

Proposed changes to the method of calculating Fringe Benefits Tax on motor vehicles

By Albert Gigl, MW Partners (insert photo of Albert)

The announcement by Prime Minister Kevin Rudd to change the method of calculating fringe benefits tax on motor vehicles will have far reaching affects if the proposals are legislated.

FBT is a tax paid by the employer on the value of benefits provided to employees. This means the value of the benefit is free from income tax to the employee.

FBT affects dentists employed in the public health system as a leased motor vehicle often forms part of their salary package. The proposed changes on these dentists will mean that the effective cost of providing the motor vehicle will increase, absorbing more of the packaged benefits thereby leaving less of the salary package available for other incentives. As the cost will vary significantly dependent upon the employee dentists' circumstances it is not proposed to discuss this matter any further in this article.

The proposed change will have a significant impact on dentists who operate their dental surgery through a corporate entity or trust and that entity owns or leases a motor vehicle that is provided to the dentist, the dentist's spouse, an associate (e.g. a relative) or an employee.

Methods of calculating

There are two methods for calculating FBT. The first one is the operating cost method whereby all the costs of operating the motor vehicle (fuel, registration, insurance, depreciation, interest and leasing costs) are accumulated and then multiplied by the private use proportion as evidenced by the motor vehicle log book. The second method is a statutory formula whereby the cost of the motor vehicle is multiplied by a statutory percentage determined by the total kilometres travelled by the motor vehicle.

Most dental practitioners will probably be unaware of the FBT on their motor vehicle as a calculation is usually done by their accountant and an adjustment is made in their financial statements/tax return to allow for the FBT by making what is termed "an employee contribution". The employee contribution is effectively a re-imbusement of the benefit/expense provided. This means that it is unnecessary to lodge an FBT tax return or to pay the FBT separately. Usually, dental practitioners will have a very low business use percentage for their motor vehicle and therefore using a log book and the operating method will result in a very low tax deduction as well as a high FBT liability. Travel between the dentists home and the surgery is normally considered private and therefore the only true business use will be travel from the surgery to lab/home

visit/another surgery etc. Typically this will only result in five to 10 per cent of business use.

Due to the low business use, dental practitioners will almost always use the statutory method to calculate their FBT and it is this method which the Government proposes to be abolished. Prior to the 2011 Budget, the statutory formula percentages ranged from 7% to 26% dependent upon the number of kilometres travelled. The percentage range is being standardised so that from 1 April 2014, irrespective of the number of kilometres travelled, all motor vehicles using the statutory formula will be at a 20% rate.

The following examples show two motor vehicles and the FBT calculation using both the statutory method and the operating method. For the purposes of this exercise GST has been ignored. The first motor vehicle is a Ford purchased for \$50,000 and the second motor vehicle is a BMW purchased for \$120,000. Both motor vehicles travel 25,000 km per year and the maximum business use is 10%.

1. TAX DEDUCTIBLE EXPENSES

	<u>FORD</u>	<u>BMW</u>
Fuel	\$ 4,500.00	\$ 4,500.00
Registration	\$ 600.00	\$ 600.00
Insurance	\$ 900.00	\$ 1,400.00
Repairs, Maintenance, Service	\$ 1,000.00	\$ 2,000.00
Depreciation (25%)	\$ 12,500.00	\$ -
Depreciation (\$30,000) Luxury Cost Limit	-	\$ 14,368.00
Interest (6.45%)	\$ 3,225.00	-
Interest (\$7,740) Luxury Cost Limit	-	\$ 3,707.00
Tax Deduction Allowed	\$ 22,725.00	\$ 26,575.00

2. STATUTORY FORMULA

Ford \$50,000 @ 20%	\$ 10,000.00	-
BMW \$120,000 @20%	-	\$ 24,000.00

	\$	\$
FBT Cost/Employee Contribution	10,000.00	24,000.00

3. OPERATING COST METHOD

	\$	
Ford 90% x \$22,725	20,453.00	-
BMW 90% x \$26,575	-	\$ 23,918.00
BMW 90% x Luxury Cost Limit Adjustment	-	\$ 17,699.00
	\$	\$
FBT Cost/Employee Contribution	20,453.00	41,617.00

Under the statutory formula method the amount of employee contribution required to completely eliminate any FBT is \$10,000 for the Ford and \$24,000 for the BMW. If this method is abolished, the dental practitioner will have no choice other than to use the operating cost method which in the example above increases the FBT cost/employee contribution to \$20,453 for the Ford and \$41,617 for the BMW. In both cases the cost has approximately doubled and in the case of the BMW the amount of FBT reimbursement (\$41,617) exceeds the tax deduction allowed (\$26,575).

Greater administration

Using the operating cost method also imposes a greater administration burden as the calculation requires both a log book to be kept as well as a record of all expenses relating to each motor vehicle. These expenses vary from year to year and therefore it is more difficult to calculate in advance the amount of employee contribution required. The FBT calculation under the statutory formula method only requires the cost of the motor vehicle and the amount of FBT is the same year after year.

It is important to note that while the proposed changes target leased vehicles, any motor vehicle that is subject to finance or owned outright by a corporate entity/trust will be caught. Any motor vehicle owned, leased or financed by a sole trader, contractor or individual is **not** affected by the proposed change.

This article has been written on the behalf of the ADAVB by Albert Gigl, of MW Partners, Chartered Accountants. If you are concerned about how these proposed changes to FBT on motor vehicles will affect you, call (03)8825 5400 and speak to an accountant from MW Partners.