 'depreciation rate' as such, rather deductions are calculated using a statutory formula. However, effective life remains part of the formula for both the diminishing value method and the prime cost method.

Depreciation calculation for plant acquired after 11.45 a.m. on 21 September 1999

For all plant (including motor vehicles) acquired after 11.45 a.m. [by legal time in the Australian Capital Territory (ACT)] on 21 September 1999 the depreciation deduction rate is determined solely by reference to effective life as determined by the taxpayer or by the Commissioner. However, this does not apply to small business taxpayers who satisfy certain qualifying conditions (see Small business taxpayers on page 15)—these taxpayers can still use the accelerated rates of depreciation.

There are two methods of calculating depreciation:

- the **diminishing value method** and
- the **prime cost method**.

You choose the method of calculating depreciation in the first year that you are allowed a depreciation deduction. Once you have chosen a method you cannot change to the other method for that item. However, you can recalculate the effective life component contained in the method you are using.

Under the **diminishing value method** the deduction is calculated as a percentage of the balance you have left to deduct. The formula for calculating depreciation using the diminishing value method is:

$$\text{Opening undeducted cost} \times \frac{\text{days owned}}{365} \times \frac{150\%}{\text{plant's effective life (in years)}}$$

Under the **prime cost method** the deduction for each year is calculated as a percentage of the cost. The formula for determining the amount of depreciation deduction under the prime cost method is:

$$\text{Cost} \times \frac{\text{days owned}}{365} \times \frac{100\%}{\text{plant's effective life (in years)}}$$

Example—diminishing value method

The cost of an item of plant purchased on 1 July 2000 is $1000. It has an effective life of 5 years and it is owned for the full year for producing assessable income. The depreciation deduction will be $300 calculated as follows:

$$1000 \times \frac{365}{365} \times \frac{150\%}{5}$$

Example—prime cost method

Assume that the same facts apply as for the previous example. The depreciation deduction is $200 calculated as follows:

$$1000 \times \frac{365}{365} \times \frac{100\%}{5}$$

Removal of accelerated depreciation

Accelerated depreciation allowed the full cost of an item of plant to be claimed well before the end of its effective life. Until 11.45 a.m. (by legal time in the ACT) on 21 September 1999, actual rates for depreciation were set. These rates were based on effective life with a 20 per cent loading which were then broadbanded into one of 6 common rates. The loading together with the broadbanding produced accelerated rates of deductions for depreciation.

Apart from certain small business taxpayers accelerated depreciation is no longer available for plant if:

- you acquired it under a contract entered into after 11.45 a.m. (by legal time in the ACT) on 21 September 1999
- you constructed it and the construction started after that time or
- you acquired it in some other way after that time.

Depreciation, including the use of the diminishing value method, is still able to be claimed. However, the amount is calculated differently depending on whether you are a small business taxpayer and when you acquired the plant.

Depreciation calculation for plant acquired before 11.45 a.m. on 21 September 1999 or by certain small business taxpayers

Accelerated rates of depreciation are still available for plant acquired or whose construction commenced at or before 11.45 a.m. (by legal time in the ACT) on 21 September 1999. Accelerated rates of depreciation are also available to small business taxpayers who satisfy certain conditions (see **Small business taxpayers** on page 15).

The accelerated rate to be used is determined by choosing the appropriate rate that corresponds to the effective life of the item of plant. The following tables show the appropriate rates.

For most general items of plant the rates are as follows:

	Annual depreciation percentage	
Effective life in years	*Prime cost rate*	*Diminishing value rate*
Less than 3	100	100
3 to less than 5	40	60
5 to less than $6^2/_3$	27	40
$6^2/_3$ to less than 10	20	30
10 to less than 13	17	25
13 to less than 30	13	20
30 and over	7	10

For most motor vehicles the following rates apply:

	Annual depreciation percentage	
Effective life in years	*Prime cost rate*	*Diminishing value rate*
Less than 3	100	100
3 to less than 5	33	50
5 to less than $6^2/_3$	20	30
$6^2/_3$ to less than 10	15	22.5
10 to less than 13	10	15
13 to less than 20	8	11.25
20 to less than 40	5	7.5
40 and over	3	3.75

The ATO has published a list of standard effective lives for various items of plant. Where an item's effective life is different from the one published by the ATO taxpayers may make their own estimate.

There are two methods of calculating depreciation:

- the **prime cost method** and
- the **diminishing value method**.

You choose the method of calculating depreciation in the first year that you are allowed a depreciation deduction. Once you have chosen a method you cannot change to the other method for that item.

Under the **prime cost method** the deduction for each year is calculated as a percentage of the cost. The formula for calculating depreciation using the prime cost method is:

$$\frac{\text{Cost x days owned}}{365} \times \text{Prime cost rate}$$

Under the **diminishing value method** the deduction is calculated by applying the diminishing value rate of depreciation from the table in the previous column to the balance you have left to deduct. The formula for calculating depreciation using the diminishing value method is:

$$\frac{\text{Opening undeducted cost x days owned}}{365} \times \text{Diminishing value rate}$$

It uses a rate generally equal to one-and-a-half times the prime cost depreciation rate for that item. The deduction in the first year is equal to the depreciation rate for that item multiplied by its initial cost. In subsequent years, the rate is applied to the amount remaining after deducting the depreciation claimed in all previous years from the initial cost.

Example—prime cost method

An item of plant costing $1000 with an effective life of 9 years would have a prime cost rate of depreciation of 20 per cent. This would mean a claim of 20 per cent of $1000 or $200 each year for 5 years. The accelerated depreciation rate is determined by choosing the appropriate rate from the table in the previous column that corresponds to the effective life of the item. Taking account of the days owned as a fraction of the year produces a proportionate deduction where the plant has been owned or installed ready for use for less than the full year.

Example—diminishing value method

If the cost of an item of plant is $1000 and the prime cost rate of depreciation is 20 per cent, then the depreciation by the diminishing value method will, in the first year, be 30 per cent of $1000, or $300. The value for depreciation in the next year will be $700, and the depreciation claim will therefore be 30 per cent of $700 or $210 and so on.

Depreciation of plant acquired at or before 11.45 a.m. on 21 September 1999 but first used or installed ready for use after that date

Accelerated rates of depreciation apply to all plant acquired at or before 11.45 a.m. (by legal time in the ACT) on 21 September 1999 even if it is first used or installed ready for use after that date. The accelerated rate is determined by choosing the appropriate rate from the published table that corresponds to the effective life of the plant. The effective life of the plant is determined at the time that it is first used or installed ready for use.

