

# Fleet & Taxation

## INSIDE

**42** | The practical lowdown on company car taxation

**46** | How capital allowances affect tax relief

**48** | Understanding the time value of money

**50** | Tax implications of ECO, cash and salary sacrifice

**52** | Are ULEVs a tax-efficient option for a company car?

How to get the tax treatment of your vehicles right and unlock potential savings



# The practical low-down on company car taxation

How and when companies and drivers pay tax on company cars can be a very delicate process, *Jeff Whitcombe*, director of BCF Wessex Consultants, explains

Since the turn of the century, to help reduce the UK's dependence on fossil fuels and meet international environmental commitments, successive governments have offered tax incentives for drivers and companies to choose low-emission company cars.

These measures continue to encourage manufacturers to improve vehicle and engine technology, which has already resulted in the average CO<sub>2</sub> emissions of new cars in the UK falling by one third\* between 1997 and 2013, from 190g/km to just 128g/km.

When a company procures a company car, there are several tax consequences, including corporation tax, VAT and Class 1A NIC. Companies have to account for Class 1A NIC on the benefit provided and claim corporation tax and VAT relief on the costs they incur, including ancillary costs such as maintenance and fuel.

To complicate matters, VAT relief is governed by the availability of the car for private use, while corporation tax and VAT relief are intrinsically linked to the car's CO<sub>2</sub> emissions and the way in which the car is acquired and financed.

How big a slice should you be paying?



## CORPORATION TAX

Corporation tax is due on a company's taxable profits each year. Companies that pay the main rate of corporation tax must make quarterly payments on account but other companies must settle their corporation tax within nine months and one day of the end of their financial year. For example, if the year-end is December 31, 2014, tax must be paid by October 1, 2015.

The current rates of corporation tax are:

Company rate	Profits	Effective rate to 31/03/15
Small	Up to £300,000	20%
Marginal	£300,001 to £1,500,000	21.25%
Main	Above £1,500,000	21%

From April 2015, all three company rates will be unified at 20%.

### Purchased cars – capital allowances

Capital allowances enable companies to claim corporation tax relief for the depreciation of assets they purchase and use in their trade. For example, if a company bought a car for £20,000, which it sold several years later for £8,000 it would be able to claim capital allowances of £12,000.

The timing of the tax relief depends on a car's CO<sub>2</sub> emissions, with companies able to claim tax relief more

quickly for cars with lower CO<sub>2</sub> emissions.

- Currently, capital allowances may be claimed as follows:
- a 100% first year allowance for cars with CO<sub>2</sub> emissions not exceeding 95g/km;
  - an annual 18% writing-down allowance for cars with CO<sub>2</sub> emissions between 96g/km and 130g/km
  - an annual 8% writing-down allowance for cars with CO<sub>2</sub> emissions above 130g/km

From April 2015 the 95g/km first year allowance threshold will fall to 75g/km. As there is currently only one conventionally-powered car that meets that threshold, any company wishing to buy a qualifying car after March 2015 must initially

embrace new technology and adopt a pure electric, range-extended electric, or plug-in hybrid electric vehicle.

#### Leased cars – lease rental restriction

When a company leases a car it obtains corporation tax relief by deducting the cost of the lease rentals from its taxable income, but the proportion of the rental a company may deduct from taxable profits depends on the CO<sub>2</sub> of the car, as follows:

- For cars emitting 130g/km or less, the rental is fully tax deductible
- Cars with emissions exceeding 130g/km face a 15% restriction, meaning companies can only deduct 85% of the rental (plus any blocked VAT). For example, a company leases a car with CO<sub>2</sub> emissions of 143g/km for an effective rental of £330 per month:

	Monthly	Annually
Effective rental	£330.00	£3,960
Disallowed lease rental (15%)	£49.50	£594
Allowable deduction for corporation tax purposes	£280.50	£3,366

#### Other costs

Corporation tax relief should be available for ancillary costs such as maintenance, interest, insurance, business fuel and Vehicle Excise Duty in the financial year in which the expenses are incurred, although care should be taken when structuring payment arrangements as HMRC may insist that for tax purposes front-loaded payments should be spread evenly over the term of the contract.

## VALUE ADDED TAX

#### Purchased cars

VAT is chargeable on all new cars purchased or imported for use in the UK, but it cannot be recovered unless the car:

- will be used exclusively for business purposes and is not available for any private use
- is a 'stock-in-trade car' of a motor manufacturer, dealer or leasing company
- is intended to be used primarily as a taxi, driving-instruction car or daily rental

Unlike most companies, leasing companies normally buy cars exclusively for business use and, provided the cars are leased at commercial rates, they may recover the VAT incurred on purchase, but must apply VAT to rentals and state on the VAT invoice that the leased car is a qualifying car.

VAT may be recovered on the purchase of a pool car provided it remains unavailable for private use at all times, which should be determined by considering factors such as whether it is normally kept at the company's place of business, allocated to a specific individual, or kept at an employee's home.

#### Leased cars

Subject to any partial exemption, companies that lease qualifying cars may reclaim 50% of the VAT charged on the rental. However, all of the VAT may be recovered if the leased car is used exclusively for the purposes of the business and is not available for any private use, or is intended to be used primarily as a taxi or driving instruction car.

#### Other costs

Any VAT incurred on costs such as maintenance, or fuel used for business purposes, may be reclaimed in full, subject to any partial exemption limitation of the company.

# £3.50

'Free fuel' could cost as much as £3.50 per litre.

*"Buying out free fuel may well be the best financial and tax efficient move for both employer and employee"*

## NATIONAL INSURANCE CONTRIBUTIONS

#### Cars

Employers pay Class 1A NIC on most employee benefits including company cars and private fuel. It must be settled in one payment in July. Each year the charge is calculated by multiplying the employee's benefit-in-kind (BIK) by the maximum employer's NIC percentage, which is presently 13.8%. For this tax year, the Class 1A NIC for a company car with an average list price and CO<sub>2</sub> emissions would be calculated as follows:

List price	£27,742
CO <sub>2</sub> emissions	128g/km
Fuel	Diesel
Appropriate (BIK) percentage	21% (including 3% diesel supplement)
BIK	£5,825.82 (£27,742 x 21%)
Class 1A NIC	£803.96 (£5,825.82 x 13.8%)

As the employee's BIK determines the employer's Class 1A NIC liability, the lower the employee's BIK the lower the employer's Class 1A NIC.

#### Employer-provided fuel

If a company provides free, or subsidised, fuel for a company car driver's private use it must pay Class 1A NIC on the additional benefit. It is calculated by multiplying the fuel benefit charge multiplier, currently £21,700, by the BIK percentage and the maximum employer's NIC percentage.

This year's Class 1A NIC charge on private fuel provided to the company car driver in the table above would therefore be £628.87 (£21,700 x 21% BIK x 13.8% NIC).

