

## **“COST PRICE OF THE VEHICLE” – MEANING OF THE TERM FOR FRINGE BENEFIT TAX PURPOSES**

**Public Ruling - BR Pub 09/08**

**Note** (not part of ruling): The key issue considered by this ruling is what is included in the “cost price” of a motor vehicle for fringe benefit tax purposes. The conclusion is that the cost price includes the vehicle’s purchase price, initial registration and licence plate fees, the cost of accessories (other than “business accessories”), and the cost of transporting the vehicle to the place where it is first to be used (each of these costs being on a GST-inclusive basis).

This ruling replaces public ruling BR Pub 03/06, which was published in *Tax Information Bulletin* Vol 15, No 9 (September 2003). BR Pub 03/06 applied until 31 October 2008 and was a reissue of BR Pub 00/10, which was published in *Tax Information Bulletin* Vol 12, No 10 (October 2000). This ruling is essentially the same as BR Pub 03/06, but now indicates that the Commissioner is prepared to accept that sign-writing the vehicle in the employer’s colours (in physical terms, the addition of paint or other graphics) is not part of the cost price of the vehicle for FBT purposes. A reference is also made to road user charges. The ruling has been updated to apply the Income Tax Act 2007, which came into force on 1 April 2008. The changes between the provisions in the Income Tax Act 1994 and the Income Tax Act 2007 do not affect the conclusions previously reached.

BR Pub 09/08 applies for an indefinite period beginning on 1 November 2008.

This is a public ruling made under section 91D of the Tax Administration Act 1994.

### **Taxation Laws**

All legislative references are to the Income Tax Act 2007 unless otherwise stated.

This Ruling applies in respect of section CX 6(a) and Schedule 5 (and the meaning of “cost price” for the purposes of determining the value of a benefit to an employee).

### **The Arrangement to which this Ruling applies**

The Arrangement is the provision of a motor vehicle by an employer, who owns, leases, or rents a motor vehicle, to an employee for the employee’s private use and enjoyment.

### **How the Taxation Laws apply to the Arrangement**

The Taxation Laws apply to the Arrangement as follows:

The “cost price of the vehicle” for the purposes of the calculation of fringe benefit tax under section CX 6(a) and Schedule 5 will be determined as follows.

- The “cost price of the vehicle” will include the:
  - purchase price of the vehicle (inclusive of goods and services tax (GST));

- cost of initial registration and licence plate fees (inclusive of GST);
- cost of accessories, components, and equipment (other than "business accessories") fitted to the vehicle at the time of purchase or at any time thereafter (all costs inclusive of GST);
- cost (if any), including freight insurance costs and any customs duty, of transporting the motor vehicle to the place where the motor vehicle is to be first used (all charges inclusive of GST).
- The "cost price of the vehicle" will not include the cost of:
  - annual vehicle re-licensing fees;
  - road user charges;
  - sign-writing the vehicle in the employer's colours or style (in physical terms, the addition of paint or other graphics such as magnetic signs, decals or transfers);
  - "business accessories", fitted to the motor vehicle at the time of purchase or at any time thereafter; and
  - financing the purchase of the vehicle.

For the purposes of this Ruling the terms "business accessories" and "fitted to the vehicle" have the following meanings.

- The term "business accessories" means accessories, components, and equipment fitted to the vehicle, required for and relating solely to the business operations for which the vehicle is used, and that are in themselves "depreciable property" for the purposes of the Act. Where powered, they will usually require the vehicle's power source to operate them (for example, a two-way radio, roof-mounted flashing warning lights, and electronic testing/monitoring equipment).
- The term "fitted to the vehicle" means permanently affixed to the vehicle. Permanency would not be negated if the accessory were removed from the vehicle on a temporary basis, for repair or maintenance, or on the removal of the accessory at the time of sale or disposal of the vehicle or the accessory itself.

### **The period or income year for which this Ruling applies**

This Ruling will apply for an indefinite period beginning on 1 November 2008.

This Ruling is signed by me on the 30<sup>th</sup> day of November 2009.

**Susan Price**

Director, Public Rulings

## **Commentary on Public Ruling BR Pub 09/08**

This commentary is not a legally binding statement, but is intended to provide assistance in understanding and applying the conclusion reached in public ruling BR Pub 09/08 (“the Ruling”).

All legislative references are to the Income Tax Act 2007 unless otherwise stated.

