
TREASURY LAWS AMENDMENT (MEASURES FOR CONSULTATION) BILL
2023: SMALL BUSINESS ENERGY INCENTIVE

EXPOSURE DRAFT EXPLANATORY MATERIALS

DRAFT

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Glossary

This Explanatory Memorandum uses the following abbreviations and acronyms.

<i>Abbreviation</i>	<i>Definition</i>
GST	Goods and Services Tax
IT(TP) Act	<i>Income Tax (Transitional Provisions) Act 1997</i>
ITAA 1936	<i>Income Tax Assessment Act 1936</i>
ITAA 1997	<i>Income Tax Assessment Act 1997</i>

Chapter 1: *Small Business Energy Incentive*

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Outline of chapter

- 1.1 Schedule X to the Bill amends the IT(TP) Act to provide small businesses (with an aggregated annual turnover of less than \$50 million) with access to a bonus deduction equal to 20 per cent of the cost of eligible assets or improvements to existing assets that support electrification or more efficient energy use.
- 1.2 This is a temporary measure to support small businesses improve their energy efficiency and save on their energy bills. The bonus deduction applies to the cost of eligible assets and improvements up to a maximum amount of \$100,000, with the maximum bonus deduction being \$20,000.

Context of amendments

- 1.3 This measure supports small businesses to save on energy bills through incentivising the electrification of assets and improvements to energy efficiency.
- 1.4 Small businesses will have access to a 20 per cent bonus deduction for the cost of eligible depreciating assets and improvements to depreciating assets that

support electrification or more efficient energy use, up to a maximum bonus deduction of \$20,000.

- 1.5 This new tax incentive, which applies from 1 July 2023 until 30 June 2024, will help ensure small businesses share in the benefits and opportunities of the energy transition that is now underway.

Summary of new law

- 1.6 Schedule X to the Bill amends the IT(TP) Act to provide small businesses (with an aggregated annual turnover of less than \$50 million) with access to a bonus deduction equal to 20 per cent of the expenditure on eligible assets or improvements to existing assets that support electrification or more efficient energy use.
- 1.7 To be eligible for the bonus deduction:
- the expenditure must be eligible for a deduction under another provision of the tax law; and
 - the asset must be first used or installed ready for use, or the improvement cost incurred, between 1 July 2023 and 30 June 2024.
- 1.8 Certain kinds of assets and improvements are not eligible for the bonus deduction, including where the asset or improvement uses a fossil fuel.
- 1.9 Small businesses may claim up to a maximum bonus deduction of \$20,000.

Detailed explanation of new law

Entities eligible for the bonus deduction

- 1.10 The bonus deduction is available to entities that meet the definition of a small business entity under section 328-110 of the ITAA 1997. Section 328-110 defines a small business entity as an entity that carries on business with an aggregated annual turnover of less than \$10 million.
[Schedule X, item 1, paragraphs 328-470(1)(d) and (3)(d) of the IT(TP) Act]
- 1.11 The bonus deduction is also available to entities that would meet the definition of a small business entity under section 328-110 of the ITAA 1997 if the reference to \$10 million was replaced with a reference to \$50 million.
[Schedule X, item 1, paragraphs 328-470(1)(d) and (3)(d) and subsection 328-470(4) of the IT(TP) Act]
- 1.12 Small businesses are eligible for the bonus deduction if they meet these requirements in the income year in which the asset is first used or installed, or the improvement cost is incurred.
[Schedule X, item 1, paragraphs 328-470(1)(d) and (3)(d) of the IT(TP) Act]

Costs eligible for the bonus deduction

- 1.13 To be eligible for the bonus deduction, a cost must be for an eligible depreciating asset first used or installed, or an eligible improvement to a depreciating asset for which the cost is incurred, between 1 July 2023 and 30 June 2024. The cost must be able to be deducted under another provision of the tax law.

Bonus period

- 1.14 An entity can only claim the bonus deduction for the cost of depreciating assets first used or installed for any purpose, or the improvement cost incurred, between 1 July 2023 and 30 June 2024 ('the bonus period').
[Schedule X, item 1, paragraph 328-470(1)(c) and (3)(c) of the IT(TP) Act]

Depreciating assets

- 1.15 A depreciating asset is eligible for the bonus deduction if it:
- uses electricity and there is a new reasonably comparable asset that uses a fossil fuel available in the market;
 - uses electricity and is more energy efficient than the asset it is replacing or, if it is not a replacement, a new reasonably comparable asset available in the market; or
 - is an energy storage, demand management or efficiency-improving asset.

