

December 2009

## 31 December 2009 cut off for 50%/10% investment allowance

Time is running out for businesses to claim the investment allowance which expires on 31 December 2009.

Small businesses with an annual turnover of less than \$2 million can claim the 50% investment allowance for assets costing \$1,000 or more. To qualify for the 50% allowance, a small business must have committed to acquire the asset (or commenced construction) by 31 December 2009. In addition, the asset must be used (or installed ready for use) by 31 December 2010.

Businesses with an annual turnover of \$2 million or more can still claim a 10% tax deduction for eligible assets (costing \$10,000 or more) if they commit to acquire the asset by 31 December 2009 and use them (or install them ready for use) by 31 December 2010.

Regardless of annual turnover, the asset must be used principally in Australia and principally for business. The investment allowance will no longer be available for eligible assets with a commitment time after 31 December 2009.

Below are some additional issues which should be considered in regard to claiming the investment allowance.

### Investment thresholds

New investment in an asset must be made between 13 December 2008 and 31 December 2009 for any deduction to apply and the amount of your investment in an asset needs to meet the 'new investment threshold' which is as follows:

- ▶ \$1,000 for small business entities, and
- ▶ \$10,000 for all other business.

For the purposes of meeting the thresholds, goods and services tax (GST) is excluded.

### When has the investment occurred?

The investment is considered to have occurred when you have committed to investing in the asset. This is generally when you have:

- ▶ Entered into the contract under which you hold the asset or will start to hold at a later time;
- ▶ Started to construct the asset; or

- ▶ Started to hold the asset in some other way.

To satisfy the investment commitment time test, it is enough that you entered into a contract in relation to the asset between 13 December 2008 and 31 December 2009. This means you do not have to pay for the asset out right or have taken delivery of the asset within this period. However, the contract must be non-conditional or any conditions must be met before 31 December 2009.

For example if the contract is conditional on obtaining finance, the commitment time is generally not until the finance has been obtained. Generally a contract is non-conditional if you were to break the commitment the vendor could take legal action against you to enforce the contract.

Where a particular contract is conditional, it is recommended that legal advice be obtained to determine when the contract becomes enforceable.

## What rate of deduction applies?

The rate at which you can claim the investment allowance depends on whether you are classified as a small business or other business and when you committed to acquire the asset.

The following table summarises the key dates relating to the different investment allowance rates which apply for small and other businesses.

Business entity	Investment commitment time (inclusive)	Date of first use or installed ready for use (inclusive)	Rate of Investment Allowance
Small business	13 December 2008 to 31 December 2009	By 31 December 2010	50%
	13 December 2008 to 30 June 2009	By 30 June 2010	30%
Other business	1 July 2009 to 31 December 2009	By 31 December 2010	10%
	13 December 2008 to 30 June 2009	1 July 2010 to 31 December 2010	10%

(Source: ATO website, *Business Tax Break guide*)

## When can you claim the deduction?

Provided all of the eligibility criteria are satisfied for the income year, the investment allowance can be claimed as a tax deduction in the income tax return for the income year in which the asset is first used or installed ready for use.

## Hire purchase and luxury car leases

For most leased or rented assets it is the owner of the asset, and not the lessee or renter, who is eligible for the investment allowance. The exceptions are hire purchase and luxury car leases.

However, for assets acquired under a hire purchase (HP) arrangement or a luxury car lease, the commitment date for the investment allowance is the date of entering into the HP arrangement or the lease, not when the order contract is made with the supplier. The rationale behind this is the investment allowance

provisions requires the taxpayer to be the "holder" of the asset under Division 40, (the depreciation rules).

For hire purchase (and similar arrangements) and luxury car leases, the hirer / lessee are deemed to be the holder of the asset, but the ATO's view is the investment allowance commitment requirement for hire purchase and luxury car leases are not satisfied until the taxpayer has entered into the hire purchase agreement or the lease agreement.

Businesses have until 31 December 2009 to enter into the HP arrangement or luxury car lease to be eligible for the investment allowance. Investment decisions after that date will not attract the allowance.

If the hire purchase agreement or luxury car lease cannot be made by the investment deadline, you may need to consider alternative financing arrangements such as chattel mortgage, as discussed below.

Different rules apply if you purchase a depreciating asset and become the legal owner prior to entering into the HP agreement or the luxury car lease. In this case, the investment commitment time is the time you enter into the contract to purchase the asset. This may be when the order contract is made with the supplier (provided the order is non-conditional).

## Chattel mortgages

If the finance is by way of chattel mortgage, the commitment time will depend on whether the mortgagee (lender) is the legal owner of the asset or just has an equitable interest in the asset. If the chattel mortgage gives legal ownership to the mortgagee, it is treated like a HP agreement. That is the commitment time is the date the chattel mortgage is entered into.

However, if you purchase a depreciating asset and become its legal owner prior to entering into the legal chattel mortgage, the investment commitment time is the time at which you enter into the contract to purchase the asset. This may be when the order contract is made with the supplier.

If you enter into an equitable chattel mortgage (ie the mortgagee only has an equitable interest in the asset) which operates only by way of a charge over the asset and you are the legal owner of the asset, the investment commitment time is when you enter into the order contract with the supplier.

If you are unsure whether you have a legal or equitable chattel mortgage, you should obtain legal advice in this regard.

## Assets held by partners

Where a partner in a partnership acquires depreciating assets in his own name (ie the asset is not a partnership asset) the partner may be able to claim the investment allowance. This is on the basis the partnership is not a separate legal entity. It is a relationship which exists between persons carrying on business in common with a view to a profit. Therefore, for the purposes of the investment allowance rules, each partner of the partnership is considered to be carrying on the partnership business.

### Example

*George and Michael are partners in a business. They both purchase cars on 28 December 2009 and immediately start to use the cars in the partnership business. The cars are not partnership assets so George and Michael are each the holders of their own cars. As both George and Michael are carrying on the partnership business, their use of the cars is use for the 'purpose of carrying on a business'. Therefore, if the cars are used principally for the purpose of carrying on the partnership business and all of the other conditions for the deduction are met, George and Michael will be able to claim the investment allowance.*

Note however, the partner is not considered to be a small business entity (for the purposes of Division 328 of the ITAA 1997). Therefore, the partner cannot use the \$1000 threshold or the 50% deduction rate applicable to small business entities. They would be entitled to the 10% rate.

## Calculating the \$2 million annual turnover

To qualify for the 50% investment allowance, small businesses must determine whether their annual turnover is less than \$2 million. The calculation of the annual turnover is based on the "Small Business Entity turnover test" which includes certain amounts and excludes other amounts. Examples of these amounts are in the table below.

Should you require assistance or additional information, please **contact your PKF Tax Adviser** or:

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## Amounts included and not included in ordinary income

Include these amounts	Do not include these amounts
trading stock sales	GST you charge on a transaction
fees for services you provide	amounts you borrow for the business
interest from business bank accounts	proceeds from selling business capital assets
amounts you receive to replace something that would have had the character of business income, for example, a payment for loss of earnings.	insurance proceeds for the loss or destruction of a business asset
	amounts you receive from farm management deposit repayments.

(Source: ATO website, *Business Tax Break guide*)

### Retail fuel sales

There is a special rule for fuel retailers to work out if they are a small business entity. Retail fuel sales are not included in their turnover. This special rule is in the law because sales of retail fuel are characteristically high in sales volume with low profit margins.