### **Background**

If an employee has the private use or enjoyment, or the availability for private use or enjoyment, of a motor vehicle that is made available by the employer of the employee, the employer must pay fringe benefit tax (FBT) on the value of the benefit. An employer has the option (since 1 April 2006) of valuing owned, leased, or rented motor vehicles at either the vehicle’s cost price or tax value. When choosing the cost price option the benefit is calculated by reference to the cost price of the vehicle to the employer, not the value of the benefit to the employee. If an employer purchases, leases, or rents a motor vehicle to be used by, or to be made available for use by, an employee, costs are incurred in addition to the purchase price of the vehicle for the vehicle to be in a state where it can be used by the employee. Additional costs include:

- on-road costs – under section 5 of the Transport (Vehicle and Driver Registration and Licensing) Act 1986, no motor vehicle can be driven on the road unless the:
  - motor vehicle is registered; and
  - registration plates and a current licence issued for the vehicle are affixed and displayed on the vehicle; and
  - full amount of the accident compensation levy has been paid;
- road user charges – under section 5 of the Road User Charges Act 1977 subject to section 7 of the Road User Charges Act 1977, no person shall operate certain motor vehicles on a road unless there is carried on the motor vehicle in accordance with the Road User Charges Act 1977 a distance licence;
- the cost, including freight insurance costs and any customs duty, of transporting the vehicle to the initial place where it is to be used;
- the cost of fitted accessories, components, or equipment required for and relating solely to the business operations for which the vehicle is used; and
- the cost of accessories, components, and equipment, such as tow bars, roof racks, and stereos, fitted to the car at the time of purchase or at some later time.

This Ruling identifies the costs that form part of the “cost price of the vehicle” for the purposes of calculating FBT.

The Commissioner considers the cost of a motor vehicle includes any accessories that are permanently affixed to the vehicle. Everything that is permanently affixed to the vehicle, including accessories such as CD players, tow bars, and radio-telephone sets, is part of the cost to the employer of making the vehicle available to the employee. Accessories that are not permanently affixed are not part of the cost price of the vehicle in the first place and their FBT (or other income tax) status is to be determined separately. However, the Commissioner

considers that certain accessories, permanently fitted to the vehicle and relating solely to the business operations for which the vehicle is used, should not be treated as part of the cost of the vehicle for FBT purposes. For example, a radio-telephone set fitted to the vehicle and able to be used only for business purposes would be excluded from the vehicle's cost price because it is a "business accessory". On the other hand, a mobile phone is an example of an item considered not to be part of the cost price of the vehicle because it does not meet the test of being permanently affixed to the vehicle.

## Legislation

The legislative provisions relevant to the subsequent analysis in this commentary are set out below.

Section CX 6 provides that a fringe benefit arises, when a motor vehicle is made available to an employee for their private use, and section RD 29(2) and (4) sets out the formulae for calculating the value of such a benefit:

### RD 29 Private use of motor vehicle: formulas

...

#### *Quarterly payment*

- (2) If FBT is paid quarterly, the value of the benefit is calculated using the formula—

$$\frac{\text{days} \times \text{schedule 5 amount}}{90}$$

...

#### *Payment by income year*

- (4) If FBT is paid on an income year basis, the value of the benefit is calculated using the formula—

$$\frac{\text{days} \times \text{schedule 5 amount}}{365}$$

Clause 1 paragraphs (a)(i) and (b)(i) of Schedule 5 state:

### Fringe benefit values for motor vehicles

- 1** The following paragraphs apply to determine the value of the benefit that an employee has for a quarter, tax year, or income year when section RD 60 applies, if in the quarter, tax year, or income year, a motor vehicle is provided by a person for the private use of an employee, or is made available for their private use:
- (a) if the vehicle is owned by the person, jointly or otherwise,—
    - (i) on the basis of the **cost price of the vehicle to the person**: for a quarter, 5% of the **cost price**, and for a tax year or income year, 20% of the **cost price**;
    - (ii) ...
  - (b) if the vehicle is leased or rented by the person from another person, whether they are associated or not,—
    - (i) on the basis of the **cost price of the vehicle** to its owner at the time the benefit is provided to the employee: for a quarter, 5% of the **cost price**, and for a tax year or income year, 20% of the **cost price**: [Emphasis added.]

Clause 8 of Schedule 5 provides:

To determine the value of a benefit under clause 1—

(a) any GST paid on the acquisition of a vehicle by the owner or lessor of the vehicle is—

(i) included in the cost price of the motor vehicle or in the calculation of the motor vehicle's tax value:

(ii) not reduced by an amount of input tax on the supply of the vehicle to the owner or lessor:

The definition of "adjusted tax value" in section YA 1(a) provides:

**adjusted tax value—**

(a) is defined in sections EE 55 to EE 60 ...

Sections EE 55(1)(a), EE 56(1) and (2), and EE 57(1) and (2), which are particularly relevant to this matter, provide:

#### **EE 55 Meaning of adjusted tax value**

(1) **Adjusted tax value** means,—

(a) for an item of depreciable property, the amount calculated using the formula in section EE 56: ...