[Schedule X, item 1, paragraph 328-470(1)(e) and subsection 328-470(2) of the IT(TP) Act]

Assets that use electricity instead of a fossil fuel

- 1.16 An asset is eligible for the bonus deduction if there is a new reasonably comparable asset that uses a fossil fuel available in the market, and the asset instead uses electricity.
[Schedule X, item 1, paragraph 328-470(2)(a) of the IT(TP) Act]
- 1.17 For example, if a business installs an electric reverse cycle air-conditioner in place of a gas heater and uses it for a taxable purpose, the business could claim a bonus deduction for the cost of that air-conditioner as it uses electricity and a fossil fuel alternative is available in the market.
- 1.18 The asset must be reasonably comparable to a new asset that uses a fossil fuel available in the market at the time it is first used or installed ready for use for any purpose. An asset will not qualify for the bonus deduction if the only reasonably comparable asset that uses a fossil fuel is a second-hand asset.

Assets that use electricity more efficiently

- 1.19 An asset that uses electricity may be eligible for the bonus deduction even if there is no comparable asset available on the market which uses a fossil fuel. In this case, the energy efficiency of the asset will determine its eligibility.
[Schedule X, item 1, paragraphs 328-470(2)(b) of the IT(TP) Act]
- 1.20 If the asset is replacing another depreciating asset, it must be more energy efficient than the asset it is replacing.
[Schedule X, item 1, subparagraph 328-470(2)(b)(iii) of the IT(TP) Act]
- 1.21 If the asset is not replacing another asset, then it must be more energy efficient than a new reasonably comparable asset available in the market at the time it is first used or installed ready for use for any purpose. The comparable asset cannot be a second-hand asset.
[Schedule X, item 1, subparagraph 328-470(2)(b)(iv) of the IT(TP) Act]
- 1.22 For example, if a business installs a refrigerator (when it previously did not have one) and uses it for a taxable purpose, the business could only claim the bonus deduction if the purchased refrigerator is more energy efficient than another comparable refrigerator available in the market. In this case, the business could use the Energy Rating Label to compare energy efficiency.

Assets that facilitate energy storage, efficiency or demand management

- 1.23 Demand management and enabling assets may also be eligible for the bonus deduction.
[Schedule X, item 1, paragraph 328-470(2)(c) of the IT(TP) Act]
- 1.24 An asset that allows another asset (the affected asset) to be more energy efficient is also eligible for the bonus deduction, provided the affected asset is not an excluded asset.
[Schedule X, item 1, subparagraph 328-470(2)(c)(i) of the IT(TP) Act]
- 1.25 An asset may be eligible for the bonus deduction if it enables the storage of electricity, or the storage of energy that is generated from a renewable source. For example, a battery that stores electricity may be eligible for the bonus deduction. Similarly, a thermal storage system that can store heat or cold from a renewable source, such as a solar thermal hot water system may be eligible for the bonus deduction.
[Schedule X, item 1, subparagraph 328-470(2)(c)(ii) of the IT(TP) Act]
- 1.26 An asset can also qualify for the bonus deduction if it allows energy to be consumed at a different time. For example, a time-shifting device that allows electric appliances to be operated at off-peak hours may be eligible for the bonus deduction.
[Schedule X, item 1, subparagraph 328-470(2)(c)(iii) of the IT(TP) Act]
- 1.27 An asset can also qualify for the bonus deduction if it enables energy use to be monitored. For example, a data logging device attached to a regular utility meter that enables a business to better measure their energy consumption may be eligible for the bonus deduction.
[Schedule X, item 1, subparagraph 328-470(2)(c)(iv) of the IT(TP) Act]

Improvements

- 1.28 In addition to newly-acquired depreciating assets, improvements to existing depreciating assets may also be eligible for the bonus deduction.
- 1.29 An improvement to a depreciating asset is eligible if it:
- enables the asset to use electricity instead of fossil fuels.
 - enables the asset to be more energy efficient; or
 - facilitates energy storage, demand management or monitoring.