Special depreciation rates for certain items of plant acquired before 11.45 a.m. on 21 September 1999 or by certain small business taxpayers

Employees' amenities

A special minimum rate of 33 per cent prime cost or 50 per cent diminishing value apply to employees' amenities.

Employees' amenities means property used mainly to provide clothing cupboards, first aid, rest rooms, recreational facilities, cafeteria and the like for employees or for the care of the children of employees.

Works of art

Works of art that are originals or reproductions are items of plant—for example, paintings, sculptures, drawings, engravings and photographs.

Diminishing value depreciation rates for these items are worked out by dividing 1.8 by the effective life and multiplying your answer by 100. The prime cost rate is two-thirds of that rate, rounded to the nearest whole number. For example, a painting with an effective life of 100 years would have a diminishing value rate of 1.8 per cent and a prime cost rate of 1.2 per cent. However, the prime cost rate for an artwork with an effective life of fewer than 3 years is 100 per cent—that is, you can deduct the full cost immediately.

Plant used partially for producing income

You may use a depreciable item of plant for more than one purpose. For instance, you may use a computer partially for business and partially for private purposes. In this case, you are allowed only a partial depreciation deduction, based on the percentage for business use.

Working out your deductions

If you are using the diminishing value method to work out depreciation deductions for an item of plant used partially for producing income, first work out depreciation in the usual manner by applying the depreciation rate to the opening undeducted cost.

The depreciation deduction you are allowed is the depreciation reduced by the percentage of non-income-producing use.

Although you are not allowed a deduction for the percentage of non-income-producing use of the plant, work out the undeducted cost as if there had not been any such use. The examples on pages 11, 12 and 13 show you how to work out undeducted costs.

If you are using the prime cost method, the depreciation deduction allowable is the deduction worked out in the usual way, reduced by the percentage of non-income-producing use of the plant. You are not allowed any further deductions once the undeducted cost of the plant reaches zero.

Can you change methods?

No. Once you adopt one method of depreciation for a particular item, you cannot change to the other method for that item. For example, if you choose the prime cost method for all or some items becoming depreciable in a particular year, you must continue with that method for those items for as long as you own them. If you purchase similar items in later years, you must still choose which method of depreciation to apply to those items. An exception to this rule is when you have chosen the prime cost method and later decide to allocate the item to a common-rate pool. The diminishing value method is the only method allowed for calculating depreciation deductions for items allocated to a common-rate pool. Information on page 8 tells you about common-rate pools.

Effective life

The effective life of plant is the period it can be used by any entity for income-producing purposes based on your expected use and assuming it is maintained in reasonably good order and condition.

Determining effective life

You can either make your own estimate of the effective life of the plant or adopt the effective life determined by the Commissioner. *Taxation Ruling IT 2685—Income tax: depreciation* and its attachments list the effective life of various items of plant as determined by the Commissioner. IT 2685 was issued on 11 June 1992 and remained in force until it was replaced by *Taxation Ruling TR 2000/18—Income tax: depreciation effective life* which came into force on 1 January 2001. To find out how to get these rulings, see the inside front cover.

If you were entitled to deduct an amount of depreciation for plant based on the effective life specified in IT 2685, you continue to use that effective life as the basis for your deduction otherwise you use the effective life contained in TR 2000/18.

Further clarification about which Commissioner's effective life you should use is proposed in the exposure draft on the New Business Tax System (Capital Allowances) Bill 2000. This exposure draft proposes that for plant acquired after 21 September 1999 you can use the effective life contained in the particular ruling that was in force at the relevant time, provided you start to use it or have it installed ready for use within three years of the relevant time. The relevant time is the time:

- you entered into the contract to acquire it
- you started to construct it or
- you otherwise acquired it.

If you do not start to use the plant or have it installed ready for use within the required three-year period, then the ruling that will apply is the one that is in force at the date you first use it or have it installed ready for use.

However, where the plant was acquired under a contract or otherwise acquired or construction of it commenced before 21 September 1999, the appropriate ruling to be applied is that which was in force at that time. There is no restriction on the period within which this plant must be used.

Making your own estimate of effective life

If you decide to make your own estimate of effective life, you need to take into account:

- how long you expect the plant to be used irrespective of who uses it
- how you expect to use it and
- whether you would be likely to scrap it before the end of its useful life.

The sort of information which you could use to make an estimate includes:

- manufacturer's specifications
- independent engineering information
- your own past experience with similar items of plant
- the past experience of other users of similar items
- the level of repairs and maintenance commonly adopted by users of the plant
- retention periods
- scrapping or abandonment practices and
- the physical life of the item of plant.

Changing your estimate of effective life

You can change the effective life for an item of plant unless you are a small business taxpayer using accelerated depreciation rates. The change can be made whether you worked out the previous effective life yourself or adopted the effective life determined by the Commissioner. You can choose to work out a new effective life of plant if:

- there are changed circumstances that make an earlier estimate no longer accurate and
- either:
  - you became the owner of the plant under a contract entered into after 11.45 a.m. (by legal time in the ACT) on 21 September 1999 or
  - you constructed the plant and the construction started after that time or
  - you acquired the plant in some other way after that time.

Changed circumstances that result in working out a new effective life

Some examples of circumstances that would make an earlier estimate of effective life no longer accurate are:

- your use of the plant turns out to be more or less rigorous than you expected or was anticipated by the Commissioner's determination
- there is a downturn in the demand for the goods or services that the plant is being used to produce that will result in the plant being scrapped
- government legislation prevents the plant's continued use
- changes in technology make the plant redundant.

Effect of making a new estimate of effective life

The new estimate is used in the formula for calculating your depreciation deduction for the income year for which you make the estimate.

If you are re-estimating the effective life of an item of plant and you are using the prime cost method, you use the plant's undeducted cost as at the start of the income year for which you made the choice as its cost in the formula.

Immediate deduction for plant costing $300 or less or with an effective life of less than 3 years

Plant costing $300 or less acquired after 1 July 2000

The situation at the time of publication of this book is that for all taxpayers other than small business taxpayers, the immediate deduction for plant costing $300 or less has been repealed and replaced with an option to depreciate plant through a low-value pool.

However, the New Business Tax System (Capital Allowances) Bill 2000 Exposure Draft contains a proposal to reinstate the immediate write-off for plant costing $300 or less for certain taxpayers who use the plant predominantly to produce assessable income that is not derived from carrying on a business in the 2001 income year.