#### **EE 56 Formula**

*Formula*

(1) The formula referred to in section EE 55 is—

base value – total deductions.

*Definition of items in formula*

(2) In the formula,—

(a) **base value** has the applicable meaning in sections EE 57, EE 58, EE 59, and EZ 22(1) (Base value and total deductions in section EE 56: before 1 April 1995): ...

#### **EE 57 Base value in section EE 56 when none of sections EE 58, EE 59, and EZ 22(1) applies**

*When this section applies*

(1) This section applies when none of sections EE 58, EE 59, and EZ 22(1) (Base value and total deductions in section EE 56: before 1 April 1995) applies.

*Base value*

(2) **Base value** is the cost of the item to the person.

### **Application of the legislation**

The determinative factor in the calculation of FBT on motor vehicles is the "cost price of the vehicle to the person" (that is, the employer, as provided in *CIR v Atlas Copco (NZ) Ltd* (1990) 12 NZTC 7,327) where the employer is the owner or, if the vehicle is leased or rented, the cost price of the vehicle to its owner at the time the benefit is provided to the employee: Schedule 5.

The High Court decision of *CIR v Atlas Copco (NZ) Ltd* was a test case regarding the meaning of "cost price" for the purposes of FBT. More specifically the issue in this case was whether "cost price" included or excluded GST. Sinclair J held that "cost price" is the GST exclusive cost to the employer of providing the benefit to the employee.

Following this decision Parliament amended the law to expressly provide that “cost price” included GST and to reflect that the intention of the FBT rules is to equate the “cost price” of motor vehicles with the cost that the employee would have had to pay had the employee purchased the vehicle (see: Tax Amendment Act (No. 3) 1991). This amendment only dealt with GST. There were no other changes made to the existing legislative wording for valuing the benefit to an employee. The reference to the cost price remained “the cost price of the motor vehicle to **that person**” (being the person providing the benefit). A set rate (now 5% for a quarter and 20% for a tax or income year under clause 8 of Schedule 5) is then applied to the GST inclusive cost price to arrive at the value of the benefit to an employee.

### ***Meaning of “cost price”***

“Cost price” is not defined in the Act for the purposes of the FBT rules. It is therefore not clear whether it is limited to the purchase price of the vehicle, as some suggest, or whether it includes costs incidental to the purchase, such as on road costs and the costs of transporting the vehicle to the place where it is to be used. However, as shown below, the use of the term throughout the Act - in the trading stock rules, the depreciation rules and in other contexts - and as reflected in accounting practice and relevant case law, indicates that “cost” and “cost price” are interchangeable. Consequently, “cost price” includes costs incidental to the purchase, such as on road costs and the costs of transporting the vehicle to the place where it will be used.

### ***“Cost” and “cost price” in the Act***

The words “cost” and “cost price” are used extensively throughout the Act. The definitions of “cost” and “cost price” in section YA 1, which defines the words for a limited number of sections, indicate that the two words are effectively synonymous and that they include more than simply the purchase price.

Examples include the following:

- For the purposes of Part EB (Valuation of trading stock) “cost” is defined as:
  - In subpart EB (...) for trading stock, means costs incurred in the ordinary course of business to **bring trading stock to its present location and condition** including purchase costs and costs of production calculated under sections EB 6 to EB 8. [Emphasis added.]
- “Cost price” in relation to “specified leases” means:
  - the amount of expenditure of a capital nature that is incurred, in acquiring and **installing** the asset,—
  - (i) by the lessor; [Emphasis added.]

The significance of these two definitions (even though they have limited application in the Act) is that they both include a reference to costs (“bringing to its present location” and “installing”) that are more than simply the **purchase price** of the item in question. In the definition of “cost” (for the purposes of the trading stock rules), it could be argued that getting the stock “to its present location” is synonymous with “installing” as used in the definition of “cost price”. “Install” is defined in the *Concise Oxford English Dictionary* (11<sup>th</sup>ed, 2006) as “place or fix (equipment) in position ready for use”. While the two definitions relate to the two different sides of the revenue–capital distinction, they both relate to the assets used in a business.

Where the words are used in other parts of the Act and there is no specific definition, it is considered that "cost price" should be given a similar interpretation. This means that "cost price" as used for FBT purposes also means "cost".

### *Trading stock context*

The definition of "cost" applying to the valuation of trading stock requires the "cost" to include (section YA 1):

Costs incurred in the ordinary course of business to bring trading stock to its present location and condition, including purchase costs and costs of production, calculated under sections EB 6 to EB 8.

The requirements for valuing trading stock under section EB 6, which essentially says that the trading stock valuation must comply with the New Zealand International Accounting standard NZIAS2 or an equivalent standard issued in its place, endorse the view that "cost" and "cost price" are effectively interchangeable.

