

TR 2017/D1EC - Compendium



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Public advice and guidance compendium – TR 2017/D1

❗ Relying on this Compendium

This is a compendium of responses to the issues raised by external parties to draft Taxation Ruling TR 2017/D1 *Income tax: composite items and identifying the depreciating asset for the purposes of working out capital allowances*. It has been edited to maintain the anonymity of entities that have commented. It is not a publication that has been approved to allow you to rely on it for any purpose and is not intended to provide you with advice or guidance, nor does it set out the ATO's general administrative practice. Therefore, this Compendium does not provide protection from primary tax, penalties or interest for any taxpayer that purports to rely on any views expressed in it.

Summary of issues raised and responses

All legislative references in this Compendium are to the *Income Tax Assessment Act 1997*, unless otherwise indicated.

Issue number	Issue raised	ATO Response/Action taken
1	General principles We agree with the Commissioner's preliminary views that: <ul style="list-style-type: none">• in determining whether a composite item is a single depreciating asset or whether each of its component parts are separate depreciating assets, regard should be had for the five guiding principles set out in paragraph 6 of the draft Ruling, and• an 'interest in an underlying asset' refers to both a partial interest in the entirety of a composite item and a whole interest in a particular component of a composite item. We are pleased to see 14 practical examples that should assist users of the final Ruling once finalised.	Noted.
2	Composite items The second sentence of paragraph 4 of the draft Ruling sets out the legislated directive determining whether a composite item is itself a depreciating asset or whether one or more components are separate depreciating assets is a question of fact and degree. While the provision (subsection 40-30(4)) has been duly referenced in the footnotes, it would	Change made. See paragraph 6 of the updated draft Taxation Ruling TR 2023/D2 <i>Income tax: composite items - identifying the relevant depreciating asset for capital allowances</i> .

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	<p>be preferable to incorporate the reference into paragraph 4 itself.</p> <p>This is to provide clarity to readers that the directive is legislated and it is not a view or an interpretation of the Commissioner.</p>	
3	<p>Example 2 – desktop computer package</p> <p>We agree with the conclusion that the original computer package is one single depreciating asset.</p> <p>However, paragraph 30 of the draft Ruling requires some clarity. It states that the subsequent acquisition of ‘replacement’ elements of the single asset will be treated as the acquisition of separate depreciating assets.</p> <p>If the monitor in the computer package (composite item) is broken and replaced, the outcome of applying paragraph 30 of the draft Ruling is that the new monitor will constitute a separate depreciating asset apart from the original computer package asset.</p> <p>In Example 9 of the draft Ruling, the replacement of an electricity pole which was destroyed in a storm does not create a new deprecating asset separate from the distribution line (for example, the composite asset) of which the relevant pole is a part. The ATO is of the view that there has been no substantial alteration to the function of the depreciating asset. Why would the replacement of a broken monitor, being one composite part of the overall ‘desktop computer package’ asset, not give rise to the same outcome?</p> <p>If the above commentary in fact represents a misinterpretation of paragraph 30 of the draft Ruling, please reword the paragraph to clarify the circumstances in which the ‘replacement’ of one component will, and will not, constitute the acquisition of a depreciating asset separate from the original composite item.</p>	<p>Changes have been made to Examples 2 and 9 of the updated draft TR 2023/D2 so that the outcomes can be distinguished.</p>
4	<p>Example 3 – mainframe computer</p> <p>Example 3 of the draft Ruling can be improved by incorporating pertinent facts about the 20 new terminals. In particular, their ‘adaptability to work with a wide range of controllers’ and any other factors that differentiate the 20 new terminals from the 50 original terminals should be stated in paragraph 33 before the analysis and conclusion. The current drafting of paragraph 33 leaves the reader with the impression that the 20 new terminals are identical to the 50 original terminals, with a reasonable</p>	<p>Additional facts have been included in Example 3 of the updated draft TR 2023/D2 in relation to both the design of the new mainframe computer system and the acquisition and features of the additional 20 terminals.</p>