The immediate deduction will be available to the owners and quasi-owners of plant who are either small business taxpayers or other taxpayers who satisfy all of the following requirements:

- the plant is used predominantly for the purpose of producing assessable income that is not derived from carrying on a business
- the plant is not part of a set of items acquired in the same year and costing more than $300 in total and
- the plant is not one of a number of identical or substantially identical items acquired in the same year and costing more than $300 in total.

Plant with an effective life of less than 3 years

Except for small business taxpayers with access to accelerated rates of depreciation, the immediate deduction for plant with an effective life of less than 3 years is no longer available if:

- you became its owner or quasi-owner under a contract entered into after 11.45 a.m. (by legal time in the ACT) on 21 September 1999 or
- you constructed it and the construction started after this time or
- you acquired it in some other way after this time.

The calculation of the depreciation deduction for these items of plant is based solely on the effective life of the plant.

Pooling

Common-rate pools

Since 1991–92, taxpayers have had the option of combining items of plant that have the same depreciation rates so that they can make a single calculation of deductions. This is known as common-rate pooling and the following rules apply:

- Depreciation deductions for pooled items are worked out using the diminishing value method only.
- Plant depreciated at certain special prime cost rates cannot be pooled—for example, plant being depreciated under one of the repealed 5 year or 3 year concessions cannot be pooled as they were prime cost systems only.
- Plant acquired part way through an income year cannot be pooled until the beginning of the next year.
- Items of plant can be pooled regardless of when they were acquired or whether they were previously depreciated under the prime cost method.
- Items of plant can be pooled only if they are used exclusively for income-producing or business purposes
- When items are pooled, their balance of undeducted costs is simply added to the opening balance of the pool at the beginning of the year.
- An item of plant can be taken out of a pool by deducting its reconstructed undeducted cost at the start of the year from the opening balance of the pool—the reconstructed undeducted cost is the amount that would have been the undeducted cost of the item if it had never been pooled.
- Depreciation deductions for items taken out of a pool can be worked out only by using the diminishing value method, even if the prime cost method was used before the item was placed into the pool.

On the disposal of a pooled item of plant, the following options are available:

- Take the item out of the pool as described above, and treat the difference between any termination value and the undeducted cost or written down value in the usual manner. This treatment will depend on whether the disposal was before or after 11.45 a.m. on 21 September 1999—see pages 10, 11 and 12.
- Leave the undeducted value of the item in the pool and either treat the lesser of the item's termination value and its cost as assessable income or use that amount in one or more of the alternative treatments explained on pages 10, 11 and 12.

Low-value pools

From 1 July 2000, an optional low-value pooling arrangement for plant has been introduced. It will apply to plant costing less than $1000 or having an undeducted cost of less than $1000 at the start of the income year provided it has been depreciated using the diminishing value method. From 1 July 2000, such low-value plant can be allocated to a low-value pool and depreciated at statutory rates as a single item of plant.

However, this does not apply to taxpayers who qualify as small business taxpayers for capital allowances purposes. Small business taxpayers can continue to claim an immediate deduction for items of plant costing $300 or less.

Taxpayers who can choose low-value pooling

All taxpayers (including partnerships and individuals who are not carrying on a business) who acquire or hold eligible plant on or after 1 July 2000 can choose to use low-value pooling. Small business taxpayers cannot choose to use low-value pooling.

Plant that can be allocated to a low-value pool

Two classes of depreciable plant can be allocated to a low-value pool from 1 July 2000:

- low-cost plant—individual items of plant you acquired on or after 1 July 2000 that cost less than $1000 and
- low undeducted-cost plant—items of plant you held in the previous year of income that you have already (or could have) depreciated using the diminishing value method to an undeducted cost of less than $1000.

Plant that cannot be allocated to a low-value pool

The following plant cannot be allocated to a low-value pool:

- plant that costs $300 or less which you acquired before 1 July 2000 (you are entitled to an immediate deduction for such plant if you used it solely for income-producing purposes)
- plant with an undeducted cost of less than $1000 which has been depreciated using the prime cost method
- plant that has already been allocated to a common-rate pool
- software
- in addition, the New Business Tax System (Capital Allowances) Bill 2000 Exposure Draft contains a proposal to reinstate the immediate write-off for plant costing $300 or less for certain taxpayers who use the plant predominantly to produce assessable income that is not derived from carrying on a business in the 2001 income year. Plant covered by this proposal will not be able to be allocated to a low-value pool.

Method of depreciation

The low-value pool is depreciated using the diminishing value method. Items of plant in the pool have an effective life of 4 years. The pool is depreciated using 2 statutory depreciation rates.

Rates of depreciation

There are 2 statutory depreciation rates that must be used together to calculate the total depreciation deduction for the low-value pool in a year of income. In a year of income, you must calculate your depreciation deduction for a low-value pool using the following 2 statutory rates:

- for low-cost plant that has been allocated to the pool for the first time in that income year—18.75 per cent (which is 50 per cent of the pool depreciation rate) of the total cost of that plant allocated, regardless of when during that year the item(s) was actually acquired. This eliminates the need to calculate a pro-rata depreciation deduction for each item of plant, based on the actual date it was pooled. It is consistent with the simplification aim of the low-value pooling measure and
- for all other plant in the pool (that is, plant that has been allocated to the pool in a previous year and low undeducted-cost plant allocated to the pool in the year of income)—37.5 per cent of the sum of:
  – the pool closing balance from the previous year and
  – the total undeducted cost of any low undeducted-cost plant allocated to the pool in the year of income.

Plant that must be allocated once a low-value pool is created

Once you choose to create a low-value pool and an item of low-cost plant is allocated to the pool, all other low-cost plant acquired in that year and later years must be allocated to the low-value pool.

Additionally, once you allocate an item of low-cost plant to the low-value pool, it must remain in the pool. This means the initial choice to use the low-value pooling arrangement for low-cost plant is a once-and-for-all choice.

Allocating items to the low-value pool

The low-value pool is created in the year in which you first choose to allocate an item of plant to it. The low-value pool then contains all items that you allocate to it, regardless of the year in which they were first allocated.

Items of low-cost plant and/or low undeducted-cost plant are allocated to the same low-value pool simply by recording the income year in which they are first allocated. They must then be depreciated at a statutory rate as if the pool were a single item of plant. There is no requirement to record the low-value pool depreciation percentage as the rate for low-value pooled plant is set by law. This is in contrast to the existing 'common-rate' depreciation pooling rules.

Plant that has previously been depreciated under the prime cost method

Plant that has previously been depreciated to an undeducted cost of less than $1000 using the prime cost method is not eligible to be allocated to a low-value pool. You will still have to continue to depreciate these items of plant under the prime cost method.