[Schedule X, item 1, paragraph 328-470(3)(e) of the IT(TP) Act]

Improvements enabling electricity use

- 1.30 An improvement that allows an asset to only use electricity, or to use energy generated from a renewable source may be eligible for the bonus deduction if, prior to the improvement, the asset could use energy from a fossil fuel.
- [Schedule X, item 1, subparagraph 328-470(3)(e)(i) of the IT(TP) Act]*
- 1.31 For example, an electric motor may be eligible for the bonus deduction if it replaces a diesel engine in an asset, allowing that asset to only use electricity.

Improvements to energy efficiency

- 1.32 An improvement that allows the asset to be more energy efficient may be eligible for the bonus deduction, provided the asset being improved uses electricity or energy generated from a renewable source.
- [Schedule X, item 1, subparagraph 328-470(3)(e)(ii) of the IT(TP) Act]*
- 1.33 For example, a variable speed drive fitted to an existing electric motor may be eligible for the bonus deduction.

Improvements facilitating energy storage, demand management or monitoring

- 1.34 An improvement that allows for energy use by an asset to be monitored, reduced at specific times, or confined to specific times may be eligible for the bonus deduction, provided the asset being improved uses electricity or energy generated from a renewable source.
- [Schedule X, item 1, subparagraphs 328-470(3)(e)(iii)-(v) of the IT(TP) Act]*
- 1.35 For example, a switchboard-mounted device that enables the shifting of loads from peak times to off-peak times may be eligible for the bonus deduction.

Cost used to calculate the bonus deduction must be able to be deducted under another taxation provision

- 1.36 In order to claim the bonus deduction for an amount of expenditure, the entity must be able to deduct the eligible expenditure under another provision of the taxation law, regardless of which income year or income years in which they

claim the deduction.

[Schedule X, item 1, paragraphs 328-470(1)(b) and (3)(b) of the IT(TP) Act]

- 1.37 Generally, the cost of an asset can only be deducted to the extent that that asset is used for a taxable purpose. For example, under Division 40 of the ITAA 1997, an entity can deduct an amount equal to the decline in value of a depreciating asset and this amount must be reduced to the extent that the decline in value is attributable to the asset being used or installed ready for use, for a purpose other than a taxable purpose.
- 1.38 Therefore, if expenditure is for multiple purposes (e.g. a mix of private and business use), the bonus deduction will only apply to the proportion of the expenditure that is for a taxable purpose.

The deductions operate as bonus deductions under the ITAA 1997

- 1.39 The amendments provide that the bonus deduction provisions have effect as if they were provisions of Division 25 of the ITAA 1997. This does not affect the requirement that the eligible expenditure must be able to be deducted under another taxation provision.
[Schedule X, item 1, subsection 328-465(2) of the IT(TP) Act]
- 1.40 Division 25 sets out amounts you can deduct under the ITAA 1997. Deductions set out in Division 25 are specific deductions under section 8-5 of the ITAA 1997. The bonus deduction introduced by these amendments will therefore be considered a specific deduction, ensuring it can be taken into account as a deduction when computing taxable income.
- 1.41 The amendments provide that section 8-10 of the ITAA 1997 (about no double deductions) does not prevent a taxpayer from claiming the bonus deduction.
[Schedule X, item 1, subsection 328-465(3) of the IT(TP) Act]
- 1.42 Section 8-10 specifies that when multiple provisions of the ITAA 1997 allow for deductions in respect of the same amount, the taxpayer can deduct only under the provision that is most appropriate. The deduction introduced by these amendments is a bonus deduction, where the same expenditure provides eligibility for the original deduction as well as the bonus deduction. The amendments clarify that section 8-10 of the ITAA 1997 does not apply to the bonus deduction to ensure that the bonus deduction can be claimed in addition to the ordinary deduction.
- 1.43 The amendments also provide that section 40-215 of the ITAA 1997 does not prevent a taxpayer from claiming the bonus deduction.
[Schedule X, item 1, subsection 328-465(3) of the IT(TP) Act]
- 1.44 Section 40-215 provides that each element of the cost of a depreciating asset is reduced by any portion of that element of cost that is deducted, can be deducted, or will be taken into account when working out the amount that can be deducted, other than under Division 40, 41 or 328. The deduction introduced by these amendments is a bonus deduction, where the same expenditure provides eligibility for the original deduction as well as the bonus deduction. The amendments clarify that using the cost of an asset to calculate

the bonus deduction amount does not reduce the amount of that cost that may be deducted under Division 40.

