IT'S A WRITE-OFF

CHOOSING BETWEEN WRITING OFF AN ITEM OR USING DEPRECIATION AT TAX TIME CAN BE A TOUGH DECISION. BRAD CALLAUGHAN, ACCOUNTANT AND FINANCIAL PLANNER, HELPS MAKE THINGS A LITTLE CLEARER.

Businesses constantly require new assets and frequently update their equipment. Specifically, this can be due to underperforming servers, out-of-date computers, hardware and equipment, or a need to invest in assets which may be more energy efficient, and so on.

Businesses have always faced the issue of using depreciation versus just writing off the item in the first year. To write-off an item, you would claim the outright tax deduction in that year, but forgo any benefit you may have received in the next year. To depreciate that item, you would write it off over its effective life (determined by the ATO).

Many business owners became worried about the effects of writing off an item in the same year and not receiving an ongoing tax deduction to help reduce tax in future years. While there are always going to be different opinions, the majority of them seem to be changing.

Several years ago, businesses had to rely on the tight depreciation tax rules to gain a deduction on the depreciable amount. Anything worth $300 or less could be written off in that year and anything over had to be depreciated at the pre-determined ATO rate. Over the years, the rules have gradually changed to allow items under $1000 in cost to be written off within the first year.

From 1 July 2012, small businesses (ie, with annual turnover of less than $2 million) were able to choose from three new items to help them gain a greater tax deduction in the first year, instead of waiting for the depreciation over the item's effective life.

They are as follows:

- write-off depreciating assets costing less than $6500 in the income year in which they commence use of the asset or have it installed ready for use for a taxable purpose during or before that income year
- immediately write-off up to $5000 for motor vehicles acquired after 1 July 2012, with the remainder to be written-off at a rate of 15 per cent in the first year and 30 per cent in following years
- for assets that cost $6500 or more, small businesses will be able to allocate these to the general pool and depreciate them at a rate of 15 per cent in the first year and 30 per cent in following years.

These new rules are sure to make any small business happy regarding tax, potentially saving up to $1950 on one new item that costs $6500. The great thing is that you are not limited to a cap, and can also split items purchased in bulk. Imagine you purchased 20 chairs worth $1000 each. Even though the total is $20 000, you can claim the whole $20 000 outright in that year, as each item is under $6500.

Why?

The answers are simple and include:

- increasing your cash flow by deferring your tax liabilities
- reducing compliance costs by removing the requirement to calculate depreciation allowances and track assets for depreciation
- making asset ownership more attractive than leasing or debt financing
- removing the long-life pool and allowing small businesses to depreciate assets (other than buildings) in a single pool further simplifies depreciation calculations.

The government has simply realised that to encourage businesses to spend on infrastructure, they need to give businesses an incentive. Their successful campaign of offering 50 per cent rebate on new items some years back was a huge success in encouraging businesses to purchase new equipment.

So should you replace all your equipment? The short answer is 'yes'. There has been no better time to buy equipment that you require. If your equipment is old, there is no better time to upgrade. If you require new assets to bring your business in line with competitors and be able to compete, do it.

If you have the cash flow and need the equipment, you will, as mentioned, effectively save $1950 on a $6500 purchase, which will stay in your pocket and not go to the government.

Businesses should not be worried about the next year and not receiving any of the tax deduction for that year. The focus is on the current year and what you should be doing to decrease you tax bill. As part of your tax planning, you should be looking to increase your current tax deductions.

It is now that you should be taking advantage of this opportunity. The benefits of reducing your tax and increasing your cash flow and productivity, and therefore increasing your profits, are far too inviting to not take advantage of.

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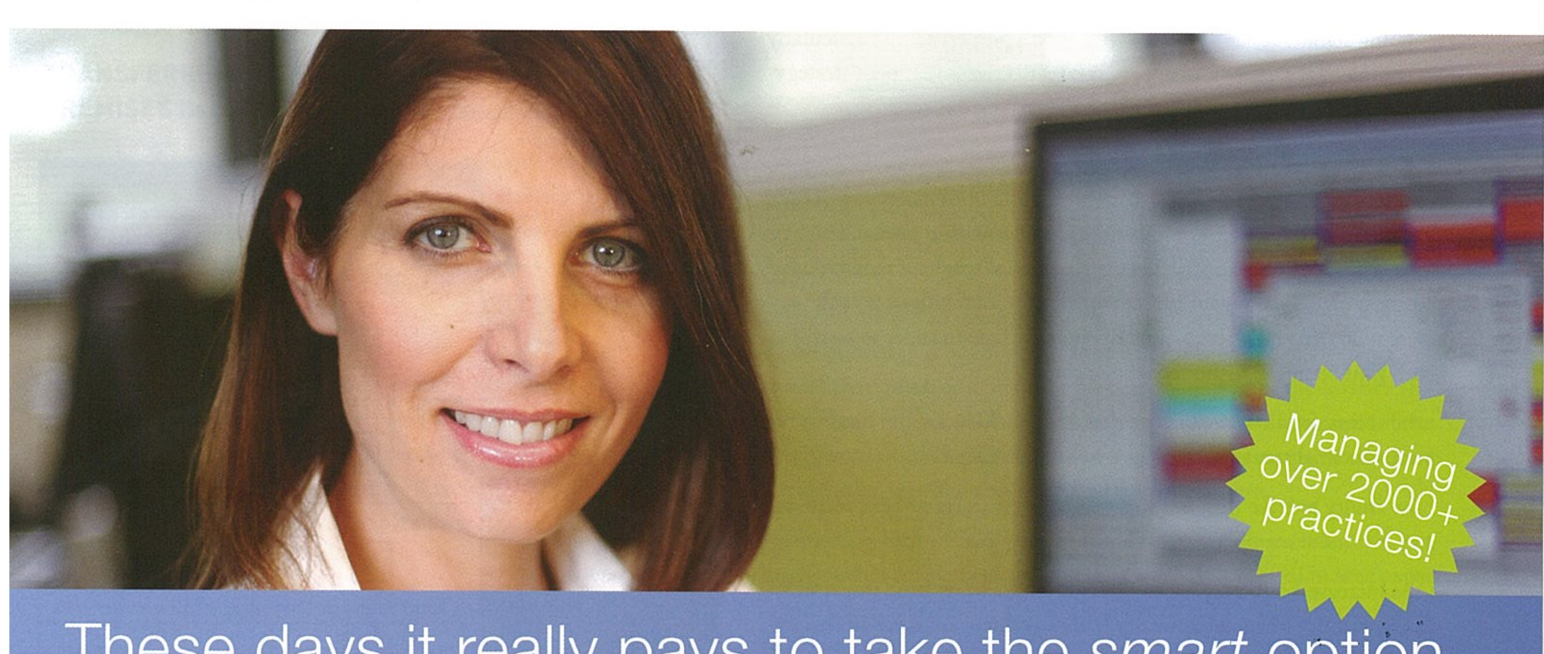

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