Plant used partly for non-income-producing purposes

When you first allocate an item of plant to the pool, you need to make and record a reasonable estimate of the percentage of any proposed non-income-producing use. The cost or undeducted cost of the plant that you allocate to the pool is reduced by that percentage of non-income-producing use.

The cost or undeducted cost of plant (whichever is relevant) must be less than $1000 for it to be allocated to a low-value pool, irrespective of the estimated percentage of non-income-producing use.

Once you have allocated the plant to the pool, you cannot vary your estimate of non-income-producing use if it changes in a later year.

Disposal of an item of plant from a low-value pool

If an item of plant from a low-value pool is disposed of (sold, lost, scrapped or destroyed) in a year of income, the pool closing balance for that year is reduced by the disposal proceeds (if any) of that plant. However, you do not include in the disposal proceeds the percentage that you estimated the plant would be used for non-income-producing purposes.

Disposal proceeds exceed the pool closing balance

Where you dispose of items of plant from a low-value pool and the disposal proceeds exceed the pool closing balance the excess must be included in your assessable income.

Capital gains tax (CGT) and low-value pooling

Items of plant allocated to a low-value pool are excluded from the CGT regime.

Record keeping requirements

You must record in writing the first income year in which you choose to allocate plant to a low-value pool. This initial choice to use low-value pooling creates the low-value pool. Items of plant are allocated to the low-value pool by recording in writing the income year in which they are allocated to the pool.

You must also make an estimate of the percentage (if any) of non-income-producing use of an item of plant when you allocate it to the pool.

Items will only need to be identified as low-value pooled plant at the time of disposal—details such as date or value at time of purchase will not be required.

What happens if you no longer own an item of plant

There have been a number of changes to the depreciation provisions that apply to the disposal of plant under business tax reform. These changes take effect under the *New Business Tax System (Capital Allowances) Act 1999* which received Royal Assent on 10 December 1999.

Under the changes, any capital gain or capital loss arising from disposal of an item of plant after 11.45 a.m. (by legal time in the ACT) on 21 September 1999 is disregarded. The gain or loss resulting from the disposal is treated as a further balancing adjustment and is either included in assessable income or allowed as a deduction.

If an item of plant is disposed of after 11.45 a.m. on 21 September 1999 for more than its cost, the amounts that would be included in assessable income are:

- the balancing adjustment and
- the further balancing adjustment.

If you dispose of an item of plant at or before 11.45 a.m. on 21 September 1999, then you only include the balancing adjustment in your assessable income and the rest is a capital gain (if the capital proceeds are greater than the cost base or indexed cost base).

Assessable balancing adjustment

An assessable balancing adjustment arises where the termination value (see page 1) of the plant exceeds the written down value of the plant disposed of. The balancing adjustment represents the amount of depreciation that has been claimed or could have been claimed upon disposal of the plant.

Further balancing adjustment

The further balancing adjustment arises where the termination value of the item of plant exceeds its cost.

The following rules apply to calculate the further balancing adjustment if you dispose of an item of plant after 11.45 a.m. (by legal time in the ACT) on 21 September 1999:

- if you acquired the plant on or before that time, the further balancing adjustment equals the termination value of the item of plant minus its cost base or indexed cost base
- if you acquired the plant after that time, the further balancing adjustment equals the termination value of the item of plant minus its cost.

Plant acquired and disposed of after 11.45 a.m. on 21 September 1999

When plant is acquired and disposed of after 11.45 a.m. (by legal time in the ACT) on 21 September 1999, the further balancing adjustment is the difference between the termination value (usually the sale proceeds) of the plant and its written down value plus the balancing adjustment amount.

Plant acquired before 11.45 a.m. on 21 September 1999 but disposed of after this time

For plant disposed of after 11.45 a.m. (by legal time in the ACT) on 21 September 1999 but acquired before this time, the further balancing adjustment is the difference between the termination value and the cost base of the plant indexed up to 30 September 1999. The purpose of this is to:

- take into account expenditure other than the cost of the plant and
- preserve the benefit of indexation on items of plant that have been owned for at least 12 months before disposal.

The cost base and the indexed cost base are to be calculated in accordance with the CGT provisions.

Termination value is less than undeducted cost

You can claim a deduction if you dispose of an item of plant for less than its undeducted cost. A deductible balancing adjustment arises where the termination value of an item of plant (that is, usually its sale price) is less than its undeducted cost. The difference is deductible in the year of disposal if the plant is being used solely for income-producing purposes.

Undeducted cost is less than reduced cost base

If you dispose of an item of plant after 11.45 a.m. (by legal time in the ACT) on 21 September 1999, you may be able to claim a further deduction. Where the undeducted cost of the item of plant is also less than its reduced cost base (as calculated under the CGT regime), you can claim a further deduction for the difference. This further deduction will not be reduced even if you have used the plant for any non-income-producing use.

Disposal of plant where no depreciation claimed or plant is incomplete

Subdivision 42–GA of ITAA 1997 ensures that the further balancing adjustment provisions apply to plant where no depreciation has been claimed or where there is an incomplete unit of plant. In these situations, the further balancing adjustment will include as income or allow as deduction those amounts that would have been a capital gain or capital loss under the CGT provisions.

The further balancing adjustment calculation could arise in the following circumstances:

- where an item of plant is completed and disposed of before it is used in your income-producing process
- where an item of plant is destroyed before its completion or you disposed of it before its completion.

The further balancing adjustment calculation must be made in the year in which the balancing adjustment event occurs. If you are not sure of the balancing adjustment calculation, contact your professional tax adviser or ring the ATO.

The purpose of this is to take into account expenditure other than the cost of the plant and to preserve the benefit of indexation on items of plant that have been owned for at least 12 months before this time.

Plant excluded from the further balancing adjustment provisions

The further adjustment provisions do not apply to the following:

- cars that are designed to carry a load of less than one tonne and less than 9 passengers
- motor cycles
- valour decorations
- collectables acquired for $500 or less
- personal use assets acquired for $10 000 or less
- plant used to produce exempt income
- plant acquired before 20 September 1985.

Balancing adjustments for plant partly used for business

Where you are using an item of plant for both income-producing and non-income-producing purposes, the difference between the undeducted cost and the termination value will be reduced to reflect any non-income-producing use of that item of plant.

You must compare the termination value on the sale, loss or destruction of an item of plant—including insurance proceeds—with both the undeducted cost of the item and its written down value. The written down value of an item is the cost of that item less the total depreciation deductions actually allowed.

