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Market Update

Capital Allowance & Tax Incentives

The Annex, 12 Creek Street Brisbane
Developed by Dexus,
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Capital Allowance & Tax Incentives

There has never been a better time to spend on capital assets.

Supported by stimulating levels of capital allowance incentives, the message from the federal government is that there has never been a better time to spend on capital assets.

In response to the expected reduction in expenditure by businesses due to COVID-19, the Federal Government has announced the provision of more generous depreciation allowances, to encourage small and large businesses alike to purchase plant and equipment, continue spending on construction and fitouts and maintain strong activity in manufacturing.

Since the onset of the lockdowns and especially considering the resultant slowing of economic activity in many sectors, activity in the construction industry has remained at reasonable levels – hinting that the policy has been successful.

So what exactly has changed?

The 'Backing Business Investment' (BBI) measure provides a time-limited incentive to support business investment and economic growth by accelerating depreciation deductions.

Initially designed to run from 12 March 2020 through to 20 June 2021, the expected depth and duration of the economic downturn has led to the government extending the provisions until the end of 2021.

The key features are as follows:

- Businesses can claim an immediate deduction for multiple assets, new or second-hand, provided each asset costs less than AU$150,000;
- From 12 March 2020 until 31 December 2020, the instant asset write-off threshold amount is AU$150,000 (up from AU$30,000);
- Eligibility has been expanded to businesses with an aggregated turnover of less than AU$500 million (up from AU$50 million).

As this does not apply to building works, it remains advisable to have the costs broken down into their respective categories by a quantity surveyor, ensuring no overclaims are made and that all assets are claimed in their correct category. This is critical as the incorrect categorisation may result in substantial overclaims.

The table below demonstrates how the tax depreciation write-off rules have been significantly expanded to maintain sound levels of business investment and keep the broader economy moving.

An entity is eligible for accelerated depreciation when:

- They have an aggregated turnover of less than AU$500 million;
- The asset is a new or second-hand depreciating asset acquired and first used, or installed ready for income producing purposes from 12 March 2020 until 30 December 2021; and
- The owner did not already apply other depreciation deductions, or the instant write off.

Any asset where the purchase transaction was made prior to 12 March would only be claimable under the old regime with the lower thresholds.

Remember - this is about stimulating new activity – not providing more generous allowances for previously commenced projects.

Category of Expenditure	Pre- 12 March 2020	Covid-19 Changes
Division 40 (Plant and Equipment)	Effective Life x 200%	Effective Life x 200%
Division 43 (Building)	2.5% or 4%	2.5% or 4%
Low Value Pool	$1,000	$1,000
Division 40 Instant Write-off Threshold	$30,000	$150,000
Turnover Eligibility Threshold	$30 Million p.a.	$500 Million p.a.

Case Study - Fitout

A typical fitout contains plant and equipment (such as furniture, lighting and AV equipment), often approximately half of the overall expenditure. The balance is considered building works and would be depreciated at 2.5%. Previously, the depreciation on the plant and equipment would be broken down into various categories and would be depreciated according to the effective life allocated by the ATO for that category.

This process is now much simpler, providing the owning entity has a turnover of less than $500M. The 'plant and equipment' component is now eligible for immediate tax deduction where each item, system or set is below the $150,000 threshold. Only a marginal number of fitout items would fall outside these parameters.

Of course, theory is often better than real life practice. Such a substantial deduction in one hit is only useful if the income is adequate to take advantage of it. Moreover, investment decisions to capitalise on these allowances are required to be made in a crisis – where capital investment is being delayed or reduced in favor of retaining cash. This is the conundrum the federal government is specifically trying to address.

The fact is, the government has used capital allowances and other tax incentives to both stimulate and dampen capital expenditure in various sectors since introduction in the 1970s. The generosity of this scheme is a clear indication of the extent of concern the government has for the economy and an insight into how long they expect the impacts of COVID-19 to linger.

Another noteworthy feature of this stimulus is that the key dates relate to the timing of the decision to make the expenditure, rather than when the expenditure is paid.

This usually relates to date of contracts, commencement on site or exchange on the purchase of property. This means long term projects commencing up to 31 December 2021 can be depreciated at the accelerated depreciation rates even if they complete two or three years later, a point at which incomes may have returned to 'normal'.

