

Motor vehicle expenditure.

Changes to the motor vehicle expenditure of Close Companies

A key change brought about as a result of the **Taxation (Business Tax, Exchange of Information, and Remedial Matters) Act** is an update on the current rules regarding the motor vehicle expenditure of close companies. The current rules for close companies who provide a motor vehicle for private use of shareholder-employees result in the requirement to register and pay FBT on the value of the benefit provided. The amendment to the rules allows certain close companies to elect to use the motor vehicle expenditure rules (e.g. logbook) previously not available to companies, rather than paying FBT on the value provided to shareholder-employees. The amendment comes into force for the 2017-18 and later income years.

What is a Close Company?

A close company is a company which (at a particular time) has five or less natural persons (or trustees from 28 March 2018) whose combined voting interests in the company are greater than 50%. All natural persons who are associated will be treated as one natural person. Care should be taken when dealing with close companies which have trusts as shareholders prior to 28 March 2018 as technically these would not be close companies.

What is a shareholder-employee?

A shareholder-employee is a person who is a shareholder in a company and is also receives (or is entitled to receive) salary, wages or another form of income with or without PAYE.

Old motor vehicle rules for Close Companies

Previously when a close company provided a motor vehicle for private use to a shareholder-employee, the company was required to register and pay FBT on the value of the benefit provided. The value was based on the availability of the vehicle rather than the actual private use by the shareholder employee.

The issue with the old rules

The old rules resulted in high compliance costs for close companies because of the requirement to register and pay FBT. Sole traders and partners in a partnership who used a motor vehicle in a similar way were not required to register and pay FBT. Instead they could apportion the expenditure between business and private use. This meant there were different treatments of a very similar situation which arose only due to the different entities involved.

New motor vehicle rules for Close Companies

When a motor vehicle is made available to a shareholder-employee of a close company, the company is now able to elect to use the motor vehicle expenditure rules previously only available to sole traders and partnerships which apportion the expenditure between business and private use. The close company will then use the proportion of the business use of the vehicle to calculate the amount of their deduction for motor vehicle expenditure. This includes the business proportion of depreciation and interest costs arising from a loan or hire purchase agreement.

The issue with the new rules

The election will only apply to new motor vehicle arrangements between close companies and shareholder-employees (arrangements entered into after the start of the 2017 income year) and will continue to apply until the close company disposes of the motor vehicle. Only close companies where the sole fringe benefit is the provision of one or two motor vehicles to shareholder-employees (for their private use) may elect to use the apportionment rules.

Notice

In order to use the new rules for a particular vehicle, notice must be given to the Commissioner before the Fringe Benefit return is due for the period in which the benefit is first provided.

Example

Brad owns 70% of Brad's Design Ltd which is a close company and has a balance date of 31 March. Brad is also an employee of the company. On 1 April 2017, the company provides Brad with a motor vehicle to use for both business and private use. It is expected that Brad's business use of the vehicle will be 60% for the 2017 financial year. The total motor vehicle expenditure for the year is estimated to be \$5,000 including GST. The cost price of the vehicle is \$25,000 including GST.

Under the old rules

The company would pay FBT on the availability for private use of the vehicle. As the vehicle is available for the whole year the value of the fringe benefit is \$5,000 (20% x Cost) and thus an FBT liability of \$2,463 (using a rate of 49.25%) plus GST of \$652. The company will be entitled to claim the full vehicle costs (\$4,348 net of GST) and depreciation (\$6,521) for the year as well as GST on the purchase price (\$3,261) and running costs (\$652).

Under the new rules

As this is a new arrangement (entered into during the 2017 financial year), the company can elect to use the motor vehicle expenditure apportion rules where the company can use the proportion of business use of

the vehicle by Brad to apportion the deductible motor vehicle expenditure. This method results in \$2,608 being deductible motor vehicle expenditure for the company net of GST and \$3,912 of depreciation. GST is claimable on the deductible portion of expenditure when the log book or actual cost method is used. In this case \$391 would be claimable ($\$3,000 \times 3 / 23$.) GST would also be claimed on the purchase price of \$1,956 ($\$25,000 \times 3 / 23 \times 60\%$.)

Tax Position	Year 1		Year 2	
	FBT	New Rules	FBT	New Rules
Deductible Costs				
FBT	3,115	-	3,115	-
Running Costs	4,348	2,608	4,348	2,608
Depreciation	6,521	3,912	4,565	2,739
	13,984	6,520	12,028	5,347
Tax Benefit at 28%	3,915	1,826	3,368	1,497
GST Claimable				
Purchase Price	3,260	1,956	-	-
Running Costs	652	391	652	391
GST Benefit	3912	2347	652	391
FBT to pay	(3,115)	-	(3,115)	-
Cash Benefit	4,712	4,173	905	1,888

Implications

In the past, there was a choice between whether a company should own the motor vehicle and pay FBT on any private use or have the employee own the vehicle and reimburse them for any business use. The disadvantage of reimbursement was the inability to claim GST on the purchase price, however as the purchase price increases FBT becomes a significant cost.

The new rules mean the benefit of no FBT can be achieved through the apportionment method while still allowing a particular GST claim. This provides a better outcome for higher value vehicles with business use.

Disclaimer: Every effort has been made to ensure the material provided is up to date at the time of publication. However, the information provided is general in nature and should not be used as a substitute for written professional advice. No responsibility is taken for updating this material from the date of publication (June 2018).

PolsonHiggs

Business advisors

139 Moray Place, Dunedin 9016

PO Box 5346, Dunedin 9058

Phone 03 477 9923

ph.co.nz