The following example shows you how to work out written down values.

Example

Working out adjustments on the sale of an item of plant only partly used for business

Elizabeth acquired an item costing $1000 on 1 July 1999. She used it for both business and private purposes equally for 2 years. She sold the item on 30 June 2001.

Elizabeth adopted the prime cost method to work out the depreciation. The relevant prime cost rate is 27 per cent. She would work out undeducted cost and written down value as follows:

	Undeducted cost $	→	*Business use* 50%	→	*Written down value* $
1.7.99 Opening balance	1000				1000
Depreciation at 27%	270				135
30.6.2000 Closing balance	730				865
1.7.2000 Opening balance	730				865
Depreciation at 27%	270				135
30.6.2001 Closing balance	460				730

Assessable adjustments

If the termination value on disposal is more than the written down value, you must include the difference in your assessable income. In the first instance the assessable amount cannot be more than the sum of deductions actually allowed for depreciation on the item. However, if you sell an item of plant after 21 September 1999, there may be a further assessable amount if the termination value is more than the cost of the item.

Example

Assessable adjustment

If Elizabeth sold the item for $800, she would recover $70—the amount by which the termination value is more than the written down value of $730. The amount of $70 is treated as assessable income.

No adjustments

Where the termination value is between the written down value and undeducted cost, no adjustment is required.

Example

No adjustment

If Elizabeth sold the item for $700, there would be no adjustment because the termination value is less than the written down value of $730 but greater than the undeducted cost of $460.

Deductible adjustments

Where the termination value is less than both the written down value and undeducted cost, the difference between the termination value and the undeducted cost represents a deduction. However, you are eligible for a deduction only for the percentage of business or other income-producing use of that item of plant. If you sell an item after 21 September 1999, you will be eligible for a further deduction if the undeducted cost is also less than the reduced cost base. You do not reduce this further deduction to reflect any non-income-producing use of that item.

Example

Deductible adjustment

If Elizabeth sold the item for $400, she could claim a deduction for $30—that is, 50 per cent of the amount by which the undeducted cost of $460 exceeds the termination value.

Special balancing adjustment rules for cars

If your car has been disposed of, lost or destroyed you may need to work out a balancing adjustment. The following examples show you how to do this. Use this method of working out your balancing adjustment if you use the one-third of actual expenses method or the logbook method of claiming car expenses. If you use the cents per kilometre method or the 12 per cent of original value method of claiming car expenses, you will not have to work out a balancing adjustment because those methods do not result in depreciation deductions. If you switch between these methods you may have to follow special rules to work out your balancing adjustment.

Where a car subject to the depreciation cost limit described on page 3 is disposed of, lost or destroyed, the termination value is adjusted. It is reduced to an amount determined by multiplying the termination value by the fraction calculated when you divide the depreciation limit for that car by the original cost of the car.

The calculation of balancing adjustments for cars is not affected by the depreciation changes that applied from 11.45 a.m. on 21 September 1999.

Example

Where you switch between the one-third of actual expenses method and the logbook method

Dennis acquired a car on 1 July 1997 for $20 000. He elected to use the prime cost method (PC) to work out the depreciation on his car. During 1997–98 and 1998–99, Dennis used the one-third of actual expenses method to work out the deduction for his car expenses. In 1999–2000, he switched to the logbook method. His logbook showed that Dennis used the car for business purposes for 40 per cent of the time.

On 1 July 2000—that is, in the 2000–01 income year—Dennis disposed of the car for $15 000. He worked out the car's undeducted cost and written down value—one-third of the notional amount for the first 2 years then 40 per cent for the third year—as follows:

	Undeducted cost *$*		*Written down value* *$*
Cost of car	20 000		20 000
Depreciation for 1997–98 ($20 000 x 15% PC)	3 000	→ 1/3 →	1 000
	17 000		19 000
Depreciation for 1998–99 ($20 000 x 15% PC)	3 000	→ 1/3 →	1 000
Depreciation for 1999–2000 ($20 000 x 15% PC)	3 000	→ 40% →	1 200
Closing balance	11 000		16 800

The balancing adjustment in this example is nil, as the termination value of the car falls between the written down value of $16 800 and the undeducted cost of $11 000.

If Dennis had sold the car for more than the written down value —say for $19 000—he would have to include in his assessable income the difference between $19 000 and the written down value of $16 800—that is, $2200.

If he had sold the car for less than the undeducted cost—say for $10 000—he would be allowed a deduction of $356 [($11 000 – $10 000) x ($3200 ÷ $9000)], where $3200 is the sum of all actual depreciation ($1000 + $1000 + $1200) and $9000 is the sum of all notional depreciation ($3000 + $3000 + $3000).

Example

Where you use only the one-third of actual expenses method or the logbook method

Louise acquired a car on 1 July 1998 for $26 000. She elected to use the diminishing value method (DV) to work out the depreciation on her car. During both 1998–99 and 1999–2000, Louise used the one-third of actual expenses method to work out the deduction for her car expenses.

On I July 2000—that is, in the 2000–01 year—Louise disposed of the car for $24 500. She worked out the car's undeducted cost and the written down value—one-third of the notional amount—as follows:

	Undeducted cost $		*Written down value* $
Cost of car	26 000		26 000
Depreciation for 1998–99 ($26 000 x 22.5% DV)	5 850	→ 1/3 →	1 950
	20 150		24 050
Depreciation for 1999–2000 ($20 150 x 22.5% DV)	4 534	→ 1/3 →	1 511
Closing balance	15 616		22 539

The balancing adjustment in this example is $1961 ($24 500 – $22 539). Louise must include the amount of $1961 in her assessable income.

If Louise had sold her car for an amount between the written down value and undeducted cost—say for $19 000—there would be no balancing adjustment.

If she had sold the car for less than the undeducted cost—say for $15 016—she would be allowed a deduction of $200 [($15 616 – $15 016) x ($3461 ÷ $10 384)], where $3461 is the sum of all actual depreciation ($1950 + $1511) and $10 384 is the sum of all notional depreciation ($5850 + $4534).

If you use either the one-third of actual expenses method or the logbook method for one period after you begin using the car and for another period you use either the cents per kilometre method or the 12 per cent of original value method, you have to reduce your balancing adjustment to reflect the extent to which you used each method. This is only expected to occur in a limited number of cases. If you are affected and you are unsure of how to work out your balancing adjustment, contact your professional tax adviser or ring the ATO.