With the fuel benefit charge multiplier set to increase again in April to £22,100, employers should be asking the question:

## IS EMPLOYER-PROVIDED FREE FUEL WORTH HAVING?

As well as bearing the cost of the petrol or diesel, employers must pay Class 1A NIC and apply the VAT scale charge when they provide private fuel to company car drivers and, although some employees may benefit by receiving free fuel, it's likely a significant number will not.

If a higher rate tax payer drives a diesel company car with a realistic 50mpg, CO<sub>2</sub> emissions of 122g/km, travels 10,000 private miles a year and fuel costs on average £1.40 per litre, how much does his 'free fuel benefit' really cost?

**Together they pay the equivalent of nearly £3.50 a litre**

Using a historically high price of £1.40 per litre may seem excessive given oil prices are



### The cost of providing 'free' fuel...

#### To the employer

Annual cost of fuel	£1,273
- VAT recovered	£212
+ VAT scale charge	£156
+ Class 1A NIC	£599
= Sub total	£1,816
- Corporation tax relief	£381
<b>Total cost of providing fuel</b>	<b>£1,435</b>

#### To the employee

Income tax charge:	
Fuel benefit multiplier	£21,700
x BIK	20%
x employee tax rate	40%
<b>Total tax charge</b>	<b>£1,736</b>

**The tax charge to the employee is £463 more than the actual cost of the fuel**



## DRIVER TAXATION

### Benefit-in-Kind (BIK)

BIK arises when a car is provided for the private use of a director, or employee earning over £8,500 a year, by reason of employment without transfer of ownership.

### How is the tax due on the BIK calculated?

Broadly, in its simplest form it is calculated by multiplying a car's list price by a percentage based on its CO<sub>2</sub> emissions and the employee's tax rate. The monthly income tax this year for a 20% tax payer, driving a Ford Focus Ecoboost, a typical company car, is:

List price	£20,990
CO <sub>2</sub> emissions	128g/km
Appropriate percentage	18%
Benefit-in-Kind	£3,778 (£20,990 x 18%)
Income tax	£63 (£3,778 x 20% ÷ 12)

### What's happening over the next few years?

In short, it's going up. The most relevant forthcoming changes are:

#### April 2015:

- the maximum percentage increases to 37%
- two new ultra-low emission bands will be created

#### April 2016:

- the 3% diesel supplement will be withdrawn

Also, over the next four years the BIK percentage will rise year-on-year by 2% for bands exceeding 75g/km, and will increase for the new ultra-low emission bands to give a differential of just 4% between 0g/km and 94g/km by 2019.

### What does this mean for the company car driver?

The tax charge for our Ford Focus driver will increase as follows:

	2014/5	2015/6	2016/7	2017/8	2018/9
Monthly BIK tax	£63	£70	£77	£84	£91

Will such an increase force employees out of company cars? Not necessarily. Our driver's monthly tax increases to just £91 over five years – would he be personally able to buy, insure and maintain that car as cheaply?

HMRC data shows that, as average emissions have fallen, drivers have chosen lower emission cars.

So changing to a Ford Focus TDCi, with CO<sub>2</sub> emissions of 98g/km and list price of £21,190 in 2016 should lower the monthly tax increase to just £8 by 2018/9.

	2016/7	2017/8	2018/9
Monthly BIK tax	£57	£64	£71



currently at a five-year low but, while using lower pump prices reduces the company's cost the employee's tax charge isn't affected, meaning that they pay even more for their 'benefit'.

Even if pump prices continue to fall, the tax on free fuel will rise in April. Opting out should enable drivers to avoid a deliberately punitive tax charge and benefit from significantly lower pump prices, whilst enabling their employers to make significant fuel cost savings, some of which may be shared with the drivers.

There's a simple solution: only one party should pay for the fuel. Buying out free fuel may well be the best financial and tax efficient move for both the employer and the employee.



For more on fleets and tax, visit [fleetnews.co.uk/tax-legislation](http://fleetnews.co.uk/tax-legislation)

- less tax relief is available on the rental of the Škoda due to the lease rental restriction;
- the Class 1A NIC due on the Škoda is nearly three times that of the Peugeot
- the Peugeot should be cheaper to run as lower emissions mean higher fuel economy

So, it's likely that the wholelife costs of the Škoda would be significantly higher than those of the Peugeot. This simple comparison shows that taking account of wholelife costs should be a fundamental requirement for any fleet.

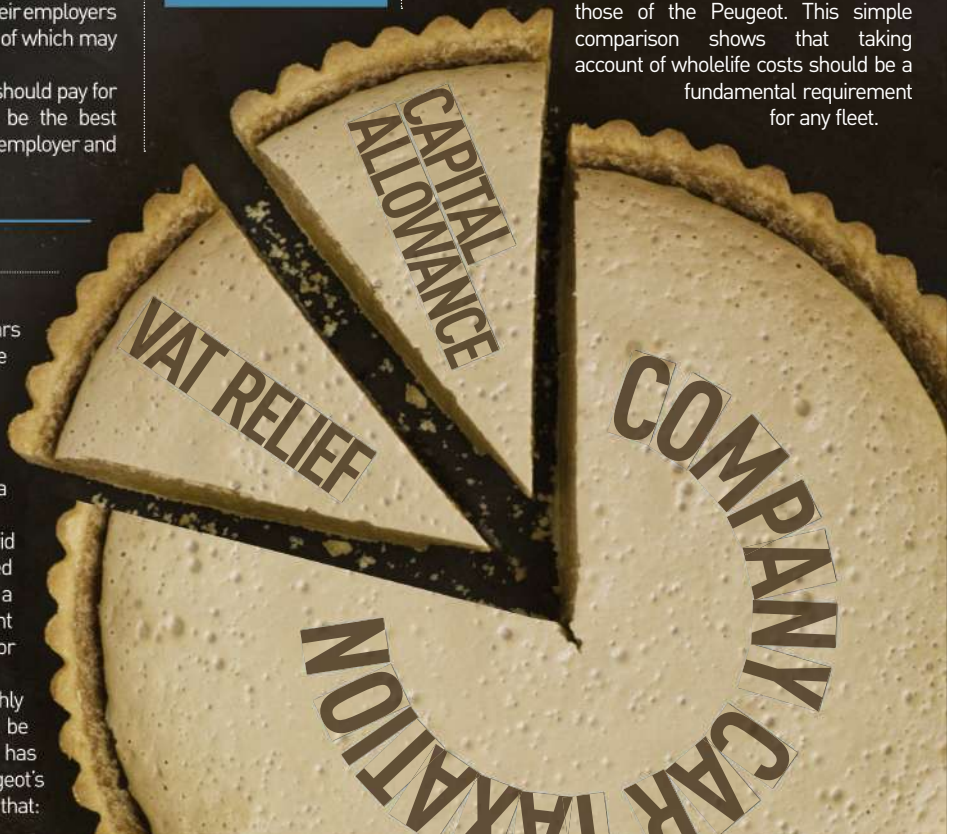
## WHOLELIFE COSTS

### Why are wholelife costs important?

Many companies decide which company cars to acquire by reference to the monthly lease rental or list price. However, using the wholelife cost of a car, including the tax relief available, should show this approach to be flawed and to have little bearing on the true cost of ownership over a replacement cycle.

