PRACTICE STATEMENT No. 48 2016

SUBJECT	**FIJI REVENUE & CUSTOMS AUTHORITY:** **DEPRECIATION DEDUCTION**
DATE OF EFFECT	1 January 2016
CONFIDENTIALITY STATUS	May be released to the public
LEGISLATIVE REFERENCES	*Income Tax Act 2015 Section 1 (1), 1 (2), 31, 32, 33, 34 (1).* *Income Tax (Depreciation Rates) Regulations 2016* (Legal Notice #2)
PRACTICE CO-ORDINATOR	Deputy Director Revenue Management

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INTRODUCTION

1. The purpose of this Practice Statement is to provide information on the depreciation allowance for tangible assets used in a business. It is issued with the authority of the Chief Executive Officer (CEO) of the Fiji Revenue & Customs Authority (FRCA) and applies to the tax years that begin on or after 01/01/16.

2. The income tax law allows taxpayers to claim deductions for expenses incurred in gaining or producing income that will be included in gross income.

3. A deduction can be claimed for depreciation on most tangible property (except land) such as buildings, machinery, vehicles. Depreciation is an amount of annual allowance to recover the cost of property that has declined due to wear and tear, deterioration or obsolescence.

4. For tax purposes, the following requirements, which are consistent with the International Financial Reporting Standards, must be met before a deduction is allowed:
   - the asset must be used in the business or income-producing activity;
   - the asset must have a determinable useful life;
   - the asset must be expected to last more than one year or one accounting period.

5. The following changes which are effective from 1 January 2016, apply to the tax year 2016 and subsequent years.
   - taxpayers must use only one of the two depreciation methods - either Straight Line (SL) or Diminishing Value(DV); however, the Straight Line method is used for structural improvements only;
   - taxpayers can change the depreciation method upon CEO's approval;
   - there are four (4) broad categories of assets and depreciation rates;
   - for assets not included in any category, the rates are 20% (SL) and 12.5% (DV).
   - the new rates apply to all assets used in the business;
   - for assets acquired prior to the tax year 2016 that are not fully depreciated, the depreciation amount is determined by applying the new rate to the cost of the asset and should not exceed the written down value. (Refer Paragraph 26);
   - if an asset is disposed, there is no depreciation deduction in the year of disposal.

6. If a taxpayer has applied the old rates in the calculation of depreciation for the tax year 2016, the person can either submit an amended return or make adjustments in the return for the tax year 2017 (Refer Paragraph 27).

7. Taxpayers that qualify for accelerated depreciation allowance (ADA) may continue to claim the accelerated rate. This applies to the following assets :
   - buildings , plant and machinery that qualified for ADA before 01/01/16;
   - buildings completed before 31 December 2018 and which qualify for ADA;
   - plant and machinery that qualify for ADA before 31 December 2018.

8. When a person disposes of any depreciable asset acquired before or after 01/01/16, (e.g. if it is sold, transferred, no longer used etc.), no depreciation deduction is allowed for the tax year; instead the person is required to work out the amount to include in gross income (if a gain is made) or the amount to claim as a deduction (in the case of a loss). Information on the disposal of depreciable assets is covered in Practice Statement # 49.

LEGISLATIVE BASIS

9. The basic principles on the depreciation of depreciable assets is covered in Sections 31, 32 and 33 of the *Income Tax Act 2015*. Extracts of the relevant Sections are given in Attachment 1. The rates of annual depreciation are those set out in the *Income Tax (Depreciation Rates) Regulations* 2016. (Refer Attachment 2)

10. Section 1 (2) of the Act states that the new rates applies to the tax years that begin on or after 01/01/16. (Refer Paragraph 28 and Attachment 3)

11. Depreciable assets are defined in Section 2. It includes tangible personal property (such as plant and equipment) or structural improvements (e.g. buildings) if the property or improvement:
    (i) has a useful life of more than one year;
    (ii) loses value due to normal wear and tear or has become obsolete;
    (iii) is used to derive amounts included in gross income.

12. The asset must be available for use and held by that person per definition in Section 2.

13. A person is allowed a deduction in a tax year for assets that meet the requirements (Section 31 (1)).

14. A person is required to choose one of the two depreciation methods, straight line method or diminishing value method and once the election is made, that method will apply to all assets owned by the person. (Section 31 (2)).

15. For structural improvements, only the straight line method is used. The cost of a structural improvement does not include the cost of the land on which the structural improvement is situated as land does not have a limited useful life. ((Section 31 (3)).