Balancing adjustment offsets

Balancing adjustment offset for plant disposed of at or before 11.45 a.m. on 21 September 1999

Where you dispose of depreciable plant at or before 11.45 a.m. (by legal time in the ACT) on 21 September 1999 for more than its depreciated value you can elect to offset any assessable balancing adjustment against:

- the cost of any replacement or other plant acquired or
- the written down value of other depreciated items of plant.

Balancing adjustment offset for plant disposed of after 11.45 a.m. on 21 September 1999

For disposal of plant after 11.45 a.m. (by legal time in the ACT) on 21 September 1999, taxpayers (other than small business taxpayers) will not be able to offset an assessable balancing adjustment against the cost or written down value of replacement or other plant unless the disposal was involuntary.

Balancing adjustment offset and small business taxpayers

The balancing adjustment offset will continue to be available to small business taxpayers until the commencement of the Simplified Tax System which is expected to come into operation on 1 July 2001.

Balancing adjustment offset for involuntary disposals

An involuntary disposal arises where plant is lost or destroyed or an Australian government agency acquires the item of plant compulsorily or by forced negotiation after 11.45 a.m. (by legal time in the ACT) on 21 September 1999.

When an item of plant is subject to involuntary disposal, the assessable balancing adjustment can be offset against the cost of replacement plant. The replacement plant must be acquired no earlier than one year before the time of disposal of the plant and no later than one year after the end of the income year in which the disposal occurred. The Commissioner can agree to extend the time limit.

To offset the assessable balancing adjustment the replacement plant must be wholly used for income-producing purposes.

Computer software

After 10 a.m. (by legal time in the ACT) on 11 May 1998, expenditure you incur on software is to be depreciated, subject to certain modifications, under the depreciation provisions that apply to plant. Before that date expenditure on software, in accordance with *Taxation Ruling IT 26—Computers—depreciation, investment allowance*, was generally an allowable deduction in the year you incurred the expenditure, even though most software had a reasonably long life. The ruling was withdrawn on 11 May 1998.

In applying the depreciation provisions to software, the references to 'its cost to you' for plant are to be read as references to 'your expenditure on software'.

If you can claim software costs under the software depreciation provisions then you cannot deduct the costs under any other provision. There are, however, 3 exceptions to this.

- the provisions do not apply to expenditure on software if it is or is part of trading stock or
- you can get a more favourable deduction under another capital allowance provision—for example, under the mining exploration and prospecting provisions
- the provisions do not apply to manufacturers, distributors or developers of software whose principal purpose is to sell or license the software unless they are not able to obtain a deduction under any other provision or section.

Meaning of software

Software means a right, including a licence, to use software. Expenditure on software includes expenditure you incur on acquiring or developing software or in having another person develop software principally for you to use to perform the functions for which you acquired or developed the software.

Expenditure on software for depreciation purposes excludes expenditure that does not involve substantial improvements to the software. Under the software depreciation provisions, you cannot claim a deduction for expenditure on maintenance, testing, code reviews, minor alterations or modifications or remedying defects. Such expenditure is considered for deduction under the general deduction provisions.

Where you acquire software with or attached to other items of plant such as units of hardware and the software does not have a specific value, you can claim a deduction for expenditure that is reasonably attributable to the software.

Depreciation of software

The general depreciation provisions applying to plant are modified for expenditure on computer software. The modifications include the following:

- You must use the prime cost method for calculating the depreciation claim.
- The effective life of all software is $2^1/_2$ years and the depreciation rate is 40 per cent.
- Expenditure in relation to software projects is capitalised and depreciated from the time you use the software or install it ready for use.
- The low-cost limit of $300 continues to apply to units of software unless the total cost of that unit of software and any other substantially identical software acquired in the same income year exceeds $300.
- Information on pages 10, 11 and 12 explains what happens to plant which is sold, lost or destroyed. A deductible adjustment is also available for software where you permanently cease to use it and do not have it installed ready for use.
- If you have a right to use software, the deductible adjustment occurs if it is reasonable to expect that you will never obtain a subsequent right to use the underlying software. The termination value will generally be nil unless you receive consideration as a result of the termination.
- Software can be pooled but not under the pooling provisions that apply to general plant.
- You can claim an immediate deduction for the unrecouped expenditure on software (not in the software pool) that you will never use or install ready for use, to the extent that, when you incurred the expenditure, the software was to be used or installed ready for use to produce assessable income.

Pooling software

You can use the software pooling method only for expenditure you incur in developing software or having another person develop software for your own use and wholly to produce assessable income. Once you elect to use this method it will apply to all software development expenditure incurred in the income year for which you elected the pooling method and later years. You cannot revoke the election.

You cannot pool expenditure on low-cost software that can be claimed immediately.

Under the pooling method you cannot depreciate software in the year you incur the expenditure. You are allowed deductions at the rate of 40 per cent in each of the following 2 years and 20 per cent in the third year.

Software development expenditure on a project that is abandoned continues to be depreciated as part of the pool. There is no balancing adjustment.

You include in assessable income any consideration received for software for which expenditure has been pooled. Examples include consideration received for:

- disposal of software
- granting of a licence to use the software
- loss or destruction of software—insurance proceeds.

GST related expenditure

An immediate deduction for the cost of plant or software acquired or upgraded for the purpose of meeting existing or future obligations or rights under the GST law was available where you entered into a contract to do so during the period 1 July 1999 to 30 June 2000.

You must have also met the following conditions to be eligible for the deduction:

- became the owner of the plant or software before 1 July 2001
- used the plant or software for producing assessable income or had it installed ready for that use before 1 July 2001
- had a pre-GST annual turnover of $10 million or less
- incurred the expenditure to meet existing or future obligations or to exercise existing or future rights under the GST law and
- been registered under the GST Act immediately before 1 July 2000.

If you claimed the deduction but failed to meet the above conditions you will need to amend your tax return for the income year ended 30 June 2000 accordingly.

Submarine cables

This section outlines the indefeasible right to use (IRU) and submarine cable systems provisions contained in a *New Business Tax System (Capital Allowances) Act 1999*.

Under this legislation, depreciation deductions for the cost of an indefeasible right to use the capacity in an international telecommunications submarine cable system are allowable over the effective life of the submarine cable.

The granting of an IRU is treated as a disposal by the granter of an ownership interest and the grantee can deduct the cost as a depreciation allowance. As the IRU is treated as plant, the holder has the choice of using either the prime cost or diminishing value methods. The deduction commences when you first exercise the right to use the allocated capacity of the cable for income-producing purposes.