Recently, a Peugeot 508 RXH HDi hybrid with a list price of £34,155 could be leased over 48 months for £417 per month, and a Škoda Superb 3.6-litre V6 Laurin & Klement with a list price of £34,575 could be leased for £429 per month.

With little difference between the monthly rental or the list prices both cars could be offered on a choice list; but the Škoda has emissions of 217g/km while the Peugeot's emissions are just 104g/km, which means that:





Real time telematics fleet information for a  
**bigger picture**

### A small box that could mean big savings for your fleet

Our Telematics system allows you to track your fleet using advanced black-box technology, enabling you to control costs, monitor driver behaviour and increase productivity. Accessed through an easy-to-use internet based fleet manager portal, you can monitor your drivers in real time or through our comprehensive suite of management reports and dashboards from any PC, tablet or internet enabled phone anywhere in the world 24/7.

Whether you lease your fleet through us or not, our monthly charges are fully inclusive\*, highly competitive and totally transparent. The 'Plug and Play' units are guaranteed for the duration of the agreement or contract term.

\*All prices exclude VAT.

**Find out more about a free Telematics trial call **0870 333 2229**  
or visit [makingleasingsimple.co.uk/telematics](http://makingleasingsimple.co.uk/telematics)**



not exceeding  
**95g\km**  
attract  
**100% WDA**

between  
**96-130g\km**  
attract  
**18% WDA**

above  
**130g\km**  
attract  
**8% WDA**

# How capital allowances will affect your tax relief

*Jeff Whitcombe*, director of BCF Wessex Consultants, demonstrates the impact of vehicle emissions on writing down allowances

Successive governments have proved that they can use taxation to influence behaviour. This has been amply demonstrated in the company car market, which has witnessed a significant reduction in average CO<sub>2</sub> emissions. Figures published by the annual *Fleet News* FN50 leasing report show average emissions of company cars have fallen from 157g/km in 2008 to 122g/km in 2014.

Driver taxation was linked to emissions in 2002 but in 2009, to encourage the continued acquisition of ever lower emission cars, the Government changed the way in which businesses could claim tax relief when it linked the availability of capital allowances wholly to CO<sub>2</sub>.

**18%**  
allowance for cars with CO<sub>2</sub> emissions between 96g/km and 130g/km

### Cars with average CO<sub>2</sub> emissions

Let's assume that on February 1, 2015 a company bought a Volvo V40 D3 SE, after discount, for £23,000. It has CO<sub>2</sub> emissions of 114g/km so qualifies for an 18% writing-down allowance, to be calculated on a reducing balance basis via the main pool (see table below).

Over the period of ownership the company may claim tax relief of £2,233 (£828+£679+£557+£169); that is, its tax bill will have been reduced by £2,233. The remaining tax written-down value of £3,838 will continue to qualify for writing-down allowances until reduced to nil, which could take 40 years.

## WHAT ARE CAPITAL ALLOWANCES?

Capital allowances enable companies to claim tax relief for the depreciation of assets, such as cars, purchased by the business and used in its trade.

The rules summarised on page 42 show when capital allowances may be claimed, and therefore when the company will obtain its tax relief.

As far as company cars are concerned, the rules are designed to promote government policy and encourage the acquisition of low emission cars so, if a company chooses not to fall in line with the government's objective, tax relief is delayed and it could literally take decades for a company to receive all of the tax relief available. It all depends on the CO<sub>2</sub> emissions of the car.

To understand how these rules work in practice, let's initially consider the capital allowances available for a typical company car.

We will then take a look at how the rules favour cars with lower emissions while penalising those with higher emissions.

## CARS WITH AVERAGE CO<sub>2</sub> EMISSIONS

	Writing down allowances	Tax relief claimed at 20%
<b>Year ended 31 December 2015</b>		
Cost	£23,000	
Writing Down Allowance (WDA) at 18%	-£4,140	£828
Tax written-down value carried forward	£18,860	
<b>Year ended 31 December 2016</b>		
WDA at 18%	-£3,395	£679
Tax written-down value carried forward	£15,465	
<b>Year ended 31 December 2017</b>		
WDA at 18%	-£2,784	£557
Tax written-down value carried forward	£12,681	
<b>The car is sold in September 2018 for £8,000</b>		
<b>Year ended 31 December 2018</b>		
Disposal proceeds	-£8,000	
Adjusted tax written-down value	£4,681	
WDA at 18% [£12,681 - £8,000] x 18%	-£843	£169
Tax written down value carried forward	£3,838	

Multiplied across a fleet, this could represent a significant amount of company money tied up in government coffers, for nearly half a century.

### Cars with low CO2 emissions

Companies are incentivised to buy cars with lower CO2 emissions via the 100% first year allowance, which enables a company to claim all the tax relief available in the year in which the car is purchased rather than having to spread the tax relief over several years.

Let's assume that on 1 February 2015, a company bought a Volvo V40 D2 SE Nav, after discount, for £23,000. It has CO2 emissions of 88g/km and so qualifies for the first year allowance:

Year ended 31 December 2015	Writing down allowances
<b>Cost</b>	£23,000
<b>First Year Allowance (FYA)</b>	£23,000
<b>Tax written down value carried forward</b>	£Nil

If the car is then sold in 2018, the disposal proceeds reduce the tax written-down value of other cars and assets in the main pool, which will reduce the tax relief available.

Effectively, the company is given too much tax relief in the year of purchase, which it must repay after the car is sold. However, there is a significant advantage as the excess tax relief is clawed back over a number of years, meaning the money stays in the company and is drip-fed slowly back to the government, over as much as half a century.

### Cars with high CO2 emissions

Companies are discouraged from buying cars with higher CO2 emissions via a special capital allowance rate. Cars with emissions exceeding 130g/km only qualify for an 8% writing-down allowance, which will be calculated on a reducing balance basis via the special rate pool, thereby delivering tax relief to the company over a much longer period, which could be up to 100 years.

Quite simply, for a business to make the most effective use of capital allowances it must choose cars with lower CO2 emissions. As the table below shows, for a company paying corporation tax at the rate of 20%, purchasing a low-emission car in 2014/15 for the average price of a new car means an effective saving of more than £4,500 in the year of purchase. And that's just one car.

## HOW WILL THE RULES CHANGE FROM APRIL 2015?

The 95g/km threshold will be reduced to 75g/km from April 2015. Therefore, in the run-up to the new tax year, fleets may wish to accelerate planned purchases of cars with emissions between 76g/km and 95g/km in order to secure the first-year allowance.