- 1.45 The amendments also provide that section 355-715 of the ITAA 1997 does not prevent a taxpayer from claiming the bonus deduction.

[Schedule X, item 1, subsection 328-465(3) of the IT(TP) Act]

- 1.46 Section 355-715 specifies that where a taxpayer is entitled to a notional deduction under the Research and Development Tax Incentive regime and another deduction under the tax law, then the taxpayer is only entitled to the notional Research and Development deduction, and not the other deduction. The notional Research and Development deduction is used to calculate a tax offset.

- 1.47 The deduction introduced by these amendments is a bonus deduction, where the same expenditure provides eligibility for the original deduction as well as the bonus deduction. Therefore, if expenditure is eligible for both the Research and Development Tax Incentive and the bonus deduction, the taxpayer may claim both the bonus deduction and the tax offset. The bonus deduction will not affect the amount of the tax offset.

Exclusions

- 1.48 Some types of assets and expenditure are ineligible for the bonus deduction even where they would otherwise meet the requirements. These are:

- assets, and expenditure on assets, that can use a fossil fuel;
- assets which have the sole or predominant purpose of generating electricity (such as solar panels);
- capital works;
- motor vehicles (including hybrid and electric vehicles) and expenditure on motor vehicles;
- assets and expenditure on an asset where expenditure on the asset is allocated to a software development pool; and
- financing costs, including interest, payments in the nature of interest and expenses of borrowing.

[Schedule X, item 1, paragraphs 328-470(1)(f) and (2)(f), subsection 328-470(6) of the IT(TP) Act]

- 1.49 Other incentives are available for electric and hybrid vehicles and renewable electricity generation and these are not eligible for the bonus deduction.

Assets that can use a fossil fuel

- 1.50 If an asset can use a fossil fuel, then that asset and any expenditure on that asset is not eligible for the bonus deduction, unless that use is merely incidental.

[Schedule X, item 1, paragraphs 328-470(6)(a) and (b) of the IT(TP) Act]

- 1.51 This is the case even if, in practice, the asset predominantly or solely uses electricity, or other energy that is generated from a renewable source. For example, if a solar hot water system uses gas to heat water when there is no solar-heated water available, that hot water system is not eligible for the bonus deduction.
- 1.52 The only exception to this exclusion is an improvement that allows an asset to only use electricity, or other energy that is generated from a renewable source. For example, an improvement to the gas and solar hot water system mentioned above would be eligible for the bonus deduction if that improvement allowed the system to use electricity and not gas to heat additional water.
[Schedule X, item 1, paragraph 327-470(6)(b) of the IT(TP) Act]

Balancing adjustment events

- 1.53 An entity cannot claim the bonus deduction for the cost of a depreciating asset, or an improvement to a depreciating asset, if any balancing adjustment event occurs to the asset while the entity holds it during the relevant time period, unless the balancing adjustment event is an involuntary disposal. This means, for example, that an entity cannot claim the bonus deduction if it sells the asset within the bonus period.
[Schedule X, item 1, paragraphs 328-470(1)(g) and (3)(g) of the IT(TP) Act]

Calculating and claiming the bonus deduction

20 per cent of eligible cost

- 1.54 The amount of the bonus deduction is calculated as 20 per cent of the total eligible cost, up to a maximum bonus deduction of \$20,000 across the bonus period.
[Schedule X, item 1, subsection 328-465(1) of the IT(TP) Act]
- 1.55 This applies regardless of how the entity calculates any other deductions in respect of the expenditure.
- 1.56 The bonus deduction is a one-off bonus deduction that does not affect any other deductions in the taxation law.
- 1.57 The requirement that expenditure is deductible under a taxation provision means that there are certain exclusions to eligible expenditure. For example, if a business is registered for GST, and the expenditure is not for a GST-free supply, the bonus deduction is calculated on the amount of expenditure less the GST amount claimable as an input tax credit. The GST component of expenditure that is claimed as an input tax credit is not deductible in accordance with section 27-5 of the ITAA 1997.
- 1.58 When calculating the bonus deduction for the cost of an asset or improvement to an asset, it is assumed that the entity will continue to hold the asset throughout its effective life; and:

- if the bonus deduction is for the cost of an asset, the entity will use it for a taxable purpose to the same extent that it does in the income year it first uses or installs the asset for a taxable purpose; or
- if the bonus deduction is for expenditure on an improvement, the entity will use it for a taxable purpose to the same extent that it does in the income year in which the expenditure is incurred.