Small business taxpayers

The *Treasurer's Press Release No. 58, 21 September 1999* announced reforms to certain business tax concessions effective from the time of the announcement. These reforms included the end of accelerated depreciation and removal of the balancing charge offset.

However, a small business can generally retain accelerated rates of depreciation until the start of the proposed Simplified Tax System for small business on 1 July 2001, provided that the following conditions are met at the time the plant is first used or installed ready for use:

- it is a small business taxpayer for that income year
- at least 50 per cent of the intended use of the plant is in carrying on a business for income-producing purposes
- it is not reasonably likely to expand beyond being a small business taxpayer for the next 3 income years because of the plant's use and
- the plant is not to be let or leased other than for short-term hire.

Small businesses which are able to continue to use accelerated rates of depreciation will not be able to reassess the effective life of their plant.

Definition

You are a small business taxpayer if you carry on a business during the income year and either:

- your average turnover for the year is less than $1 million or
- you choose to recalculate your average turnover for an income year before the 2001–02 income year and it is less than $1 million.

Average turnover

Generally, your average turnover for an income year is the average of your 'group turnovers' for the current year and the preceding 2 years, if any. However, you can only average the years in which you carried on a business. For example, if you have carried on a business for the current and previous year only, you would average only the sum of group turnovers for those 2 years.

You are taken to be carrying on a business in an income year if you are winding up a business you formerly carried on and you were a small business taxpayer at the time that you stopped carrying on the business.

You may choose to recalculate the average turnover for an income year before the 2001–02 income year by calculating the average of the group turnover of the current year and a reasonable estimate of the group turnover for the following 2 years.

Group turnover

To determine the group turnover for an income year, a small business taxpayer's turnover is grouped with the turnover of entities it controls or is controlled by. These grouping measures are based on those that apply under the CGT roll-over relief for small business.

Record keeping

If you claim a deduction for depreciation in your tax return, you must keep the following information:

- the undeducted cost and written down value of each item of plant at the start of the income year
- the cost and the date you first used or installed ready to use each additional item you acquired during the income year
- where you dispose of an item during the year, the cost and sale price, dates of acquisition and disposal and the undeducted cost and written down value of the item
- the adjustments made to cost, undeducted cost and written down value
- details of balancing charge relief including the alternative treatment of assessable adjustments
- the rate and amount of depreciation claimed for each item of plant
- the undeducted cost and written down value of each item at the end of the income year.

To help you keep this information, we have provided depreciation worksheets at the back of this publication. You may make photocopies. Do not attach any worksheets to your tax return but keep them with your other tax records.

You must also keep:

- details of the basis of your estimates of effective life where you have not adopted the life periods determined by the ATO
- original documents such as suppliers' invoices and receipts for expenditure on plant.

You must keep the information and records for the entire period over which you depreciate an item and for a further 5 years from the date of your last claim. The 5 years starts on either 31 October or the date you lodge your tax return, whichever is the later. This period is extended if, at the end of the 5 years, you are in a dispute with the ATO that relates to the depreciation claim.

Completing the depreciation schedule

You do not need to complete a *Depreciation schedule 2001* if you are a small business taxpayer as defined under **Small business taxpayers** on page 15.

If you are not a small business taxpayer within the definition on page 15 and you are carrying on a business and claim a deduction for depreciation of more than $1000, you will need to complete the *Depreciation schedule 2001* and attach it to your tax return.

For a copy of the *Depreciation worksheet* and the *Low-value pool worksheet,* refer to the back of this publication. You should use these worksheets to help you complete your income tax return and the *Depreciation schedule 2001*.

For more information about the *Depreciation schedule 2001,* see the *Depreciation schedule 2001 instructions*. To find out how to get these publications, see the inside front cover.

Extracts from *Taxation Ruling IT 2685* and *Taxation Ruling TR 2000/18* showing changes in the effective lives of some commonly used items

Item	*Effective life in years given in* *IT 2685*	*TR 2000/18*
Air conditioners		
– ducted	15	13 1/3
– room units	10	10
Alarms	20	20
Calculators, electronic	10	10
Carpets, business premises	5	5
Cash registers	7	6 2/3
Chainsaw	3	2
Computers	5	4
Curtains and drapes	7	6 2/3
Electric hand tools	5	5
Electric vacuum cleaners	10	10
Furniture	15	13 1/3
Hot water service	20	20
Libraries	10	10
Lights, fluorescent	20	20
Loose hand tools	full replacement cost	5
Motor vehicles		
buses		
– carry 9 or more	7	6 2/3
– carry fewer than 9	7	6 2/3
cars		
– taxis	4	4
– other	7	6 2/3
trucks		
– carry 1 tonne or more	7	6 2/3
– carry less than 1 tonne	7	6 2/3
Photocopiers	10	5
Television sets	10	10
Washing machines	7	6 2/3
Houses and flats let furnished		
blind, venetian	20	20
carpets	10	10
curtains and drapes	7	6 2/3
electric bed	15	13 1/3
electric clock	15	13 1/3
electric heater	10	10
furniture and fittings	15	13 1/3
garbage unit, compacting	7	6 2/3
hot water service	20	20
lawn mowers		
– motor	7	6 2/3
– self-propelled	5	5
linoleum and similar floor coverings	10	10
microwave ovens	7	6 2/3
radios	10	10
refrigerators	15	13 1/3
stoves	20	20
television sets	10	10
vacuum cleaners	10	10
washing machines	7	6 2/3

Note 1: To find out which effective life you should use for a particular item of plant, refer to pages 6 and 7 of this publication.

Note 2: If you are a small business taxpayer who is eligible to use accelerated rates of depreciation, refer to one of the tables on page 5 of this publication.

Guidelines for the use of the depreciation worksheet

The depreciation worksheet (Worksheet 1) is at the back of this publication.

Primary production and non-primary production—use a separate worksheet for each category of income.

Adjustments—the cost of an item of plant for income tax depreciation purposes may differ from its cost to you. For adjustments that you may have to take into account see **Adjustments to cost for depreciation purposes** on page 2.

Written down value—the cost of the plant reduced by the depreciation deductions actually claimed for the plant. It does not take into account deductions that were not allowable due to private or exempt use of the plant. You have a written down value at the start and end of an income year. You include an amount in your assessable income if the termination value of plant exceeds its written down value.

Undeducted cost—the cost of the plant reduced by the depreciation deductions allowable for the plant or that would have been allowable if you had used it wholly for income-producing purposes from the time you acquired it. You have an undeducted cost at the start and end of an income year. Diminishing value depreciation is based on undeducted cost and you can deduct an amount upon the disposal of the plant if its termination value is less than its undeducted cost.