Under NZIAS2, Inventories it is stated that:

10 The cost of inventories shall comprise all **costs of purchase**, costs of conversion and **other costs incurred in bringing the inventories to their present location and condition**. [Emphasis added.]

Similarly the predecessor of NZIAS2, FRS4, which applied from 1994, indicated "cost" and "cost price" were interchangeable by taxpayers in valuing trading stock under the former valuation option, "cost price", and that the Commissioner accepted similar calculations to FRS 4. That is illustrated by the contents of an item on the valuation of trading stock published in *Public Information Bulletin* No 82 (December 1974). This item set out the three options available to taxpayers: cost price, market selling value, or replacement price. The item then went on to define "cost" (note, not "cost price"). In respect of purchases of finished goods, the item said (at page 2):

Here the cost should include **freight inwards**, customs duty, **insurance**, and sales tax in addition to the actual purchase price of the goods. [Emphasis added.]

This view that "cost" and "cost price" have the same meaning finds support in the decisions referred to below. Both the Australian decisions of *Phillip Morris Ltd v FCT* [1979] ATC 4, 352, and *Australasian Jam Company Proprietary Limited v Federal Commissioner of Taxation* 88 CLR, 23, considered section 31(1) of the Australian Income Tax Assessment Act 1936, which gave taxpayers an option of valuing trading stock at its "cost price". The wording of the section was very similar to the former New Zealand equivalent - section EE 1(3) of the Income Tax Act 1994 before amendments that applied from the 1998/99 income year (that is, the same "cost price" option applied to New Zealand taxpayers). It follows that in considering the use of the words "cost price" in New Zealand, New Zealand courts would arguably adopt the same position the Australian courts adopted in those decisions.

- In *Phillip Morris Ltd v FCT* [1979] ATC 4, 352, the Supreme Court of Victoria had to decide what constituted "cost price" for the valuation of cigarettes (trading stock) on hand at the end of an income year under section 31(1) of the Income Tax Assessment Act 1936 (Australia). Jenkinson J said:

the words "cost price" in section 31(1) of the Income Tax Assessment Act 1936 should be understood as meaning "cost" (page 355).

The statutory conception of "cost price" or, **in the case of manufacturer's stock, "cost"** is merely a value at a particular time... [Emphasis added. Page 360]

...

- In *Australasian Jam Company Proprietary Limited v Federal Commissioner of Taxation* 88 CLR, 23, Fullagar J said (at page 529):

The words "cost price" in the section [relating to the valuation of trading stock] are **perhaps not literally appropriate to goods manufactured, as distinct from goods purchased**, by the taxpayer, but I feel no difficulty in reading them as meaning simply "cost". [Emphasis added.]

[See also "Some Aspects of Valuation of Trading Stock for Income Tax Purposes" (1964) 1 NZULR 256, ILM Richardson (now Sir Ivor) which endorsed Fullagar J's view in *Australasian Jam* at page 261 – "If "price" adds anything to "cost" it is only in emphasis, in stressing that what is involved is the actual expenditure of money by the taxpayer with relation to the trading stock".]

- In *TRA Case S12* (1995) 17 NZTC 7,102, Barber DJ considered what is meant by "its cost price" in relation to the valuation of foals born to broodmares owned by a horse breeder. He determined that the foal's cost price should include the write-down (depreciation) of the broodmare. Barber DJ said (at page 7,107):

The Legislature has provided that the breeder or farmer must take progeny into account at "its cost price". Those words do not seem to me to be a particularly happy choice because **"cost price" is normally that which a merchant buys something** (refer Sixth Edition of the *Concise Oxford Dictionary*). The cost is the price to be paid for a thing and the price is the money or other consideration for which a thing is bought or sold. The taxpayer has not purchased the foal but has had the foal created through the mare after servicing from the stallion. However, in their context, the words "its cost price" must be given a sensible interpretation. In the *Shorter Oxford English Dictionary* (3rd Edition) a meaning for "cost" is "That which must be given in order to acquire, produce or effect something". [Emphasis added.]

### *Accounting practice more generally*

The *Atlas Copco* decision also provides support for the view that "cost" and "cost price" effectively have the same meaning. In *Atlas Copco*, for example:

- Sinclair J (at page 7,332) referred to expert accounting evidence on the meaning of "cost" and stated:

This accords with the expert evidence given by two accountants, Mr John Hagen and Professor David Emanuel. Professor Emanuel cited a number of definitions of "cost" from leading textbooks on accounting:

- (a) 'Costs represent the financial sacrifices which are involved in acquiring or producing assets.' Ma, Matthews and MacMullen, *The Accounting Framework* (2<sup>nd</sup> Ed, [Longman Cheshire] 1986) at p 43.
- (b) 'Accountants have placed a great deal of emphasis upon the principle of objective evidence, and nowhere is it more apparent



than in accounting for the acquisition of plant and equipment. Cost is used as the valuation method in this instance because it is more easily identified than any other valuation and because it is said to be the sacrifice given up now to accomplish future objectives.' [McCullers and Schroeder, *Accounting Theory: Text and Readings* (Wiley, 1978,)] at p 233.

