USING AN ASSOCIATE LEASE TO BOOST FAMILY INCOME

FRINGE BENEFITS TAX

An associate lease is a **tax effective way** to acquire a vehicle while boosting the income earned by the family.

HOW THIS IS **ACHIEVED**

The following 4 steps outline how this is achieved:

1. An associate of an employee (i.e., usually their spouse) purchases a car from an arm’s length party using their own cash reserves;
2. The associate then leases the car to the employee’s employer, who then provides the same car back to the employee as a car fringe benefit. Any FBT payable in relation to the car fringe benefit is calculated in the usual way under either the Operating cost or Statutory formula method; and
3. The employee is required to salary sacrifice the GST-exclusive amount of any car expenses (including the lease or other payments made to the associate of the employee), as well as any FBT that is payable by the employer in relation to the car fringe benefit; and
4. The associate of the employee then includes any lease (or other related) payments made to them by the employer as assessable income and claims the appropriate deductions with respect to the leased car against this income.

The **flow of transactions required** to execute the associate lease, is illustrated below:

EMPLOYER

Leases car from associate

**1 Novated Lease**

between Associate & Employer

**2 Car Benefit**

provided to Employee

**3 Net Lease Payment** salary sacrificed

**4 Salary Sacrificed Amounts** paid to Associate as Lease Payment

MEET **JERRY AND BETH**

The best way to show how an associate lease can boost family income is with an example, meet Jerry and his wife Beth below.

**Assumptions**

|  |  |
| --- | --- |
| DETAIL | AMOUNT |
| Salary & Wage Income – Beth (Wife) | $200,000 |
| Salary & Wage Income – Jerry (Husband) | $30,000 |
| Interest Income – Jerry (based on 2.5% of $100,000 term deposit) | $2,500 |
| **Car Details** |  |
| Purchase price | $40,000 |
| Depreciation (year one) | $6,000 |
| Lease Amount (per annum - GST Exclusive) | $7,500 |
| **Running Costs** (per annum) |  |
| Fuel | $5,200 |
| Registration | $800 |
| Insurance | $1,000 |
| Repairs & Maintenance | $1,500 |
| **Total Running Costs** (per annum) | **$8,500** |

For working out the benefits of the associate lease we will assume that **Beth & Jerry** have no other deductions to offset against their salary and wage income.

**Outcomes**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | STANDARD NOVATED LEASE | | ASSOCIATE LEASE | |
| DETAIL | BETH | JERRY | BETH | JERRY |
| Salary & Wage Income | $200,000 | $30,000 | $200,000 | $30,000 |
| Add: Lease Income Received | - | - | - | 7,500 |
| Add: Interest Income | - | $2,500 | - | $1,500 |
| **Total Income** | **$200,000** | **$32,500** | **$200,000** | **$39,000** |
| Less: Salary Sacrificed Lease Payments | $7,500 | - | $7,500 | - |
| Less: Depreciation on car | - | - | - | 6,000 |
| **Taxable Income** | **$192,500** | **$32,500** | **$192,500** | **$33,000** |
| Tax Expense | $63,707 | $2,922 | $63,707 | $3,027 |
| Less: Tax Withheld by Employer | $67,232 | $2,842 | $67,232 | $2,842 |
| Tax Refund / (Payable) | $3,525 | ($80) | $3,525 | ($185) |
| **After Tax Income** | **$128,793** | **$29,578** | **$128,793** | **$35,976** |
| **Combined After Tax Income** | **$158,371** | | **$164,769** | |

IMPACT ON JERRY, THE ASSOCIATE

Whilst **Jerry’s** interest income has reduced (to reflect the $40,000 spent on buying the new car) the after-tax income for the group is $6,398 higher by executing the associate lease. This is because the return on leasing the car is higher than the return achieved by investing in the term deposit.

As the car is being used to generate assessable income (i.e. lease income), depreciation of the car becomes a deduction for Jerry to offset against his income.

We do want to point out that the general tax avoidance provisions in Part 4a may be applied to this strategy. However, the example above clearly illustrates that the primary reason for executing this strategy was to maximise after tax cash flows so in our opinion is outside the scope of Part 4a.

However, if **Jerry** obtained arm’s length finance to purchase the car, Part 4a may apply, because the lease income he received would be simply on paid to his finance company. As such, there would be no significant increase in after tax cash flows, just the tax benefits.

IMPACT ON BETH, THE EMPLOYEE

The last thing to address for Jerry and Beth is the FBT impact on **Beth** as she is receiving a car benefit from her employer. This can be reduced to nil, if Beth covers the running costs of the car herself and is illustrated below:

|  |  |
| --- | --- |
| DETAIL | NO SALARY PACKAGING |
| Purchase Price of Car | $40,000 |
| Taxable Value (20% of purchase price) | $8,000 |
| **Less: After Tax Employee Contributions** | - |
| Fuel | $5,200 |
| Registration | $800 |
| Insurance | $1,000 |
| Repairs & Maintenance | $1,500 |
| **Total Running Costs** | **$8,500** |
| **Remaining Taxable Value** | **($500)** |
| **FBT Payable** | **-** |

HOW IT AFFECTS BETH’S EMPLOYER

As the remaining taxable value is less than nil, there are no FBT issues for **Beth’s employer**. It is important to note that if the running costs fall below the taxable value amount in any FBT year then Beth should physically pay the difference to her employer to ensure no FBT issues arise.

Finally, the benefits of Beth salary sacrificing her car in the first place are outlined here:

|  |  |  |
| --- | --- | --- |
| DETAIL | NO SALARY PACKAGING | WITH SALARY PACKAGING |
| Salary & Wage Income | $200,000 | $200,000 |
| Less: Salary Sacrificed Lease Payments | - | $7,500 |
| **Taxable Income** | **$200,000** | **$192,500** |
| Tax Expense | $67,232 | $63,707 |
| Less: Tax Withheld by Employer | $67,232 | $67,232 |
| Tax Refund / (Payable) | - | $3,525 |
| **After Tax Income** | **$132,768** | **$128,793** |
| **Less: Car Running Costs** |  |  |
| Finance Payments | $7,500 | - |
| Fuel | $5,200 | $5,200 |
| Registration | $800 | $800 |
| Insurance | $1,000 | $1,000 |
| Repairs & Maintenance | $1,500 | $1,500 |
| **Total Running Costs** | **$16,000** | **$8,500** |
| **Income After Tax & Car Expenses** | **$116,768** | **$120,293** |

By salary sacrificing Beth’s new car, she has increased her income after tax and car expenses by $3,525.

WANT TO **KNOW MORE?**

If you believe an associate lease would be beneficial to you and would like more information on how they work, please contact your advisor at FIRM NAME today.

**FIRM NAME**

**a** address

**p** phone xxx **e** email

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