16. A person can change their method of depreciation with the written approval of the CEO (Section 31 (4)).

17. If a depreciable asset is used partly to derive income included in gross income and partly for another purpose, the depreciation deduction is only allowed for the part of the asset used to derive income included in gross income (Section 31 (5)).

18. An adjustment is also required if a depreciable asset is used for part of the tax year. The amount of the deduction is computed according to the formula given in Section 31 (6).

> Depreciation formula for part-year use adjustment
>
> **A x B/C**
>
> where—
>
> **A** is the depreciation deduction computed under section 32 or 33 after taking into account Section 31 (5);
>
> **B** is the number of days in the tax year the asset is used in deriving income included in gross income; and
>
> **C** is the number of days in the tax year.

19. The rules for calculating a depreciation deduction is covered in Section 32 (straight-line depreciation method) and Section 33 (diminishing value depreciation method) and further guidance is given in the following paragraphs.

20. Section 34(1) provides that no claim for depreciation is made in the tax year that an asset is sold.

APPLICATION

21. The conditions that must exist to qualify for a depreciation deduction are as follows :
    - the asset must have a determinable useful life of more than one year;
    - the asset must be used or held for use in the taxpayer's business or in an income-producing activity;

- for leased property, the taxpayer may also depreciate any capital improvements for that property;
- the taxpayer can only deduct depreciation based on the business use of that property, so an adjustment must be made for personal use.

22. A depreciable asset is treated as used on a day if it is either actually used on that day or is available for use. An asset is treated as available for use on any working day or non-working day in a tax year (e.g., a Sunday or a public holiday).

23. Further guidance on the application of the straight line and diminishing value methods are given in paragraphs 24 and 25.

Straight Line Depreciation Method

24. The effect of straight-line depreciation is that the cost of a depreciable asset is deducted evenly. The total deductions allowed must not exceed the cost of the asset (Section 32 (2)).

Example 1 – Asset used wholly for business purpose

Jone acquires a computer on January 1, 2017 wholly for use in his accounting business. The computer cost $4,000. According to Schedule 3, the depreciation rate is 25%. Assuming Jone holds the asset for four tax years, the depreciation deduction for each year is $1,000 ($4000 x 25%)

2017	2018	2019	2020
$1000	$1000	$1000	$1000

Example 2 - Asset partly used for business purpose

If Jone uses the computer 75% of the time to derive gross income and 25% of the time for personal use. Assuming that Jone holds the asset for four tax years, the depreciation deduction for each year (taking into account Section 31(5)) is $750 ($4,000 x 25% x 75%).

2017	***2018***	***2019***	***2020***
$750	*$750*	*$750*	*$750*

Example 3 - Asset used for part of the year

Assume that Jone acquired the computer on July 1, 2017.

- *The depreciation deduction for the 2017 tax year is $504 (4,000 x 25% x 184/365).*
- *Jone is allowed a depreciation deduction of $1,000 in each of*

the next three tax years (2018, 2019 and 2020 tax years).

- *At the end of the 2020 tax year, Jone has been allowed total depreciation deductions of $3,504 in relation to the computer. If the computer is used for the whole of the 2021 tax year, the depreciation deduction for the year is limited to $496 ($4,000-$3504).*

2017	***2018***	***2019***	***2020***	***2021***
$504	*$1000*	*$1000*	*$1000*	*$496*

Example 4 Asset used partly for business purpose for part of the year

Assume that the computer acquired on July 1, 2017 is used by Jone only 75% of the time for use in deriving gross income with the balance of the time used for private purposes.

- *The deduction for the 2017 tax year is $378: ($4000 x 25% x 184/365) = $504, $504 x 75%.*
- *Jone is allowed a depreciation deduction of $750 ($1,000 x 75%) in each of the next three tax years, 2018, 2019 and 2020.*
- *It is necessary to take account of section 32(2) in computing the depreciation deduction for the 2021 tax year.*
- *The total deduction allowed prior to the 2021 tax year is $2,638. However, the total amount that would have been allowed but for section 31(5) would have been $3,504. This is the amount that is taken into account for the purposes of section 32(2), which means that the deduction allowed for the 2021 tax year is $372 ($496 x 75%).*

2017	***2018***	***2019***	***2020***	***2021***
$378	*$750*	*$750*	*$750*	*$372*

Diminishing Value Depreciation

25. The diminishing value depreciation method allows taxpayers to deduct a given percentage of the written down value of a depreciable asset each year. Because the written down value diminishes over time but the percentage does not change, the effect is to allow a larger deduction in the first year and decreasing deductions in subsequent years. This is based on the assumption that the decrease in value of depreciable assets caused by wear and tear is greater in the earlier years of use.