- (c) 'We define cost here as the sum of the quantitative representations of the sacrifices necessarily incurred **to bring the fixed asset to its place and state of use.**' Most, *Accounting Theory* ([Grid] 1977) at p 235. [Emphasis added.]
- (d) 'Cost is thus the economic sacrifice expressed in monetary terms required to obtain a specific asset or group of assets.' Hendriksen, *Accounting Theory* (3<sup>rd</sup> Ed, [Irwin, by ES Hendriksen] 1977) at p 270.
- (e) 'Cost is an economic sacrifice, an outflow of wealth, by giving up asset value or incurring liability value.' Staubus, *Activity Costing for Decisions* ([Garland Publishers, New York,] 1988) at p 192."

Professor Emanuel then summarised the position by saying that:

"Cost is the economic sacrifice associated **with getting the purchased item to its current location and condition.**" [Emphasis added.]

[It is interesting to note that here the accountants used the term "cost" rather than "cost price" – the term (as used in Schedule 5) that the court was considering.]

- When the Commissioner objected to the evidence of the accountants Sinclair J said (at page 7,333):

Counsel for the Commissioner objected to the evidence of the two accountants on the basis that the interpretation of "cost price" is a question of law for the Court, and to rely upon the interpretation of accountants would infringe the "ultimate issue" rule. Moreover, counsel felt that the accountants had mistakenly placed economic substance over legal form in analysing the nature of the payment paid by the purchaser.

It is true that defining "cost price" is a question of statutory interpretation and, as such, must be resolved by the Court. **Where the meaning of words in a statutory context is unclear or ambiguous, however, the Court may derive some assistance from common business parlance and practice**, as well as international standards. Moreover, as I have already discussed, the approach of the accountants accords with both the economic substance and the legal form of the transaction: the GST component of the purchase price which may be recovered by a registered purchaser cannot be considered part of the effective "cost price". [Emphasis added.]

Here, the Court accepts that where there is uncertainty in the legislation common business practice can be taken into account in defining terms or words. As sufficient doubt surrounds the use of the words in question, accounting or business usage may be of assistance.

Generally, the accounting treatment is that the initial cost of a fixed asset includes the costs of putting it into the working condition necessary for its intended use, installation costs, freight and so on (see, for example, NZIAS2 and the expert evidence given in *Atlas Copco*).

### *Depreciation context*

The only provisions that deal with valuation of capital assets in the Act are the depreciation rules set out in Subpart EE.

Generally, business assets are “depreciable property” as defined in section EE 6. Section EE 6 provides that depreciable property is property that:

...might reasonably be expected to decline in value while it is used or available for use ... in carrying on a business for the purposes of deriving assessable income.

This is provided the assets are not trading stock, land, financial arrangements, or intangible property. Motor vehicles are “depreciable property” and qualify for depreciation deductions under Part EE.

Under section EE 17(4) the value or cost to calculate depreciation is, where the:

- diminishing value method is being used, on the “adjusted tax value” of the item; or
- straight-line method is being used, on the “cost of the item” to the taxpayer.

“Cost” is not defined in the Act for the purposes of section EE 17. Section YA 1 provides that “adjusted tax value” is defined in sections EE 55 to EE 60. The main component of the formula to calculate the adjusted tax value is the “base value” of the property (section 56). “Base value” in most cases, especially in respect of property acquired after the beginning of the 1993/94 income year, will be its “cost” (sections EE 57(2), EE 58, and EE 59).

As stated above, as far as trading stock is concerned there appears to be no difference between the use of the words “cost” and “cost price”. The words are interchangeable. If the same applies in respect of the word “cost” used in Subpart EE, it could mean that “cost” and “cost price” are interchangeable elsewhere in the Act (for example, in Schedule 5, in determining the “cost price” of a motor vehicle for FBT purposes).

### *Conclusion*

On the above analysis, it is concluded that “cost” and “cost price” as used in the Act are interchangeable. The calculations of both terms, using accepted accounting principles, include costs in addition to what can be termed the “purchase price”. This means that for the purposes of the phrase “cost price of the motor vehicle” in the FBT rules, the “cost price” of a motor vehicle will be more than just its purchase price.