From April 2015, to be able to claim 100% first-year allowances, businesses must think strategically, and decide whether to embrace technology and adopt ultra-low emissions vehicles. This may be best accomplished by evaluating

## COMPARING THE IMPACT OF CO2 EMISSIONS

CO2 emissions	95g/km	130g/km	>130g/km
<b>Purchase price*</b>	£27,742	£27,742	£27,742
<b>FYA/WDA</b>	£27,742	£4,994	£2,219
<b>Tax written-down value carried forward</b>	£Nil	£22,748	£25,523
<b>Tax relief on capital allowances</b>	£5,548	£999	£444

\*Thisismoney.co.uk - average price of a new car September 2013

VW GOLF COMPARISON		VW Golf 1.6 TDi BlueMotion	VW Golf 1.4 TSi GTE		
Purchase price		£21,600	£33,000		
Plug-in car grant		£Nil	£5,000		
CO2 emissions		85g/km	35g/km		
<b>Year to 31 December 2015</b>					
Cost		£21,600	£28,000		
WDA* at 18%/FYA		-£3,888	-£28,000		
TWDDV** carried forward		£17,712	£Nil		
<b>Year to 31 December 2016</b>					
WDA at 18%		-£3,188			
TWDDV carried forward		£14,524			
<b>Year to 31 December 2017</b>					
WDA at 18%		-£2,614			
TWDDV carried forward		£11,910			
<b>Cars sold in 2018 for 35% of purchase price</b>					
<b>Year to 31 December 2018</b>					
Disposal proceeds		-£7,560	-£11,550		
Adjusted TWDDV		£4,350***	£11,550		
WDA at 18%		-£783	-£2,079		
TWDDV carried forward		£3,567	£9,471		
<b>Depreciation</b>		<b>-£14,040</b>	<b>-£16,450</b>		
<b>Tax relief for each year</b>					
	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>	<b>Total</b>
<b>Golf BlueMotion</b>	£778	£638	£523	£157	£2,096
<b>Golf GTE</b>	£5,600	£Nil	£Nil	-£374	£5,226

\*WDA: Writing down allowance \*\*TWDDV: tax written down value \*\*\*=Cost-disposal proceeds-WDA during ownership

**75g/km**  
100% first year allowance threshold from April 2015



For a fleet CO2 calculator, visit [fleetnews.co.uk/CO2](http://fleetnews.co.uk/CO2)

*"To make the most effective use of capital allowances, a company must choose cars with low CO2"*

whether the availability of a first year allowance will offset the additional purchase cost.

For example, after March 2015 would it be more cost-effective for a company to buy a VW Golf 1.6 TDi BlueMotion, or a VW Golf 1.4 TSi GTE? (see table above). Assuming the company pays corporation tax at the rate of 20%, the tax relief available for each car would be as per the above table.

We've presented a simple example in which the additional tax relief of £3,130 available for the Golf GTE over the period of ownership would be sufficient to overcome its higher depreciation.

The Golf GTE should also be cheaper to run than the BlueMotion, but first-time buyers of electric cars will need to consider other issues, such as installation of charging points. Although the GTE should be more cost-effective during ownership, following disposal the company would have to pay back the excess tax relief received in the first year, whereas had it chosen the BlueMotion it would continue to receive the tax relief it is due. So companies need to think very carefully when choosing a car and may need to take account of the 'time value of money', which is discussed on page 48.

# Understanding the time value

*David Rawlings*, tax director at BCF Wessex Consultants, looks into the complexities of future-proofing your fleet

It's usually easy to avoid those seemingly complicated subjects that we believe are best left to accountants or financial advisors, especially when you're immediately faced with acronyms, algorithms and financial gobble-dygook; indeed, the very title of this feature can be far from straightforward. So, in plain English, this article sets out to demonstrate how the true value of a pound in your pocket is different to the value of a pound you might receive at some point in the future.

## WHY IS THE TIME VALUE OF MONEY IMPORTANT?

To begin with, let's look at a common question that most businesses are likely to encounter at one time or another.

Scoop, Muck & Dizzy Ltd is a new company, in which the managing director, Bob, plans to invest all of his own, hard-earned cash as capital. The business will be heavily dependent on the procurement of four vans, which have a total purchase price of £100,000. Bob has two options: should he buy the vans outright, or should he lease them?

At this stage, most accountants might reach for a calculator or open a spreadsheet, but let's simply try to work through this conundrum from first principles.

## GETTING BACK TO BASICS

### Simple interest

Bob might have thought: "Why should I bother starting my own business when I can simply walk down to the bank or building society and invest my money in one of their high interest savings accounts?"

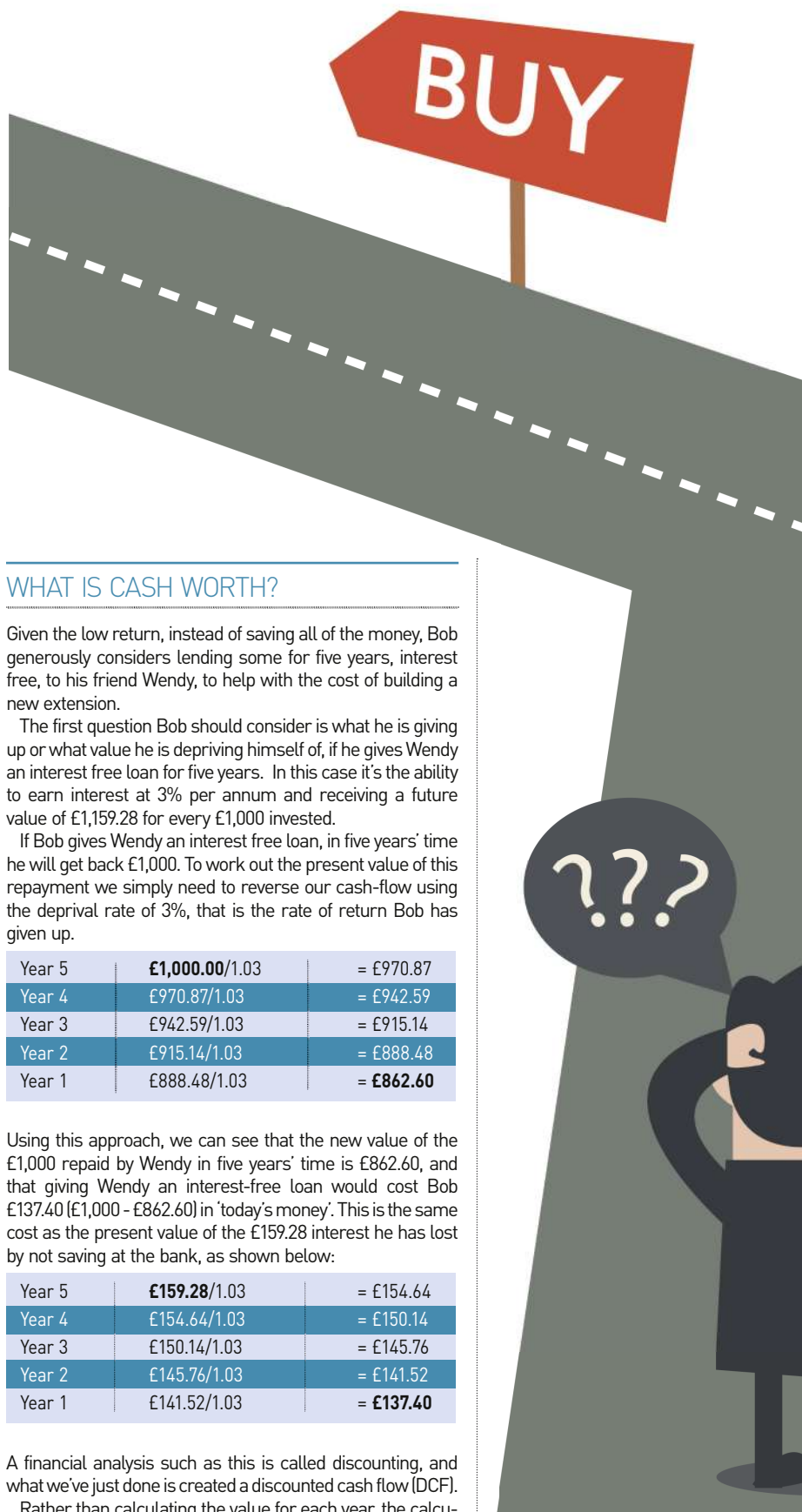
Assuming that he had taken that option and secured an interest rate of 3% a year, it's easy to calculate that after a year every £1,000 invested would have earned interest of £30 which, despite the marketing, is not worth getting excited about.