Example 1 - Asset used wholly for business purpose
On 1 January 2017, *Jone acquires drilling machinery worth $20,000 which is to be used solely in deriving mining income included in gross income. According to Schedule 3, the diminishing value rate of depreciation is 30%.*

For the 2017 tax year, the depreciation deduction is $6,000 ($20,000 x 30%). The written down value of the plant at the beginning of the 2018 tax year is $14,000 ($20,000 - $6,000) and the depreciation deduction allowed for that year is $4,200 ($14,000 x 30%). The written down value at the beginning of the 2019 tax year is $9,800 ($14,000 - $4,200).

2017	**2018**	**2019**	**2020**
$6000	$4200	$2940	$2058

Example 2 - Asset partly used for business purpose
Assume that Jone used the plant partly to derive business income included in gross income (50%) and partly to derive exempt income (50%). The depreciation deduction for the 2017 tax year is $3,000 (($20,000 x 30%) x 50%) (Sections 31(5) and 33).

According to section 33(3), the written down value of the plant at the beginning of the 2017 tax year is still $14,000 (i.e. computed on the assumption that the whole amount of the depreciation was allowed). The depreciation deduction for the 2018 tax year is $2,100 (($14,000 x 30%) x 50%). The written down value of the plant at the start of the 2019 year is still $9,800.

2017	***2018***	***2019***	***2020***	***2021***
$3000	*$2100*	*1470*	*1029*	*720.30*

Example 3 - Asset used for part of the year
Assume that Jone acquired the plant on July 1, 2017. After taking into account section 31(6), the depreciation deduction for the 2017 tax year is $3024 ($20,000 x 30% x 184/365).

Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
$3024	5093	3565	2495	1747

Example 4 - Asset used partly for business purpose for part of the year
Assume that the plant acquired on July 1, 2017 was used only 75% of the time in deriving business income included in gross income. After taking account of section 31(5) and (6), the depreciation deduction for the 2017 tax year is $2268 ($20,000 x 30% x 75% x 184/365).

Year 1	Year 2	Year 3	Year 4	Year 5
$2,268	$3,990	$3,092	$2,396	$1,857

26. The following example shows how a claim for depreciation may be reported when a person purchased assets in the years before the 2016 tax year.

Example 1 Straight Line Method

- *Co X acquired a payroll system costing $300,000 on 1st January 2015.*
- *Fiscal year ends on 31st December.*
- *Depreciation deduction will be based on the* ***depreciation rates*** *in the Income Tax (Depreciation Rates) Regulations* 2016
- *The software will be classified under computers and data handling equipment and will be depreciated at 25% using the straight line method.*

Year	Cost	Depreciation Rate	Depreciation	Accumulated Depreciation	Written Down Value
2015	$ 300,000	40%	$ 120,000	$120,000	$ 180,000
2016	$ 300,000	25%	$ 75,000	$ 195,000	$ 105,000
2017	$ 300,000	25%	$ 75,000	$ 270,000	$ 30,000
2018	$ 300,000	25%	$30,000	$ 300,000	$ 0

NB: 2018 Depreciation = $300,000 x 25% = $75,000 however claimable depreciation is only $30,000 as it is limited to the written down value.

Example 2 Diminishing Value Method

- *Using the facts in Example 1*
- *The SL depreciation rate for computer software was 40% as at 2015. From 2016 the SL rate is 25%.*
- if DV method is used (approved by the CEO) , depreciation for the first 6 years will be as follows:

Year	Cost	Written Down Value	Depreciation Rate	Depreciation	Accumulated Depreciation	Written Down Value
2015	$300,000	$300,000	40%	$ 120,000	$120,000	$180,000
2016	$300,000	$180,000	40%	$ 72,000	$ 192,000	$108,000
2017	$300,000	$108,000	40%	$ 43,200	$ 235,200	$64,800
2018	$300,000	$64,800	40%	$25,920	$ 261,120	$38,880
2019	$300,000	$38,880	40%	$15,552	$276,672	$23,328
2020	$300,000	$23,328	40%	$9,331.20	$286,003.20	$13,996.80

NB:

1. XCo can claim depreciation for the remaining years but it will be limited to the written down value of $13,996.80.
2. XCo will be required to use the DV method for all assets

27. Taxpayers who have applied the old rates in the calculation of depreciation for the tax year 2016 can either lodge an amended return and request for a review of the assessment or make adjustments in the tax return for the tax year 2017.