### ***What is the “cost price” of a motor vehicle for fringe benefit tax purposes?***

When a new motor vehicle is purchased, government charges have to be paid before the purchaser can use the vehicle on the road. The purchaser may also have accessories fitted to the vehicle at the time of purchase or later. Some of these accessories may be of a non-business nature, such as a tow bar, a CD player, conversion to compressed natural gas (CNG) or liquefied petroleum gas (LPG), air conditioning, or alloy wheels. Generally, unless these accessories are part of a special deal, they will be additional costs to the purchaser. In some instances, the purchaser may have a business accessory, such as a radio-telephone, fitted to the vehicle at the time of purchase or later.

The question to be considered is whether all or any of the cost of these items forms part of the "cost price" of the vehicle.

### *Government charges*

Fees payable at the time of the purchase of a new car so that it can be driven on the road include:

- once-only payments: the registration fee and number plate fee; and
- ongoing (recurring) fees: the annual re-licensing fee, the accident compensation levy, the label fee, and road user charges.

It is arguable that without payment of the initial registration and plate fees (as distinct from the recurring annual re-licensing fees) by the owner the vehicle cannot be used immediately. The owner has to pay these costs before the vehicle can be "put on the road" or in a position to be used. This suggests these costs are properly to be treated as part of the "cost price" of the car.

Support for the view that "cost" includes such items as getting the vehicle "on the road" so that it can be used, is found in the High Court of Australia case *BP Refinery (Kwinana) Ltd v FCT* (1960) 8 AITR 113. Kitto J, in considering the issue of what was included in the term "cost", said (at page 117):

...in my opinion, the word "cost" in section 56(1)(b) [of the Income Tax Assessment Act 1936] bears the meaning which it has in the business life of the community. It seems to me impossible to suppose that the depreciation provisions of the Act are intended to apply only to those simple cases in which the ascertainment of cost is a purely arithmetical process. I interpret it as embracing the whole sum which, according to accepted accountancy practice as applied to the circumstances of the case, ought to be considered as having been laid out by the taxpayer in order to acquire the subject-matter as plant, **that is to say installed and ready for use** as plant for the purpose of producing assessable income. [Emphasis added.]

Therefore, the cost of the vehicle must include expenditure making it "ready for use" by the taxpayer. Without payment of the registration and plate fees, the vehicle is not ready for the purpose intended.

Whether the costs of the initial registration fee and the plate fee form part of the cost of the vehicle is not entirely clear. The Commissioner considers the better view of the law, and the likely intent of Parliament, is that such expenses form part of the cost price of the vehicle, particularly given that they are one-off costs that fall into the "once and for all payments" category (see *BP Australia Ltd v FCT* [1965] 3 All ER 209). Therefore, they are capital in nature. These fees are intended to make the vehicle able to be used.

The remaining fees are annual or ongoing charges and normal accounting practice would treat them as revenue expenditure, even if they were incurred upon the purchase of the vehicle.

In summary, the better view is that registration and plate fees are "once and for all" payments, are of a capital nature, make the vehicle able to be used, and are part of the "cost price" of the vehicle. Ongoing charges (such as licensing, the accident compensation levy, and road user charges) are revenue expenditure, so are not part of the "cost price".

### *Business accessories*

Generally, accessories permanently fitted to the motor vehicle are properly to be included as part of the vehicle's cost. As discussed earlier, accessories, such as stereos, tow bars, and roof racks, fitted to a vehicle will form part of its cost price.

However, some components or equipment fitted to vehicles may be of a purely business nature. The issue arises as to whether such components or equipment should also be included in the "cost price of the vehicle" for FBT purposes.

There is no legislative direction on this issue. This may indicate that all accessories, components, or equipment attached to the vehicle form part of its "cost price". It is arguable, however, that business accessories, components, and equipment fitted to the vehicle should not be treated as forming part of the cost price where they are required and relate solely to the special business operations for which the vehicle is used, and are in themselves depreciable property for the purposes of the Act (for example, a two-way radio-telephone in a salesperson's vehicle). Such components or equipment are fitted to the vehicle to facilitate the business use of the vehicle and may be considered as separate business assets located in the vehicle.

Another factor (relevant to this last-mentioned aspect) possibly pointing to the components or equipment as not being part of the cost price, is the nature of the assets and how they are treated by businesses for accounting purposes. For example, it is most likely that components such as two-way radios are accounted for and depreciated separately. The radios can be removed from vehicles or moved from one vehicle to another, so it seems logical that they be treated as separate assets for depreciation purposes. [Note that motor vehicles and radio-telephone equipment are listed separately in the Commissioner's Table of Depreciation Rates.] Two-way radios have their own depreciation rate because they are regarded as assets in their own right and not accessories to a motor vehicle. They form part of a larger asset, for example, the entire radio-telephone network, consisting of radios in vehicles and the central control unit in the employer's premises. In such circumstances, even though they are a form of accessory or addition to the motor vehicle, they are an asset in their own right, and therefore require a separate asset classification. Usually, radio networks are purchased as a package consisting of radios (one for each vehicle) plus the central control station. To treat the network as part of the cost price of each car would require an apportionment of the overall expense, including installation costs to each vehicle. The Commissioner does not consider this to be a sensible approach.