Termination value—generally, the termination value of plant is its sale proceeds less the expenses reasonably attributable to the sale. However, in some cases special rules apply, see the meaning of termination value on page 1.

Balancing adjustments—usually occur when an item of plant is sold, scrapped, destroyed, lost, given away or otherwise disposed of. See **What happens if you no longer own an item of plant** on page 10, **Balancing adjustments for plant partly used for business** on page 11 and **Special balancing adjustment rules for cars** on page 12.

Relief offsets against other plant—this is a reference to the offsetting of otherwise assessable balancing adjustments. See **Balancing adjustment offsets** on pages 13.

Rate or effective life—for items of plant acquired before 21 September 1999, depreciation deductions were calculated by applying a 'depreciation rate', after that date depreciation deductions are calculated using a statutory formula of which effective life is a part. However, depreciation rates have been retained for small business taxpayers and certain specific items. See **How are depreciation deductions calculated?** on page 4 and **Effective life** on pages 6 and 7.

Depreciation—there are two methods of calculating depreciation that is, prime cost and diminishing value, also a different formula applies depending on whether the plant was acquired before or after 21 September 1999 and whether you are a small business taxpayer. See **Depreciation calculation for plant acquired after 11.45 a.m. on 21 September 1999** on page 4, **Special depreciation rates for certain items of plant acquired before 11.45 a.m. on 21 September 1999 or by certain small business taxpayers** on page 6, **Depreciation calculation for plant acquired before 11.45 a.m. on 21 September 1999 or by certain small business taxpayers** on pages 5 and 6, and **Depreciation of plant acquired at or before 11.45 a.m. on 21 September 1999 but first used or installed ready for use after that date** on page 6.

Private use—where plant is used partly to produce assessable income and partly for private use and/or to produce exempt income depreciation is allowed only to an extent that reasonably reflects income-producing use. See **Plant used partially for producing income** on page 6.

The letters **G**, **H**, **I**, **J** and **K** on the worksheet correspond to labels on the *Depreciation schedule 2001*. You do not need to complete a *Depreciation schedule 2001* if you are a small business taxpayer as defined under **Small business taxpayers** on page 15. If you are not a small business taxpayer within the definition on page 15 and you are carrying on a business and claim a deduction for depreciation of more than $1000, you will need to complete the *Depreciation Schedule 2001*. The worksheet will assist you to complete the schedule. For more information, see the *Depreciation schedule 2001 instructions*.

Guidelines for the use of the low-value pool worksheet

The low-value pool worksheet (Worksheet 2) is on the last page of this publication.

Primary production and non-primary production—use a separate worksheet for each category of income.

Description of low-value plant—low-value plant is plant that you have already (or could have) depreciated using the diminishing value method to an undeducted cost of less that $1000. It is also known as low undeducted-cost plant. See **Plant that can be allocated to a low-value pool** on pages 8 and 9 and **Plant that cannot be allocated to a low-value pool** on page 9.

Assessable income use—you must estimate the percentage of business use for low undeducted-cost plant and low-cost plant you allocate to a low-value pool. Also you do not include in the disposal proceeds or termination value the percentage that you estimated the plant would be used for non-income-producing purposes. See **Plant used partly for non-income-producing purposes** on pages 9 and 10, and **Disposal of an item of plant from a low-value pool** on page 10.

Description of low-cost plant—low-cost plant is an item of plant you acquired after 1 July 2000 that cost less than $1000. See **Plant that can be allocated to a low-value pool** on pages 8 and 9, and **Plant that cannot be allocated to a low-value pool** on page 9.

Adjustments—the cost of an item of plant for income tax depreciation purposes may differ from its cost to you. For adjustments that you may have to take into account see **Adjustments to cost for depreciation purposes** on pages 2 and 3.

Termination value—generally, the termination value of plant is its sale proceeds less the expenses reasonably attributable to the sale. However, in some cases special rules apply, see the meaning of termination value on page 1.

The letters **N**, **O** and **P** on the worksheet correspond to labels on the *Depreciation schedule 2001*. You do not need to complete a *Depreciation schedule 2001* if you are a small business taxpayer as defined under **Small business taxpayers** on page 15. If you are not a small business taxpayer within the definition on page 15 and you are carrying on a business and claim a deduction for depreciation of more than $1000, you will need to complete the *Depreciation Schedule 2001*. The worksheet will assist you to complete the schedule. For more information, see the *Depreciation schedule 2001 instructions*.

Worksheet 1—Depreciation

Primary production only ☐ Non-primary production only ☐

Date of addition or adjustment	Description of each unit	Adjustments		Cost of plant less adjustments	Opening written down value	Opening undeducted cost	Disposals				Depreciation				Closing written down value	Closing undeducted cost
									Balancing adjustments							
		Details	Amount				Date	Termination value	Assessable income	Deductible	Percentage rate or effective life		Prime cost	Diminishing value		
															K	
								Totals							Totals	
								Loss relief offsets against other plant			Deduct for private use				Deduct for private use	
								Amount to be returned as income (Do not deduct from depreciation)	G	H	Amount to be claimed as a deduction (Do not include in **Total depreciation**)		I	J	Subtotals	
															Total depreciation	

Totals

Worksheet 2—low-value pool

Primary production only ☐ Non-primary production only ☐

1 Description of low-value plant (LVP)	2 Opening undeducted cost of LVP	3 Assessable income use (%)	4 Reduced cost of LVP (2 x 3)	5 Description of low-cost plant (LCP)	6 Cost of LCP	Adjustment: 7 Details	Adjustment: 8 Amount	9 Adjusted cost (6 – 8)	10 Assessable income use (%)	11 Reduced cost of LCP (9 x 10)	Balancing adjustments: 12 Termination value (TV)	Balancing adjustments: 13 Assessable income use (%)	Balancing adjustments: 14 Reduced TV (12 x 13)

Subtotal **O**

Add opening balance of low-value pool **B** **0***

Sum of **O** and **B** **C**

C x 37.5% **D**

** Opening balance of low-value pool for 2000–01 is zero.*

Total **N**

Subtotal **E**

E x 18.75% **F**

Depreciation deducted (**F** + **D**) **G**

Sum of reduced termination values **H**

Closing balance of low-value pool (**C** + **E** – **G** – **H**) **P**

This will be the low-value pool opening balance for the next tax year.

Note: If amount at P is negative, include that amount in your assessable income as a balancing adjustment.