Example: ***Adjustment***

XCo acquired a bus (seating capacity of 30 or more passengers) for $200,000 in January 2015 for business purposes.

XCo's year ends on 31st December

Depreciation deduction will be as follows:

Year	Cost	Depreciation Rate	Depreciation	Accumulated Depreciation	Written Down Value
2015	$200,000	18%	$ 36,000	$36,000	$ 164,000
2016	$200,000	18%	$ 36,000	$ 72,000	$ 128,000
2017	$200,000	20%	$ 40,000	$ 112,000	$88,000
2017 (2016 Adjustment)	$200,000	2% (20% - 18%)	$ 4,000	$116,000	$84,000

28. The depreciation rates set out in the *Income Tax (Depreciation Rates) Regulations* 2016 applies to the tax years that begin on or after 01/01/16 (Section 1 (2) ITA).This means that:
    - taxpayers whose tax year for 2016 commences from 01/01/2016 are required to use the new rates.
    - taxpayers whose tax year for 2016 commences before 01/01/2016 are required to use the old rates in the *Income Tax (Allowance for Depreciation and Improvements Instructions 1998). This applies to the tax years that begin on* 1 August 2015, 1 September 2015, 1 October 2015, 1 November 2015 and 1 December 2015.
    - Further guidance is given in Attachment 3.

Example: 1

XCo's year commences on 1 August and ends on 31 July.

XCo acquired a bus costing $300,000 on 1 August 2014 for business purposes.

Depreciation deduction for the tax years 2015 to 2018 will be as follows:

Year	Cost	Depreciation Rate	Depreciation	Accumulated Depreciation	Written Down Value
2015	$ 300,000	18%	$ 54,000	$ 54,000	$ 246,000
2016	$ 300,000	18%	$ 54,000	$ 108,000	$ 192,000
2017	$ 300,000	25%	$ 60,000	$ 168,000	$132,000
2018	$ 300,000	25%	$ 60,000	$ 228,000	$72,000

NB:

1. *The first depreciation claim is made in the 2015 tax return (01/08/14 – 31/07/15)*
2. *XCo will use the old rate for the tax year 2016 as the period commenced on 01/08/15 (i.e. before 01/01/16)*

Example: 2

YCo acquired a bus for $300,000 on 1 January 2015 for business purposes.

YCo's year commences on 1 January and ends on 31 December.

Depreciation deduction will be as follows:

Year	Cost	Depreciation Rate	Depreciation	Accumulated Depreciation	Written Down Value
2015	$ 300,000	18%	$ 54,000	$ 54,000	$ 246,000
2016	$ 300,000	25%	$75,000	$129,000	$171,000
2017	$ 300,000	25%	$60,000	$189,000	$111,000
2018	$ 300,000	25%	$60,000	$249,000	$51,000

PROCESS

Application to change depreciation method

29. A taxpayer may apply to the CEO in writing for a change in the depreciation method for all assets. FRCA will notify the taxpayer of the decision to accept or reject the request.

30. Separate records including depreciation schedules must be kept for assets acquired before and after 01/01/16. Depreciation records must be kept for 7 years and should include the following–
    - a list of assets in respect of which depreciation is claimed;
    - their date of purchase;
    - their cost;
    - calculation of depreciation;
    - date of disposal;
    - consideration received, and
    - records of profit and loss statement and amount claimed for income tax purposes.

31. Further information can be obtained by contacting any of our Customer Enquiry centers Fiji wide or emailing info@frca.org.fj

ATTACHMENT 1

Extracts from the Income Tax Act 2015 – Section 1, 31, 32 and 33.

Short title and commencement

"**1.**—*(1) This Act may be cited as the Income Tax Act 2015.*

(2) Subject to subsection (3), this Act shall come into force on 1st January, 2016 and shall apply to tax years commencing on or after the commencement date."

Depreciation of depreciable assets

"31.—*(1) A person is allowed a deduction for a tax year for the amount by which the depreciable assets owned by the person have declined in value during the year through use in deriving income included in gross income.*

(2) Subject to subsection (3), a person may elect for the depreciation deduction allowed under subsection (1) to be computed according to the straight-line method under section 32 or the diminishing value method under section 33 and an election so made applies to all depreciable assets owned by the person.

(3) A structural improvement can be depreciated only under the straight-line method and the cost of a structural improvement does not include the cost of the land on which the improvement is situated.

(4) A person may apply, in writing, to the CEO for a change in the method of depreciation and the CEO may, by notice in writing to the applicant, approve the application subject to such conditions as the CEO may specify in the notice.

