TD 94/D106 - Income tax: does the interest paid by an employee on a loan to purchase a motor vehicle used for income-producing purposes continue to be an allowable deduction under subsection 51(1) of the Income Tax Assessment Act 1936 after disposal of the vehicle?

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Australian Taxation Office

Taxation Determination TD 94/D106

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Draft Taxation Determination

Income tax: does the interest paid by an employee on a loan to purchase a motor vehicle used for income-producing purposes continue to be an allowable deduction under subsection 51(1) of the *Income Tax Assessment Act 1936* after disposal of the vehicle?

1. The deductibility of the interest expenses after disposal of the vehicle will depend upon whether the borrowed money is still used for income-producing purposes.

2. After the vehicle is sold, the employee may use the money received from the sale to gain or produce assessable income. In that case, the interest paid by the employee is still deductible. However, if the money is used for some other purpose, such as a private purpose or to gain or produce exempt income, the interest will not be deductible under subsection 51(1).

3. A portion of the continuing interest on the loan may be deductible if the motor vehicle is sold for less than the balance outstanding under the loan at that time. If the money received from the sale is used to produce assessable income, the interest on an equal amount of the loan principal is a deductible expense. The rest of the interest expense relates to a loss of the capital value of the vehicle; that portion is not an allowable deduction after the vehicle is sold.

Example:

Jerry has been employed for some years by PDQ Building Company as a plumber. In 1990 Jerry borrowed $30,000 to buy a four-wheel-drive vehicle which he used wholly in the course of his employment.

In June 1994 PDQ transfers Jerry to its building maintenance division, where he no longer needs the vehicle to perform his duties. Jerry sells the vehicle on 20 June 1994, but does not use the money he receives to repay the balance of $15,000 then outstanding under the loan.

(a) If Jerry sells the vehicle for $15,000 and uses the money to buy shares in a company that pays dividends, the borrowed money continues to be used to gain or produce assessable income and the interest expenses are still deductible.

(b) If he sells the vehicle for $15,000 and uses the money to discharge a mortgage over a residential property that is not used for income-producing purposes, the borrowed money is now applied for private or domestic purposes. Tax deductions are not allowable for interest that accrues on the loan after 20 June 1994.

(c) If Jerry sells the vehicle for $12,000 and uses the money to buy shares in a company that pays dividends, $12,000 of the borrowed money is still being used to gain or produce assessable income. The interest payable on that portion of the loan is tax-deductible. The remaining interest, relating to the shortfall between the amount of the loan and the money received from the sale of the vehicle, is not deductible after 20 June 1994.

Commissioner of Taxation
1/12/94

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