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	<p>expectation that the new terminals would be treated the same as the original ones, that is, included as part of the original depreciating asset (as second element of cost).</p> <p>If the new terminals pass the 'identifiable' test, the features which allow them to perform a function separate to the rest of the system needs to be clearly set out in paragraph 33.</p> <p>If however they have no identifiable function independent of the mainframe or other controlling device to which they are connected, please expand on the reasons why they would not simply be treated as an improvement to the original asset with the acquisition costs included in the second element of the cost of the original asset.</p>	
5	<p>Example 6 – car global positioning system</p> <p>For completeness, Example 6 of the draft Ruling can be expanded with commentary on the Division 40 treatment in a situation where a car dashboard is modified to install an in-built global positioning system (GPS) bracket or holder, but the GPS unit itself is removable, portable and able to be used away from the car. This is distinct from the scenario contained in paragraph 47 of the draft Ruling, where presumably the portable GPS is merely used inside the car without involving any permanent modification to the car interior.</p> <p>Presumably, the costs of modifying the car to install the bracket or holder and associated electrical components would be included in the second element of the cost of the car, while the removable GPS unit itself would be treated as a separate depreciating asset.</p>	<p>A change has not made in response to this comment. We think the further variation would have limited utility, on the understanding that most removable GPS units now come with removable holders; for example, suction cups or double-sided tape to affix to the vehicle and these can be moved to other vehicles.</p>
6	<p>Additional example – intangible asset</p> <p>We recommend that the final Ruling includes a practical example relating to a common intangible asset that is relevant to many or most taxpayers. Even though there is commentary on intangible assets in the proposed binding section of the draft Ruling and in Appendix 1 - Explanation, all of the Examples in the draft Ruling relate to tangible items.</p> <p>An ideal example is copyright in software. In the modern business environment, the sale and purchase of software is very common. ATO Interpretative Decision ATO ID 2004/982 <i>Capital allowances</i>:</p>	<p>A change has not made been made in response to this comment. It is not clear how the addition of a further example would assist in illustrating the principles given each inquiry will depend on the facts and circumstances of each case.</p> <p>However, if there is a significant issue in relation to intangible assets that we haven't appreciated that the community consider warrants guidance separate to that already provided in ATO ID 2004/982, the Commissioner would have regard to possible further public advice or guidance, subject to other priorities.</p>

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	<i>depreciating asset - copyright in computer program</i> may be a suitable scenario on which to base the example.	
7	<p>Generally the overall guiding principle in the draft Ruling is the linkage of 'depreciating asset' to the concept of 'unit of property'. The examples and principles explained in the draft Ruling rely on tax cases from years gone by when unit of property was relevant.</p> <p>Another Ruling that must be considered in the overall analysis on repairs is Taxation Ruling TR 97/23 <i>Income tax: deductions for repairs</i>.</p> <p>The very fabric of a major aspect of the tax system is held together by the concepts of what is the 'asset' or 'entirety', 'unit of property' or 'depreciating asset'. Once that is determined all other matters fall into place:</p> <ul style="list-style-type: none"> • replacement parts – expense • commencement of depreciation on use, or installed ready for use • termination of use • spare parts deductions and Taxation Ruling IT 333 <i>Expenditure on spare parts and consumable stores. Whether deduction allowable on usage basis or in year of purchase</i>, and • others. <p>The breadth of the implications of these concepts is very broad.</p> <p>Some of these 'well understood' principles may be questioned in some of the examples contained in the draft Ruling.</p> <p>Take Example 2 – desktop computer package – the inference in paragraph 30 of the draft Ruling is that the acquisition of a new keyboard to replace an existing keyboard would be capital. There are a number of factors to take into account, including the fact it is a wireless keyboard, but generally thinking, as a part of a functional whole, that replacement would be considered an expense.</p> <p>This all presupposes that underlying all this is a similar concept and the linkage of 'depreciating asset' to the concept of 'unit of property'. If that is not the case then reliance on past legal principles may not be appropriate.</p>	<p>We think it is clear from the Appendix 1 - Explanation section of the draft Ruling that the functionality test used as a basis of identifying 'unit of property' under the former general allowance deductions is useful in identifying the relevant depreciating asset for capital allowance purposes.</p> <p>It is outside the scope of the draft Ruling to consider what constitutes a repair or capital improvement.</p>