(5) If a depreciable asset is used by a person in a tax year partly to derive income included in gross income and partly for another use, the amount of the depreciation deduction allowed under subsection (1) for the year is the fair proportional part of the amount computed under section 32 or 33, as the case may be, that would be allowed if the asset were wholly used to derive income included in gross income.

(6) If a depreciable asset is not used by a person for the whole of the tax year to derive income included in gross income, the depreciation deduction for the year is computed according to the following formula—

$$A \times B/C$$

where—

A *is the depreciation deduction computed under section 32 or 33 after taking into account subsection (5);*

B *is the number of days in the tax year the asset is used in deriving income included in gross income; and*

C *is the number of days in the tax year. "*

Straight-line depreciation

"32.—*(1) Subject to section 31(5) and (6), the depreciation deduction allowed under section 31 to a person for a tax year in respect of a depreciable asset under the* *straight-line method is computed by applying the rate prescribed by Regulations made under this Act against the cost of the asset.*

(2) The total deductions allowed, or that would be allowed but for section 31(5), to a person in respect of a depreciable asset to which this section applies for the current tax year and all previous tax years must not exceed the cost of the asset."

Diminishing value depreciation

"33.*—(1) Subject to section 31(5) and (6), the depreciation deduction allowed to a person for a tax year in respect of a depreciable asset under the diminishing value method is computed by applying the rate prescribed by Regulations made under this Act against the written down value of the asset at the beginning of the year.*

(2) Subject to subsection (3), the written down value of a depreciable asset at the beginning of a tax year is—

(a) if the asset was acquired during the year, the cost of the asset; or

(b) in any other case, the cost of the asset as reduced by the total depreciation deductions allowed to the person in respect of the asset in previous tax years.

(3) If section 31(5) applies to a depreciable asset for a tax year, the written down value of the asset is computed on the basis that the asset has been used in that year solely to derive income included in gross income."

Disposal of depreciable asset

"34.— (1*) Subject to this section, if a person disposes of a depreciable asset in a tax year, the person is not allowed a depreciation deduction for the year and…"*

ATTACHMENT 2

(*Regulation 13*)

The depreciation rates are listed in Schedule 3 of the Income Tax (Depreciation Rates) Regulations 2016 (Legal Notice #2)

Asset	**Depreciation Rate**	
	Diminishing value	**Straight-line**
▪ Motor vehicles; buses and minibuses with a seating capacity of less than 30 passengers; ▪ Goods vehicles with a load capacity of less than 7 tonnes; ▪ Computers and data handling equipment ▪ Construction equipment ▪ Earthmoving equipment	40%	25%
▪ Buses with a seating capacity of 30 or more passengers ▪ Goods vehicles designed to carry or pull loads of more than 7 or more tonnes ▪ Specialised trucks; tractors; trailers and trailer-mounted containers ▪ Plant and machinery used in manufacturing, mining, or farming operations	30%	20%
▪ Vessels, barges, tugs, and similar water transportation equipment ▪ Aircraft ▪ Specialised public utility plant, equipment, and machinery ▪ Office furniture, fixtures, and equipment ▪ Any depreciable asset not included in another category	20%	12.5%
Buildings - Brick, stone or concrete - Timber buildings - Steel or steel prefabricated - Steel or steel prefabricated on copra plantations - Bures - Other		 2.5% 4% 4% 7% 15% 2.5%

- NB – for any depreciable asset that is not included in these categories the depreciation rates are 20% (SL) and 12.5% (DV).

ATTACHMENT 3

The rates of annual depreciation set out in the *Income Tax (Depreciation Rates) Regulations* 2016 applies to the tax years that begin on or after 01/01/16 (Section 1 (2) of the Act).

Tabled below is a guide on the start year for claiming the new depreciation rates.

Tax Year Commenced On	**Tax Year End**	**Tax Year**	**Depreciation Rate to be applied**
1st August, 2015	31st July, 2016	2016	Old Rate
1st September, 2015	31st August, 2016	2016	Old Rate
1st October, 2015	30th September, 2016	2016	Old Rate
1st November, 2015	31st October, 2016	2016	Old Rate
1st December, 2015	30th November, 2016	2016	Old Rate
1st January, 2016	31st December, 2016	2016	New Rate
1st February, 2016	31st January, 2017	2016	New Rate
1st March, 2016	28th February, 2017	2016	New Rate
1st April, 2016	31st March, 2017	2016	New Rate
1st May, 2016	30th April, 2017	2016	New Rate
1st June, 2016	31st May, 2017	2016	New Rate
1st July, 2016	30th June, 2017	2016	New Rate

End of Practice Statement

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