### Compound interest

Now let's assume Bob is looking to the future. He thinks: "I've got five years until the kids go to university, so I'll leave my money in the bank until then." Now it gets a little bit more exciting because, as well as earning interest on his capital, Bob will earn interest on his interest:

Year 1	£1,000.00 + 3% = £1,030.00
Year 2	£1,030.00 + 3% = £1,060.90
Year 3	£1,060.90 + 3% = £1,092.73
Year 4	£1,092.73 + 3% = £1,125.51
Year 5	£1,125.51 + 3% = £1,159.28

So, by considering one year at a time we have proved that, by year five, the 'future value' of £1,000 would grow to £1,159.28, as the value of money is affected by how long you have use of it and what return you can expect to get from it.



## WHAT IS CASH WORTH?

Given the low return, instead of saving all of the money, Bob generously considers lending some for five years, interest free, to his friend Wendy, to help with the cost of building a new extension.

The first question Bob should consider is what he is giving up or what value he is depriving himself of, if he gives Wendy an interest free loan for five years. In this case it's the ability to earn interest at 3% per annum and receiving a future value of £1,159.28 for every £1,000 invested.

If Bob gives Wendy an interest free loan, in five years' time he will get back £1,000. To work out the present value of this repayment we simply need to reverse our cash-flow using the deprival rate of 3%, that is the rate of return Bob has given up.

Year 5	£1,000.00/1.03	= £970.87
Year 4	£970.87/1.03	= £942.59
Year 3	£942.59/1.03	= £915.14
Year 2	£915.14/1.03	= £888.48
Year 1	£888.48/1.03	= <b>£862.60</b>

Using this approach, we can see that the new value of the £1,000 repaid by Wendy in five years' time is £862.60, and that giving Wendy an interest-free loan would cost Bob £137.40 (£1,000 - £862.60) in 'today's money'. This is the same cost as the present value of the £159.28 interest he has lost by not saving at the bank, as shown below:

Year 5	£159.28/1.03	= £154.64
Year 4	£154.64/1.03	= £150.14
Year 3	£150.14/1.03	= £145.76
Year 2	£145.76/1.03	= £141.52
Year 1	£141.52/1.03	= <b>£137.40</b>

A financial analysis such as this is called discounting, and what we've just done is created a discounted cash flow (DCF). Rather than calculating the value for each year, the calcu-



# Value of money



Calculations could be simplified by using published discount rate tables. In Bob's case, the relevant discount rate for a deprival rate of 3% over five years is 0.8626 which, when multiplied by our future value of £1,000, gives us the present value of £862.60 to the original investment of £1,000.

## WHY IS THIS RELEVANT TO FLEET?

Going back to Bob's original conundrum, he needs to know whether he should lease the vans or deprive his business of £100,000 and buy them outright.

To lease all four vans, his leasing company has offered him a very straightforward deal based on a £20,000 initial deposit followed by three annual rentals of £31,467 (excluding VAT), giving a total over the three years of £114,400. Alternatively, Bob could simply pay £100,000 and avoid paying the interest cost of £14,400.

## WHAT DOES IT COST BOB'S BUSINESS TO DEPRIVE IT OF CASH?

### Lease v buy analysis

In reality, as capital is likely to come from several sources such as bank loans, overdrafts, directors' loans, or other shareholders' funds, working out the true deprival rate of a business is likely to be very complicated.

For the purposes of this exercise let's assume that for every pound of capital he invests in his business, Bob can expect a return of 10%. This is the return on capital used when Bob prepared his original business plan and we will use that as the deprival rate in our lease versus buy comparison.

### Buying the vans for cash

Assume the vans are heavily used and will be worth nothing after three years in the business the cash-flow would be:

Purchase price	Year one	Year two	Year three
£100,000	0	0	0

As Bob invests £100,000 immediately it's apparent that the present value of this single cash-flow is £100,000. If we now allow for the time value of money and the effect of leaving more capital in the business we can consider whether leasing might be a better option.

### Leasing the vans

	Day 1	Year one	Year two	Year three
Deposit/rentals (future value)	£20,000	£31,467	£31,467	£31,467
Discount rate	0	0.90909	0.82645	0.75131
Present value	£20,000	£28,606	£26,006	£23,641

If we add up all of the cash-flows over the period, we arrive at an overall present value of £98,253, a saving of £1,747 (that is £100,000 - £98,253).

Therefore, assuming the vans have no value after three years' use, it's clear that despite having to pay an extra £14,400 of interest, in the long run Bob would be better off leasing. However, if the vans were each worth just £600 scrap value after three years (which is a total present value of £451) then buying would be the better option.

Of course, that's subject to the structure and terms of the leasing agreement - for example, if Bob took out a finance lease for which he may receive some of the sale proceeds these too would need to be taken in to account.

In reality, Bob should consider a range of other costs such as maintenance, fuel and insurance, as well as corporation tax and VAT relief. In fact, he should include anything that has an impact on the amount of cash available to his business.

## IS THIS RELEVANT TO WHOLE LIFE COST CALCULATIONS?

Based upon the above calculations, discounting is only useful when we need to compare significantly different cash-flows. So, to find out whether a leased Ford Focus is more cost-effective than a leased Volkswagen Golf, provided the contract term was the same and all other cash-flows occurred on the same dates, discounting would be unnecessary. The more cost-effective car could be determined merely by adding all of the actual costs, without considering the time value of money.

However, discounting is relevant for lease-versus-buy calculations, because we need to compare fundamentally different cash-flows, which can only be achieved by using a consistent method of valuing money, as shown in the above comparison.

You may not realise it, but discounting will effectively be used by companies who accelerate the purchase of a new car with CO<sub>2</sub> emissions between 76g/km and 95g/km before the start of the new tax year to ensure they are able to claim 100% tax relief in the first year\*, rather than having to claim the tax relief over many years.

