

The following examples set out the benefit of buying (whether bought outright or financed) and asset need for a business. Not included is the extra income and/or cost saving from buying the asset in question – but we would be happy to model that out for you.

Take the case of a company with a profit of \$100,000 that needs an \$80,000 asset (exc GST) in its business.

In the following example you can see that the net cost of buying the \$80,000 asset will only be \$59,200 – and hopefully that asset can help increase revenue and/or reduce costs so the net result should be even better.

However, if the asset is acquired under a hire purchase contract by way of loan, the cash flow outcome will be positive

Tax position	Don't buy	Buy asset	Finance asset
Current profit/(loss)	100,000	100,000	100,000
Less equipment needed for business	0	(80,000)	(80,000)
Less interest under finance contract	0	0	(2,181)
Resulting CY taxable income	100,000	20,000	17,819
Company tax rate for 2020/21	26.0%	26.0%	26.0%
Less tax payable	(26,000)	(5,200)	(4,633)
Net profit after tax	74,000	14,800	13,186

Cash position			
Current year profit	100,000	100,000	100,000
Less income tax payable thereon	(26,000)	(5,200)	(4,633)
Less cost of asset	0	(80,000)	0
Less finance repayments	0	0	(12,403)
Net cash position	74,000	14,800	82,964

Reduction in cash position after buying required asset	(59,200)
Increase in cash position from having acquired asset under finance	8,964

The outcome is even better to your customer if they don't qualify for the small business company tax rate as the tax savings will be larger.

Tax position	Don't buy	Buy asset	Finance asset
Current profit/(loss)	100,000	100,000	100,000
Less equipment needed for business	0	(80,000)	(80,000)
Less interest under finance contract	0	0	(2,181)
Resulting CY taxable income	100,000	20,000	17,819
Company tax rate for 2020/21	30.0%	30.0%	30.0%
Less tax payable	(30,000)	(6,000)	(5,346)
Net profit after tax	70,000	14,000	12,473

Cash position			
Current year profit	100,000	100,000	100,000
Less income tax payable thereon	(30,000)	(6,000)	(5,346)
Less cost of asset	0	(80,000)	0
Less finance repayments	0	0	(12,403)
Net cash position	70,000	14,000	82,251

Reduction in cash position after buying required asset	(56,000)	
Extra cash from having acquired asset under finance		12,251

And the results will be higher if your business is run through a trust, partnership or as a sole trader where the marginal tax rate is 39%.

Tax position	Don't buy	Buy asset	Finance asset
Current profit/(loss)	100,000	100,000	100,000
Equipment needed for business	0	(80,000)	(80,000)
Interest under finance contract	0	0	(2,181)
Resulting CY taxable income	100,000	20,000	17,819
Marginal tax rate (T, P or ST)	39.0%	39.0%	39.0%
Tax payable	39,000	7,800	6,949
Net profit after tax	61,000	12,200	10,870

Cash position			
Current year profit	100,000	100,000	100,000
Less income tax payable thereon	(39,000)	(7,800)	(6,949)
Less cost of asset	0	(80,000)	0
Less finance repayments	0	0	(12,403)
	61,000	12,200	80,648

Reduction in cash position after buying required asset	(48,800)	
Extra cash from having acquired asset under finance		19,648

But as I said earlier, the outcome is even better for a company that paid tax on the 2020 year but makes a loss in 2021. The new and temporary carry back company loss rules enable a company to claim a refund of tax previously paid. This tax break will only be in effect for two years so don't miss out!

Tax position	Don't buy	Buy asset	Finance asset
2020 year profit	200,000	200,000	200,000
2019/20 company tax rate	27.5%	27.5%	27.5%
less 2020 year tax	(55,000)	(55,000)	(55,000)
2020 profit after tax	145,000	145,000	145,000
2021 year profit/(loss)	(100,000)	(100,000)	(100,000)
Net 2020 & 2021 taxable income	100,000	100,000	100,000
Less equipment needed for business	0	(80,000)	(80,000)
Less interest under finance contract	0	0	(2,181)
Revised net 2020 & 2021 profit	100,000	20,000	17,819
Company tax rate for 2020/21	26.0%	26.0%	26.0%
Less net company tax payable at 26%	(26,000)	(5,200)	(4,633)
2020 year tax at recoupment rate of 26%	(52,000)	(52,000)	(52,000)
2020 year tax that can be recouped	(26,000)	(46,800)	(47,367)
2020 & 2021 net profit less tax	74,000	14,800	13,186

Cash position			
2020 year profit	200,000	200,000	200,000
2021 year loss	(100,000)	(100,000)	(100,000)
Less income tax payable after carry back	(26,000)	(5,200)	(4,633)
Less cost of asset	0	(80,000)	0
Less finance repayments	0	0	(12,403)
	74,000	14,800	82,964

Reduction in cash position after buying required asset **(59,200)**

Extra cash from having acquired asset under finance **8,964**



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There are some assumptions within these examples. Like the asset being bought in January, so the finance payments are for 6 months and under a 5 year contract of 60 monthly instalments with no residual. The instalments won't be as much and the cash flow better if there is a balloon payment.

Not sure what assets qualify? Then refer to our 3 part series within our blogs.

We welcome discussing how you can benefit from this.