[Schedule X, item 1, subsection 328-470(5) of the IT(TP) Act]

Eligible cost for assets

1.59 For assets first used or installed during the bonus period, expenditure that is included in the first element of cost may be eligible for the bonus deduction.
[Schedule X, paragraph 328-470(1)(a) of the IT(TP) Act]

1.60 Generally, the first element of cost is the cost associated with beginning to hold an asset. That is, the cost of purchasing and installing the asset.

Timing of first use or installation

1.61 The first element of cost of an asset may be eligible for the bonus deduction if that asset is first used or installed ready for use for any purpose during the bonus period.
[Schedule X, item 1, paragraph 328-470(1)(c) of the IT(TP) Act]

1.62 This means that, if an entity first uses or installs an asset before 1 July 2023, the entity cannot claim a bonus deduction for the first element of cost of the asset. This is the case even if the entity does not use the asset for a taxable purpose until after 1 July 2023.

1.63 Due to the general deduction rules for depreciating assets under Division 40 of the ITAA 1997, an entity can only claim a deduction for the cost of a depreciating asset to the extent that it uses the asset for a taxable purpose. An entity can only claim a bonus deduction for expenditure that would otherwise be able to be deducted, so the bonus deduction can only be claimed on the first element of cost to the extent the asset is used for a taxable purpose.
[Schedule X, item 1, paragraph 328-470(1)(b) of the IT(TP) Act]

Eligible cost for improvements

1.64 Expenditure on the part of the second element of cost of an asset worked out under paragraph 40-190(2)(a) of the ITAA 1997 may be eligible for the bonus deduction. The second element of cost under paragraph 40-190(2)(a) of the ITAA 1997 is the amount paid or taken to have been paid to bring an asset to its present condition and location since the entity started to hold the asset.
[Schedule X, item 1, paragraph 328-470(3)(a) of the IT(TP) Act]

1.65 The second element of cost of an asset can only be claimed if it allows the asset to be more energy efficient, able to store energy, monitor energy use, use energy at a different time, or enable the asset to run solely on electricity or

renewable energy. This therefore captures the cost of eligible improvements to an asset.

[Schedule X, item 1, paragraph 328-470(3)(e) of the IT(TP) Act]

- 1.66 The expenditure on the improvement must be incurred during the bonus period. The time that the improvement or the asset being improved is used or installed is not relevant.

[Schedule X, item 1, paragraph 328-470(3)(c) of the IT(TP) Act]

- 1.67 The cost of an improvement to an asset can be claimed for assets first used or installed before or during the bonus period. This means that if an entity first uses or installs an asset during the bonus period, and also improves the asset during the bonus period, it can claim the bonus deduction for the first element of cost of the asset and for the cost of the improvement.

Example 1.1 Claiming the bonus deduction for a small business entity that makes an eligible improvement

Note that in all the worked examples, it is assumed that each business is registered for GST and costs are net of GST input tax credit entitlements.

A Co Pty Ltd (A Co) is a small business entity with a normal accounting period (1 July to 30 June). On 15 July 2023, A Co purchases and installs ten variable speed drives that it fits to existing electric motors that it owns and uses in its business for a cost of \$50,000. The variable speed drive enables each motor to run more efficiently.

The expenditure on each variable speed drive is an eligible improvement to a depreciating asset. A Co can therefore claim a bonus deduction of \$10,000 (20 per cent of \$50,000).

Depreciation deductions that A Co can claim for the amount included in the second element of the cost of the existing electric motors (\$50,000) are not altered by the bonus deduction.