## CONCLUSION

Businesses make good financial decisions every day but, when times are tough and margins are being squeezed, good financial planning is always a sound policy and properly considering the time value of money is seldom time wasted.



For more on wholelife costs, visit [fleetnews.co.uk/wholelife-costs](http://fleetnews.co.uk/wholelife-costs)

\*Refer to article on capital allowances for a more detailed explanation of the application of first year allowances

# Tax impact of ECO, cash and salary sacrifice

*Mark Morton*, tax director at Ernst & Young, looks at the alternatives to the traditional company car

**C**ompany car tax has been relatively stable from a UK legislative perspective for a while, but that hasn't stopped a growing number of employees opting for an alternative to a company car when presented with the choice.

However, there are specific tax implications for employees and employers, as this article shows, in considering the common alternatives of cash allowance, employee car ownership and the increasingly popular salary sacrifice.

100%

of tax and NIC must be paid on cash allowances

0%

VAT payable on staff car cash allowances



## CASH ALLOWANCES

The option of a cash allowance in lieu of a company car is the most common alternative offered by employers. Increasingly, it is the preferred option for employees working in all types of company – large, small, private and public sector. While administratively the simplest alternative, a cash option can leave employers exposed in areas of risk management. Difficulty can also arise in actually calculating the amount to be paid.

There are often cost and administrative savings from utilising solutions to pay a flexible allowance and full tax-free mileage rates as opposed to a fixed cash allowance and fuel-only reimbursement levels.

### Tax implications

**Income tax and NIC:** A cash allowance should be paid via the payroll and is subject to income tax and national insurance contribution (NIC) in full.

**Employer's NIC:** As with other remuneration payments, a cost for the employer arises by way of secondary Class 1 NIC at 13.8% via the payroll.

**Corporate Tax (CT):** Similar to other salary costs, a full corporate tax deduction applies on any cash allowances paid to staff.

**VAT:** There is no VAT on staff wages and salaries, including car allowances.

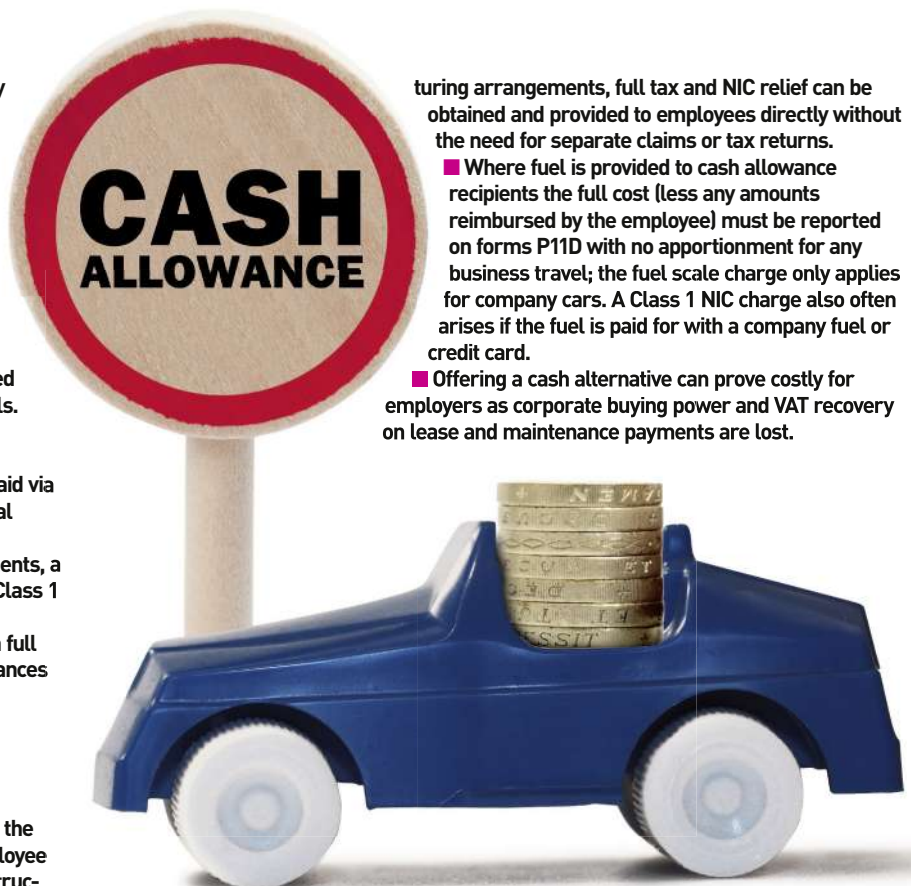
### Points to consider

■ If business mileage costs are reimbursed below the full tax- and NIC-free rates the onus is on the employee to claim any tax relief and NIC relief is lost. By restructur-

ing arrangements, full tax and NIC relief can be obtained and provided to employees directly without the need for separate claims or tax returns.

■ Where fuel is provided to cash allowance recipients the full cost (less any amounts reimbursed by the employee) must be reported on forms P11D with no apportionment for any business travel; the fuel scale charge only applies for company cars. A Class 1 NIC charge also often arises if the fuel is paid for with a company fuel or credit card.

■ Offering a cash alternative can prove costly for employers as corporate buying power and VAT recovery on lease and maintenance payments are lost.



## EMPLOYEE CAR OWNERSHIP (ECO)

ECO arrangements came to prominence with the introduction of the emissions-based system of company car taxation as a way to mitigate the increased benefit-in-kind (BIK) charges. An ECO car looks and feels like a company car with one significant difference – the employee owns the car. As ownership rests with the employee there can be no company car benefit no matter how much support or discount the employer facilitates.

The employee purchases the car under a credit sale agreement and meets the monthly finance and running costs using a mixture of:

- a) The income tax savings from no longer having a company car.
  - b) Maximum tax-free mileage reimbursement for business journeys.
  - c) A top-up payment from the employer via the payroll.
- For the right employers, ECO offers significant cost reductions over a company car, but still provides sufficient risk management safeguards and control over the cars on offer.

### Tax implications

**Income tax and NIC:** Payments under a) and b) above are tax and NIC free, any top up is paid via the payroll subject to income tax and NIC in full.

**Employer's NIC:** Payments under b) are NIC free for the employer; payments via the payroll for c) attract secondary Class 1 NIC at 13.8%.

**CT:** A full Corporate Tax deduction applies for the payments under b) and c).

**VAT:** It is possible to recover VAT on the fuel element of the full business mileage rates under b) with receipts. Again, there is no VAT on any top up paid to staff.

### Points to consider

- Employees may be subject to credit checks in order to secure finance, this can lead to some staff being excluded from the arrangements.
- HM Revenue & Customs has mounted a number of challenges to the operation of ECO, particularly with regard to NIC on mileage payments and the frequency of reconciliations. Employers should ensure their arrangements are robust and tax- and NIC-compliant on a regular basis.
- With the significant reductions in CO<sub>2</sub> emissions for many popular company car models, the tax saved from removing the benefit charge is often lower and can mean greater top-up payments are needed from the company, eroding the savings.
- Many ECO schemes have been in place for a number of years and may no longer deliver the original level of savings, particularly where business mileage has reduced.



