

Effective Life 2021/1 - Explanatory statement -



Explanatory Statement

Income Tax (Effective Life of Depreciating Assets) Amendment Determination (No 1) 2021

General Outline of Instrument

1. The authority for making an effective life determination is provided by subsection 40-100(1) of the *Income Tax Assessment Act 1997* (ITAA 1997).
2. This instrument updates the *Income Tax (Effective Life of Depreciating Assets) Determination 2015 – F2015L00798* registered on 11 June 2015 with new effective lives determined by the Commissioner.
3. The instrument is a legislative instrument for the purposes of the *Legislation Act 2003*.
4. Under subsection 33(3) of the *Acts Interpretation Act 1901*, where an Act confers a power to make, grant or issue any instrument of a legislative or administrative character (including rules, regulations or by-laws) the power shall be construed as including a power exercisable in the like manner and subject to the like conditions (if any) to repeal, rescind, revoke, amend, or vary any such instrument.

Date of effect

5. This instrument applies from 1 July 2021.
6. Under section 12(2) of the *Legislation Act 2003* this instrument does not adversely affect the rights or liabilities of any person other than the Commonwealth.

What is the effect of this instrument

7. Taxpayers are provided with a choice under the ITAA 1997 when measuring the decline in value (depreciation) of a depreciating asset. A taxpayer can either use an effective life determined by the Commissioner, or work out (self-assess) the effective life of a depreciating asset themselves in accordance with section 40-105 of the ITAA 1997.
8. The effect of this instrument is that it provides taxpayers in specific industries, and for specific assets, with effective lives determined by the Commissioner as a basis to calculate the decline in value (depreciation) of a depreciating asset for income tax purposes.
9. Effective lives determined by the Commissioner provide what is referred to as a 'safe harbour' for taxpayers as they have certainty these lives will be accepted by the Commissioner.
10. The effective life determinations in the instrument apply on a prospective basis. The effective life determinations with an application date earlier than 1 July 2021 are included in the instrument because there is a need to:
 - update industry headings to correctly align with the current Australian and New Zealand Standard Industrial Classification (ANZSIC),
 - split high level categories into sub-categories within the ANZSIC code group to enhance readability and improve user experience,

- update the asset description, or
 - correct a previous minor mistake.
11. The plus (+) in the third column of Table A that indicates the availability of an immediate deduction to primary producers for a fodder storage asset is not necessary for the purposes of the *Income Tax (Effective Life of Depreciating Assets) Determination 2015*. The purpose of the determination, as incorporated in the Taxation Ruling, is to set out the Commissioner's effective life determinations for certain assets. Importantly, this change does not represent a change in the Commissioner's view of the law.

Compliance cost assessment

12. Compliance cost impact: Minor. The instrument will affect only a small proportion of businesses and confirms existing practice. There will be no or minimal impacts for both implementation and ongoing compliance costs. The legislative instrument is minor or machinery in nature. However, affected taxpayers will nonetheless need to be aware of the changes.

Background

13. The effective life depreciation policy came into effect on 1 July 1991. Under this policy, depreciation was calculated as a percentage based on the effective life of an asset. A 20% loading was then added. The rates were then broadbanded into one of seven common rates. The 20% loading and broadbanding provided accelerated rates of depreciation.
14. On 21 September 1999, accelerated depreciation was removed. As part of that policy, the Government also endorsed the Review of Business Taxation's recommendation that the Commissioner institute an ongoing revision of the effective life schedule (Recommendation 8.5 of *A Tax System Redesigned*).
15. As a result, the ATO has been undertaking ongoing annual reviews of the Commissioner's determinations of effective life. In doing so, the Commissioner consults with a number of key stakeholders, including users of the assets, industry associations, manufacturers and suppliers of the assets and, when necessary, industry consultants.
16. The reviews are comprehensive in terms of the information gathered and the consideration given to different factors.
17. Taxation Ruling 2021/X explains the factors the Commissioner takes into account when making effective life determinations. Those factors include commercial and technical obsolescence, to the extent this can be predicted. The review does not focus on the physical life of assets to the exclusion of economic influences on its effective life.
18. Ultimately, the Commissioner's determinations must satisfy the question of how long the depreciating asset can be used by any entity for one or more specified purposes, including a taxable purpose.
19. The new determinations of effective life do not reflect any change in policy. Formatting and layout changes made to the existing entries in Table A and Table B of the Commissioner's schedule do not change the effective life determinations for the assets.

