IT 2236 - Income tax : plant purchased under hire purchase agreements - treatment of hire purchase charges

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TAXATION RULING NO. IT 2236

INCOME TAX : PLANT PURCHASED UNDER HIRE PURCHASE AGREEMENTS - TREATMENT OF HIRE PURCHASE CHARGES

F.O.I. EMBARGO: May be released

REF H.O. REF: 86/139-5 DATE OF EFFECT: Immediate

B.O. REF: DATE ORIG. MEMO ISSUED:

F.O.I. INDEX DETAIL

REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:
I 1205575	HIRE PURCHASE CHARGES - PLANT INTEREST & FINANCE CHARGES INSURANCE DEPRECIATION	51(1) 54 55(1) 57AG 57AL

OTHER RULINGS ON TOPIC : IT 196, IT 359

PREAMBLE Where taxpayers acquire plant or articles under hire purchase agreements and the plant or articles are used for the purpose of gaining or producing assessable income it has long been the practice to allow income tax deductions for interest, insurance, hiring and other charges (collectively referred to as hire purchase charges) on one of two bases. On the one hand, income tax deductions have been allowed for hire purchase charges under sub-section 51(1) of the Income Tax Assessment Act, i.e. deductions have been allowed in the year in which the hire purchase charges have been incurred. Alternatively, the hire purchase charges may be added to the cost of the plant or articles and a deduction under sub-section 54(1) may be allowed for the total expenditure on the plant or articles.

2. The alternative basis emanated from a recognition that hirers almost without exception hire the plant or articles subject to a hire purchase agreement and that the term of the hire purchase agreement broadly corresponds to the effective life of the plant calculated for the purposes of sub-section 55(1). Against this background it can be seen that the alternative basis does not operate to the detriment of the revenue.

3. Cases have come to light where taxpayers have sought income tax deductions for depreciation under the alternative basis where the term of the hire purchase agreement far exceeded the period over which the plant was to be depreciated. This has been so particularly since the introduction of accelerated rates of depreciation permitted by sections 57AG and 57AL. Thus, taxpayers have sought deductions for depreciation under the alternative basis at rates allowing write off over 3 or 5 years under section 57AL while the term of

the hire purchase agreement was 10 years or more.

RULING 4. The alternative basis of claiming income tax deductions for hire purchase charges by way of depreciation should not be permitted in future where the period of write off, e.g. 3 or 5 years, is substantially less than the term of the hire purchase agreement. In these cases depreciation should be allowed on the cost price of the plant or articles specified in the hire purchase agreement and deductions should be allowed for the hire purchase charges in the years in which these charges are incurred.

COMMISSIONER OF TAXATION
7 January 1986

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