## SALARY SACRIFICE

Expanding the opportunity to all staff to choose a company car and meet the costs using salary sacrifice has grown in popularity. The arrangements are particularly effective for low-emission cars where the BIK charge is lower than the salary being sacrificed, offering savings for employer and employee. Salary sacrifice also enable employees to benefit from corporate buying power/manufacturer support which would not normally be available in a retail transaction.

As with all arrangements combined with a salary sacrifice, careful consideration must be given to not only the financial and tax aspects, but also employment law and any wider impact on income and benefit entitlements.

### Tax implications

**Income tax and NIC, Employer's NIC and CT:** The car provided and funded by the employee's sacrifice is taxed as a regular company car and is subject to the same rules as set out on pages 42-44.

**VAT:** HMRC is currently reviewing the position on VAT recovery for leased cars; particularly where provided in conjunction with a salary sacrifice which equals or exceeds the cost of the cars. In this case, one option being considered is for the employer to recover the VAT incurred on the full cost of the car (i.e. on both the lease and the maintenance charges). However, the corollary is that VAT would be payable on the amounts sacrificed by the employees, thus removing the current 50% VAT efficiency, increasing overall costs to the employee and eroding savings.

There would be several issues to iron out around any change in HMRC policy, for instance how to determine the cost of providing a car to an employee. So in the meantime businesses await an update with bated breath.

### Points to consider

- Opening up the company car fleet to the wider workforce can create a real difference to recruitment and perhaps increase current discount levels.
- Managing periods of absence and sacrifices when on low or zero pay over such a long period can present national minimum wage and other legal challenges.
- Managing early terminations and other causes of the employment ending.
- A fleet provider experienced in operating salary sacrifice is crucial, as is a way staff can review cars and costs via sacrifice compared with running a car privately.

# 13.8%

secondary Class 1 NIC payable for Eco payments via the payroll

## CONCLUSION

The tax position around company cars and alternative arrangements varies and no one solution will meet every employer's or employee's demands, but now is the time to address the position.

As the economy improves and the need to attract and retain staff increases in order to facilitate growth, company cars (whether business need or perk, or salary sacrifice related), structured alternatives such as ECO and cash allowances will be an essential element of the overall reward package for an 'employer of choice'.

Employers should design and implement company car and/or cash allowance arrangements, and also address historic risk and reporting issues.

Those who are best-in-class in the area of cars and cash allowances typically offer a variety of options, but it is essential to understand the tax implications of any choice and which staff groups are suited to each. This generates a real win-win solution for both employer and employee.



For more on tax, visit:  
[fleetnews.co.uk/](http://fleetnews.co.uk/)  
tax-legislation



# Are ULEVs a tax-efficient option as a company car?

Ultra-low emission vehicles are a hot topic, but you must consider the full financial implications before adding them to your fleet, says BCF Wessex's *Jeff Whitcombe*

**T**he Government is serious about supporting ultra-low emission vehicles (ULEVs). In 2014 it announced it would invest £500m to boost the sale of ULEV between 2015 and 2020, including the plug-in grant of up to £5,000 for cars (available for 24 models at present). The Government has also extended the ability to claim 100% capital allowances on cars with CO2 emissions below 76g/km until 2018.

In fleet, pure electric vehicles (EVs) and plug-in hybrid electric vehicles (PHEVs) are a hot topic: with more than 600,000 sold worldwide to date, they represent the technology companies must currently embrace to build the most tax-efficient fleets.

With more than 30 derivatives available in the UK already and with another eight launches scheduled this year, 2015 is set to be a bumper year for such cars.

It's clear these vehicles are becoming more popular but adopting them may not be as straightforward as companies might think – as some have already found to their cost.

EVs and PHEVs seem to offer an impressive number of advantages but do they offer a winning position when compared with a conventionally-powered car with sub 100g/km CO2 emissions?

In April 2015, if one company purchased an Audi A3 e-tron and another purchased an Audi A3 1.6 TDI S Line, what would their post-tax costs be in the first year? Look at our comparison below, but read on to get the whole picture. Clearly other costs, such as maintenance, insurance and VED, will be incurred but let's just consider the costs that should influence the buyer's decision.

Tax year	2015/16		2016/17		2017/18		2018/19	
	e-tron	S Line	e-tron	S Line	e-tron	S Line	e-tron	S Line
Tax relief	£5,979	£898	£0	£736	£0	£604	£0	£495
Class 1A NIC	£241	£585	£337	£551	£433	£620	£626	£688
Business Fuel	£500	£1,300	£500	£1,300	£500	£1,300	£500	£1,300
<b>Total annual cost</b>	<b>£5,238</b>	<b>-£987</b>	<b>-£837</b>	<b>-£1,115</b>	<b>-£933</b>	<b>-£1,316</b>	<b>-£1,126</b>	<b>-£1,493</b>

*“HMRC does not regard electricity as a fuel”*

Over the four years, taking account of tax relief, taxes and fuel costs, the net position for the e-tron is £2,342 and for the S Line £4,911 (see table above). This differential in favour of the e-tron of £7,253 more than offsets the higher purchase price. But, as with most things in life, comparing the costs of these two cars is not so simple.

## SELLING THE CARS

Uncertain residual values pose a financial risk that should be considered as well as the claw-back of the excess tax relief claimed when the e-tron was purchased.

After the cars are sold, the company that owned the e-tron must repay all the excess tax relief claimed in the first year, on a reducing balance basis at a rate of 18% per year, whereas over a similar period the company that owned the S Line would claim its remaining tax relief, at the same annual rate of 18%.

## FUEL REIMBURSEMENT COSTS

We've assumed a reasonable re-imbursalment rate of 13 pence per mile (ppm) for the S Line and a combined rate of 5ppm for the e-tron, which may or may not be reasonable, but not restructuring the fuel policy before procuring these cars is where companies often encounter difficulties.