The same could be said of accessories such as roof-mounted flashing lights and electronic monitoring equipment. If these types of assets are added to the vehicle because they are required for and relate solely to the business operations for which the vehicle is used, they will be treated similarly to the two-way radio system.

Therefore, where business components, such as two-way radios, roof-mounted flashing lights, and electronic testing or monitoring equipment, are fitted to the vehicle and are paid for by the employer, they do not form part of the vehicle's "cost price" for FBT purposes. As mentioned earlier, such accessories are business assets of the employer, coming within the definition of "depreciable property" for the purposes of the Act.

As previously discussed under the heading "Application of the legislation", it was the intent of Parliament to equate the "cost price" of motor vehicles with the cost that the employee would have had to pay had the employee purchased the vehicle rather than having it provided by the employer. It follows that if the employee had to pay for the vehicle, the cost to the employee must also include accessories fitted to the vehicle as already discussed. Exceptions are the cost of separately depreciable components or equipment fitted to the vehicle solely to meet the special needs of any business operations for which the vehicle is used.

Therefore, the Commissioner considers that business components fitted to the vehicle that are required for and relate solely to the business operations for which the vehicle is used and are in themselves depreciable property should be excluded from the "cost price" of motor vehicles for FBT purposes. This covers assets requiring the vehicle's power source in order to operate: they are not part of the cost price of the car itself.

There may be isolated instances, where the type of business asset mentioned above will unavoidably be used for non-business purposes. The Commissioner considers that any extraordinary and unenvisaged use of the accessory for non-business use over the life of the asset will not in itself negate the purpose of fitting the accessory to be "solely for business purposes" in this context.

#### *Cost of non-business accessories*

Commonly, when a vehicle is purchased the owner asks for certain "extras" or accessories (other than business accessories) to be fitted to the vehicle. If these accessories are not "optioned" (and included in the purchase price), the dealer will charge for their cost and fitting to the vehicle. Such accessories can include: a stereo, a tow bar, a sunroof, a roof rack, CNG/LPG conversion, alloy wheels, air-conditioning, electric windows and locking systems, and higher specification tyres.

Where the vendor charges for any of these accessories, the question arises as to whether they should be added to the "cost price" of the vehicle for FBT purposes. The same issue arises if the accessories are acquired from another person or supplier, or acquired later.

Such accessories are of a capital nature and should be added to the vehicle's purchase price to arrive at its "cost price". They are part of the vehicle as a whole and are not generally removed at the time the vehicle is sold or otherwise disposed of. They are either singularly or collectively "once and for all" payment(s), culminating in the "cost price" of the vehicle that is provided to the employee by the employer for the employee's "private use and enjoyment". Under this interpretation, the cost price may vary from period to period, depending on when accessories are added (or in the unlikely or rarer event of an accessory being removed).

Therefore, in summary, accessories fitted to a vehicle form part of its "cost price" for FBT purposes (as contemplated in Schedule 5), irrespective of the time they are purchased and fitted to the vehicle.

#### *Cost of sign-writing or painting the vehicle in the employer's colours or design*

There are different types of sign-writing that fall into some broad categories including magnetic decals or door magnets that can be removed, decals or

transfers that cannot be easily removed and colour or paint that is applied permanently to a motor vehicle.

So far as magnetic decals or door magnets that are designed to be easily removed are concerned they do not become part of a vehicle and it seems reasonably clear that they should not form part of a vehicle's cost price for FBT purposes.

Other non removable sign-writing is, however, potentially part of the cost price of a vehicle in the same way that accessories such as stereos, tow bars and roof racks, fitted to a vehicle will form part of its cost price. However, it is accepted that sign-writing costs are purely of a business nature. Given this, although they are not in every case able to be separately depreciated, the Commissioner accepts that such costs do not form part of the cost price of the vehicle for FBT purposes.

#### *Transporting or freighting the vehicle to its place of use*

In the above discussion on "cost price", it is clear that the courts have accepted that the cost of transporting or freighting goods (whether those goods are trading stock or capital assets of the business) to the place where they are to be used is part of the cost of the goods. Generally, the initial cost of fixed assets will include expenditure incurred to put the asset into the working condition necessary for its intended use. In *Atlas Copco* (at page 333) there was reference to, "cost is ... associated with getting the purchased item to its current location and condition", which includes installation costs and freight.