Depreciation and the instant asset write-off

- 1.68 Under the existing taxation law, for depreciating assets, small business entities with aggregated annual turnover of less than \$10 million that use the simplified depreciation regime generally either deduct the cost of a depreciating asset in one income year, or place the asset in the simplified depreciation pool and depreciate it at set rates over time (under the instant asset write-off in Subdivision 328-D of the ITAA 1997 and section 328-100 of the IT(TP) Act).
- 1.69 Alternatively, small businesses can opt out of the simplified depreciation regime and instead deduct the decline in value of the asset over its effective life (under the uniform capital allowance regime in Division 40 of the ITAA 1997).
- 1.70 Entities with aggregated annual turnover of at least \$10 million and less than \$50 million can also deduct the decline in value of the asset over its effective life under Division 40 of the ITAA 1997.

- 1.71 The bonus deduction is equal to 20 per cent of the eligible first and second element costs worked out under the incentive. This means that regardless of the method of deduction that the entity takes (i.e. whether immediate or over time), the bonus deduction in respect of a depreciating asset is calculated based on the asset's cost.

Timing for claiming the bonus deduction

- 1.72 For depreciating assets first used or installed during the bonus period, entities must claim the bonus deduction in the income year in which the asset is first used or installed.
- 1.73 For improvements made to existing assets, entities must claim the bonus deduction in the income year in which the improvement cost is incurred.
- 1.74 This applies even if an entity has a substituted accounting period with an income year beginning before 1 July 2023 (i.e. it is an 'early balancer') or after 1 July 2023 (i.e. it is a 'late balancer').
- 1.75 Early and late balancers may claim the bonus deduction across more than one income year, provided the eligible asset was first used or installed, or the improvement cost was incurred, during the bonus period.

Example 1.2 Claiming the bonus deduction for a small business entity with a substituted accounting period

B Co Pty Ltd (B Co) is a small business entity with a substituted accounting period of 1 January to 31 December.

2023-24 income year (1 January 2023 to 31 December 2023)

On 1 August 2023, B Co purchases two commercial ride-on electric lawnmowers for a cost of \$70,000. The assets are delivered on 5 August 2023 and B Co starts to use them immediately. At the time of first use, new diesel-powered lawnmowers are available in the market.

The expenditure included in the first element of cost of each asset is \$35,000. B Co can claim a bonus deduction of \$14,000 (20 per cent of \$70,000) in its 2023-24 income tax return. Depreciation deductions that B Co can claim for the electric lawnmowers are not altered by the bonus deduction.

2024-25 income year (1 January 2024 to 31 December 2024)

On 10 March 2024, B Co purchases a new industrial air conditioning unit for a cost of \$15,000. The asset is installed on 21 March 2024. It is more energy efficient than the older unit that it is replacing.

The expenditure included in the first element of the cost of the asset is \$15,000. B Co can claim a bonus deduction of \$3,000

(20 per cent of \$15,000) in its 2024-25 income tax return. Depreciation deductions that B Co can claim for the air conditioning unit are not altered by the bonus deduction.

In total, B Co can claim \$17,000 in bonus deductions for the electric lawnmowers and air conditioning unit over the bonus period, which is below the maximum bonus deduction of \$20,000.

Cap on the bonus deduction

- 1.76 The total expenditure eligible for the bonus deduction is effectively \$100,000 over the bonus period such that entities can claim a maximum bonus deduction of \$20,000.
[Schedule X, item 1, subsection 328-465(1) of the IT(TP) Act]
- 1.77 The cap on the bonus deduction works on a cumulative basis in respect of the eligible costs. An entity may purchase multiple eligible assets or improvements. The cap operates to limit the bonus deduction to a maximum of \$20,000.
- 1.78 The cap is a limit on the total bonus deduction that may be claimed, even where the bonus deduction is claimed across more than one income year (such as for early or late balancers). If an entity can claim the bonus deduction across more than one income year, then the amount of the bonus deduction it can claim in a subsequent income year is reduced by any amount claimed in the previous income year.
[Schedule X, item 1, paragraph 328-365(1)(b) of the IT(TP) Act]

Commencement, application, and transitional provisions

- 1.79 The amendments commence on the first 1 January, 1 April, 1 July or 1 October to occur after the day the Act receives Royal Assent.
- 1.80 The amendments apply to eligible assets first used or installed, and eligible improvement costs incurred, between 1 July 2023 and 30 June 2024.
[Schedule X, item 1, paragraphs 328-470(1)(c) and (3)(c) of the IT(TP) Act]
- 1.81 The amendments apply retrospectively from 1 July 2023. The changes are wholly beneficial to entities incurring expenditure affected by these amendments.