Consultation

20. An extensive and comprehensive consultation process was undertaken to update the instrument with effective lives of new depreciating assets for the following industries:
 - Horse training (racing)
 - Salt harvesting
21. Notifications of the above industry reviews were listed under the Effective life section on ato.gov.au during July 2020 with an invitation to participate in the reviews. The notifications provided details on the review process and an ATO contact officer leading the review.
22. The notifications were supported by a communications strategy that included working with professional tax associations to include information on the reviews in their publications, inviting participation from industry associations and seeking industry assistance through the government's Business Consultation website from July 2020.
23. A targeted email campaign was conducted to contact all the taxpayers identified to be operating in the relevant industries. Key stakeholders in the specific industry under review, or who were identified operating in the relevant industry but were not listed on the bulk email campaign, were also directly contacted.
24. Manufacturers and suppliers of the assets under review were also consulted for their views on the life of the assets.
25. The draft effective lives for the above industries were published throughout February and March 2021 with requests for feedback. The drafts were also sent to key stakeholders, including industry participants and associations, for comment.
26. An effective life review panel was involved in reviewing the proposed effective lives. The review panel members include representatives of the ATO and the following organisations:
 - Corporate Tax Association
 - Chartered Accountants Australia and New Zealand
 - Australian Finance Industry Association
 - National Australian Bank Finance
27. The involvement of review panel members ensures that a full consultative process has been carried out with key stakeholders when conducting effective life reviews.
28. The panel provided detailed feedback which included:
 - The process has been comprehensive
 - There has been significant consultation undertaken
 - The reviews have been conducted in a professional manner.
29. The recommendations of the review panel are reflected in the final effective life determinations and the panel provides the final sign-off on the consultation undertaken. The final effective life determinations are sent to all taxpayers that participated in the review and are also published on the ATO website.
30. A review of the industry categorisation in Table A of the Commissioner's schedule was also conducted to improve readability and user experience. The proposed changes have been presented to the effective life review panel for consultation and have been endorsed by the panel. No changes were made to the effective life determinations for the assets under this review.
31. The ATO has an open and ongoing consultation process in relation to the Commissioner's effective life. Taxpayers can raise matters with the ATO at any time regarding the effective life determinations.

Legislative references:

- *Acts Interpretation Act 1901*
- *Human Rights (Parliamentary Scrutiny) Act 2011*
- *Income Tax Assessment Act 1997*
- *Income Tax (Effective Life of Depreciating Assets) Determination 2015*
- *Legislation Act 2003*

Other References

- Recommendation 8.5 of The Review of Business Taxation Report: *A Tax System Redesigned*

Statement of compatibility with Human Rights

Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

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This Legislative Instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview of the Legislative Instrument

The Legislative Instrument provides taxpayers with a choice when measuring the decline in value (depreciation) of a depreciating asset, because a taxpayer can either use an effective life determined by the Commissioner or work out (self-assess) their own effective life of a depreciating asset.

Effective lives determined by the Commissioner provide what is referred to as a 'safe harbour' for taxpayers, as it provides certainty to taxpayers that these lives will be accepted by the Commissioner.

Human rights implications

This Legislative Instrument does not engage any of the applicable rights or freedoms. The Instrument provides taxpayers in specific industries and for specific assets with effective lives a basis to calculate the decline in value (depreciation) of a depreciating asset for income tax purposes.

Conclusion

This Legislative Instrument is compatible with human rights as it does not raise any human rights issues.