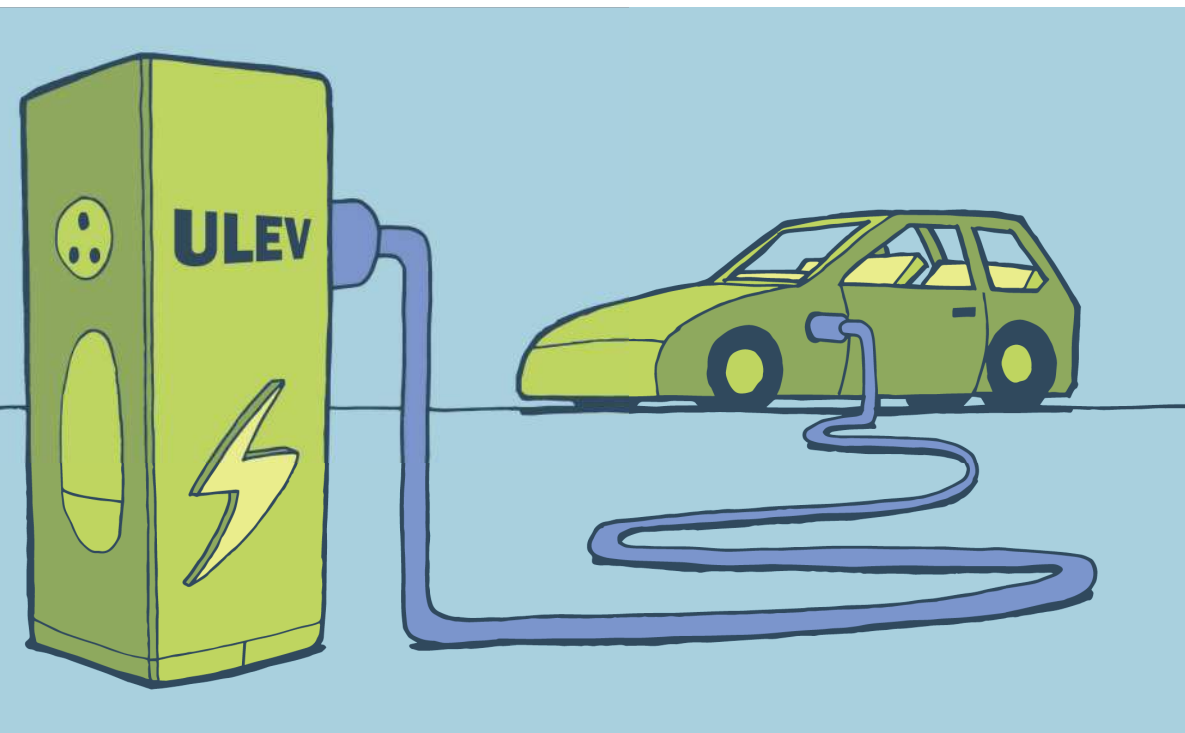
Working out a simple 'pence per mile' plan for a PHEV is a complex issue that can be fraught with difficulties.

Companies generally add PHEVs to their fleets because the low benefit-in-kind (BIK) rate appeals to their employees, but each has a similar story to tell – they hadn't thought about:

- fuel re-imbursalment
- charging points
- how employees would actually use the cars – a daily commute of 30 miles, or daily business journeys over 60 miles, for example

Not solidifying a fuel policy for these cars prior to acquisition is now giving them a headache. Companies should consider restructuring their fuel policy because, for example, drivers may not regularly charge the cars which could significantly affect combined fuel costs.

AUDI A3 COMPARISON: YEAR ONE	Audi A3 e-tron	Audi A3 S Line
CO2 emissions	37g/km	99g/km
BIK percentage	5%	17%
List price	£34,895	£24,940
Plug-in grant	-£5,000	£0
Net price	<b>£29,895</b>	<b>£24,940</b>
Tax relief in first year	£5,979	£898
VED	£0	£0
Class 1A NIC	-£241	-£585
Business fuel (10,000x5ppm)	-£500	-£1,300
<b>Net position</b>	<b>£5,238</b>	<b>-£987</b>



## THE PROS AND CONS OF ULEVs

### Pros

- Plug-in car/van grant
- Domestic chargepoint grants
- 100% first year allowances
- Vehicle Excise Duty (VED) exempt
- Lower running costs
- Cheaper servicing and maintenance
- Congestion charge exempt
- Free and reduced parking fees
- No lease rental restriction

### Cons

- High purchase price
- Grant not deducted from list price for BIK purposes
- EV range anxiety
- Lack of HMRC guidance on fuel reimbursement
- Battery life
- Uncertain residual values

## HMRC'S DEFINITION OF FUEL

HMRC does not regard electricity as a fuel. In some ways this is good news because the fuel benefit charge cannot apply to EVs so an income tax charge cannot arise when an employer provides, or pays for, the electricity required to recharge a pure EV.

But HMRC will not permit the advisory fuel rates (AFRs) to be used for electric cars. So, if the cost of either business or private mileage must be reimbursed, an employer should agree the cost (per mile) of the electricity used with HMRC. Using manufacturer's data, this should be a straightforward process for pure EVs, but it's much more difficult for PHEVs.

## SETTING A FUEL POLICY FOR PHEVs

Whether an employer provides free fuel to their employees or not, setting a fuel policy and gauging a reasonable 'pence per mile' are complex problems; to get it right an employer would have to consider:

- The length of journeys that will be undertaken on a day-to-day basis
- The range of a fully-charged battery – around 30 miles?
- How effectively the battery can be re-charged while being driven

### When both sources of power are used:

- What will the ratio of electricity to fuel be?
- Will the manufacturer's combined ratio represent the mpg of a typical business or private journey?
- Should you assume the first 30 miles of every journey is powered by electricity?
- Ensure the number of journeys undertaken is provided by the driver as well as the mileage driven

Employers will also have to consider how employees can be encouraged to charge and optimise the use of batteries. For instance, how often the battery will need to be charged at a charging point, the different costs of charging at home, work, or public charging points, and whether the main charging point will be on company premises.

### If employees are expected to charge the cars at home:

- How will the cost of electricity be proved?
- Would the employer pay to install a dedicated charging point, and should that be classed as a business or domestic supply because the VAT rate will differ?
- Whether to pay an annual allowance instead of reimbursing the cost of electricity

As well as all of these financial issues, employers should consider practical challenges such as the number of charging points needed on company premises to cater for all the cars that would need to use them.

Alternatively, if an employer installed dedicated charging units at employees' homes an itemised cost of charging an EV or PHEV would be available.

This is a surprisingly inexpensive option using a scheme such as that operated by British Gas, in partnership with several manufacturers. Take a look at: [britishgas.co.uk/energy-saving-products/electric-vehicles](http://britishgas.co.uk/energy-saving-products/electric-vehicles)

## WHAT BCF WESSEX THINKS ABOUT FUEL POLICIES

Gauging a reasonable 'pence per mile' for a PHEV may not be straightforward. But equally it may not be the headache it first appears, because adopting sensible, robust assumptions about car usage should enable a reasonable electricity/fuel ratio to be calculated.

Strictly speaking, as HMRC allows the AFRs to be used for hybrids, for simplicity employers could use the AFRs for PHEVs, but should bear in mind this option may be more costly than calculating the actual pence per mile.

## CONCLUSION

The ULEV is an increasingly popular major innovation. We like them and are even considering adding one to our own very small fleet. We think businesses may now see past the high purchase price and uncertain residual value, but as well as considering the costs and the employee benefits, we would advise employers to identify and resolve all of the practical, day-to-day issues before plugging in.

£500m

pledged by the government for ULEV investment

600,000

PHEVs and EVs sold worldwide to date



For a fleet CO<sub>2</sub> calculator, visit [fleetnews.co.uk/CO2](http://fleetnews.co.uk/CO2)