Ultimately, there have never been such generous tax concessions on capital expenditure and therefore never a better time to spend the money and get the economy flowing.

Case Study Worked Example

A company commences a $3M fitout on the 15 March 2020, reaching completion by the end of May.

A typical fitout contains 40-60% 'plant and equipment', the rest is likely to be capital works (non-plant items).

As the fitout commenced post 12 March 2020, subject to the owner of the fitout having an aggregate turnover under $500 million, this venture is eligible for accelerated depreciation.

The fitout is calculated to contain $1.6M of 'plant and equipment' and $1.4M of building works, including consultants' costs and fees.

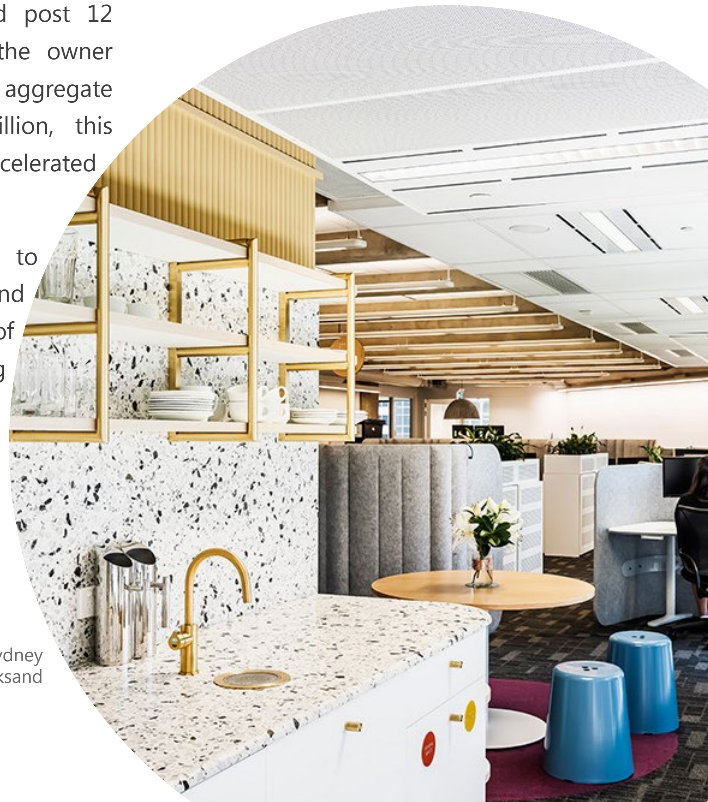
Although the total expenditure of $1.6M is over the threshold for immediate deduction, individually the assets (such as tables, chairs, blinds, joinery) are well below the $150,000 threshold, rendering the full $1.6M available as an immediate deduction in the 2019/2020 financial year.

The building works component of $1.4M will depreciate at 2.5% prime cost as per previous allowances.

These figures do not consider fitout incentives which may well be adjusted as a result of the competition for tenants post COVID-19 and as a result of which party is best able to take advantage of the instant asset write off provisions.

Key Figures to remember:

- Dates of commencement of works should be after 12 March 2020 and before 31 December 2021;
- Completion dates are not considered in the determination of depreciation entitlements;
- Aggregate turnover of owning entity should be under $500 million.



Medibank Workplace, Sydney
Designed by Gray Puksand

About Slattery

Slattery is a property and construction advisory firm specialising in quantity surveying, cost management and early phase project advisory, with an outstanding history spanning more than 40 years.

We work hand-in-hand with governments, institutions and organisations as well as planners, developers, architects and design teams on a broad range of property and construction projects.

A commitment to excellence and innovation, and an ability to become an integral part of the project team has earned Slattery the trust and respect of clients and project teams alike. Slattery adds value by taking control and ownership of the cost management process from the outset. We understand the importance to drive innovation and productivity.

We invite you to explore our knowledge sharing further at www.slattery.com.au/thought-leadership

Our Asset Services

Slattery's Asset Services Team provide tax depreciation advice to commercial organisations and institutions around Australia.

As Quantity Surveyors, Slattery are able to provide advice on the allocation of effective lives and costs to certain specific assets for capital allowances purposes. Slattery is not qualified to provide broader tax advice and recommend you seek advice on complementary tax issues from a qualified accountant.

For more information, contact Asset Services Director, Michael Ross at michael.ross@slattery.com.au