The cost of transporting a purchased motor vehicle to the place where it can be used by the taxpayer is clearly part of its "cost price", both for FBT and depreciation purposes; for example, the purchase of vehicles direct from a manufacturer or from another source overseas, where the purchaser pays for the cost of transporting the vehicle to New Zealand. Transport costs incurred may include the physical transportation costs as well as freight insurance costs and any customs duty. It is the Commissioner's view that these transport costs form part of the "cost price" of the vehicle for FBT purposes.

However, these costs relate only to the initial cost of getting the vehicle to the place it will first be used by the owner after acquisition. Subsequent transport costs of moving the vehicle within New Zealand (say from one branch of the employer's firm to another), including any costs of insuring the vehicle for such transport, are considered part of the employer's normal business operations and on revenue account.

#### **Cost of repairs and maintenance and capital expenditure**

Another issue relates to the costs of repairs and maintenance to the vehicle and/or accessories, and whether they should be added to the cost price as capital expenditure.

Generally, repairs and maintenance expenditure on the vehicle or accessories will not increase the vehicle's "cost price" for FBT purposes. However, if work on the car is more than normal repairs and maintenance, such as replacing the existing motor with one of larger capacity, the question arises whether that alteration increases the cost price of the vehicle for FBT purposes. If the repair or replacement is considered to be of a revenue nature and deductible for income

tax purposes, the cost price of the vehicle will not increase in value for the calculation of FBT. On the other hand, if the repair or replacement is of a capital nature, the cost price for FBT purposes must be increased by the amount of that capitalisation.

Each case needs to be considered on the basis of its own facts, applying the established capital/revenue tests. If the FBT cost price is increased, the recalculation of FBT (on the increased cost price) will apply from the quarter in which that capital expenditure was incurred.

## **Examples**

### ***Example 1***

Employer A purchases a second-hand motor vehicle as a company car for the use of a salesperson employee. The employee will be travelling long distances, so the employer purchases a CD player and has it fitted to the vehicle. The employee has full use of the vehicle for private use and is likely to tow his own trailer from time to time, so he asks the employer to purchase and fit a tow bar to the vehicle. The employer agrees.

The "cost price" of the vehicle for FBT purposes will be the total of the purchase price plus the cost of acquiring and fitting the CD player and the tow bar (all costs GST inclusive).

### ***Example 2***

Employer B is looking for a vehicle to replace an existing vehicle written-off by the firm's Wellington-based accountant. The accountant will be entitled to use the vehicle for private purposes when it is not being used for business purposes. While on a trip to Auckland, the employer locates a suitable second-hand car, purchases it, and has it transported to Wellington where the accountant will use it.

The "cost price" of the car for FBT purposes will be the purchase price plus the cost, including freight insurance costs, of transporting it to Wellington (all costs GST inclusive).

### ***Example 3***

Employer C decides to replace the company's fleet of cars used by its sales representatives, because of the high cost of maintaining the existing fleet. The sales representatives are permitted to use the vehicles for private use when they are not required for business purposes. Through a contact with a motor vehicle dealer, the company decides to purchase 10 second-hand diesel powered cars direct from Japan. The employer agrees on a purchase price with a Japanese car dealer and arranges for the vehicles to be shipped to New Zealand. In New Zealand employer C arranges for the company logo to be painted onto the vehicles and purchases a 1000 km road user charge distance licence for each vehicle.

The "cost price" of the vehicles for FBT purposes will be the total of:

- the purchase price of the cars, including any costs or commissions paid in Japan or New Zealand;
- the cost of transporting the cars to New Zealand, including freight insurance costs and any customs duty;

- GST and any import or inspection levies payable at the time of importation;
- the cost of initial registration and licence plate fees; and
- the cost of any accessories fitted to the cars at the time of purchase or any time after purchase, either in Japan or New Zealand.

The “cost price” of the vehicles for FBT purposes will not include:

- the cost of road user charges; and
- the cost of sign-writing the vehicles with employer C’s logo.

#### ***Example 4***

Employer D is a forestry contracting firm that has recently purchased a four-wheel drive motor vehicle for its forestry foreman. The foreman has the full use and enjoyment of the vehicle for private purposes while not working. As with the employer’s other work vehicles, the car is fitted with a radio-telephone used only for communication between the company’s headquarters and its own vehicles.

The radio-telephone is fitted solely for business purposes and may be considered a separately depreciable business asset located in the vehicle, so it does not form part of the cost price of the vehicle for FBT purposes.

#### ***Example 5***

An employee of employer E is a travelling salesperson. When the employer purchased a new vehicle for the employee’s use, a mobile phone kit (mobile phone and car kit) was installed in the car at the employer’s expense.

The cost of the mobile phone is excluded from the cost price of the motor vehicle because it is not “permanently affixed to the vehicle”. Whether use of the mobile phone gives rise to a fringe benefit in its own right will need to be considered under the FBT rules generally, including section CX 21, which applies to the use of “business tools”.