LeasePlan

What's next?

Comprehensive Guide to Fleet Funding and Taxation

2020/21 Guide

Produced in association with

Deloitte.

About this guide

The guide was published on 23 June 2020 and is designed to be an easy-to-follow explanation of how the UK's tax system affects company vehicles in areas ranging from fleet finance to HR and benefits.

We understand that the provision of car scheme arrangements can be a complex area to understand with significant implications for cost, employee engagement, environmental footprint and administration. As a result, it is an area that companies will want to get right.

There are many different taxation rules and these are often interlinked with additional commercial and operational considerations that can impact the cost and effectiveness of a car scheme. Therefore, it is important for companies to take a holistic approach to managing their arrangements to make sure that their choices will deliver a car scheme that is right for the company and its employees, now and in the future.

To help highlight some of the key issues relevant for company car provision, we have prepared three case studies, each looking at different aspects of company car provision. For each case study, the introduction and assumptions set the scene, with the results and observations providing insight into the key issues relevant for car scheme arrangements today.

We hope you find it a useful reference to the key tax and technical issues that you face when you are thinking about your fleet.

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Welcome

Welcome to the 2020/21 edition of the LeasePlan guide to funding and taxation, produced in association with Deloitte.

In my foreword to the last guide, I highlighted some of the big events we had seen since the previous edition – in particular, a new Prime Minister, Brexit and the Government losing its majority. How things haven't changed! In 2019, we had another new Prime Minister and more Brexit, but at least the Government now has a working majority.

The strange point, though, from a fleet perspective is that 2019 was pretty much the year that wasn't, as a lot of the things that were meant to happen, didn't – though we should see them in 2020 (or later). You won't be surprised to hear that this uncertainty hasn't been ideal for fleets, just as it hasn't been great for other businesses around the country.

One announcement that did arrive, albeit after years of waiting, were the Company Car Tax (CCT) rates for 2020-21 and beyond. These were required because WLTP (the new emissions testing regime) records higher CO_2 scores than the old regime, so it threatened to push some vehicles into higher tax bands than they previously occupied. Many fleets and motorists were understandably concerned, which led to the Government making CCT rates more lenient for the next few years.

However, this regime has still had a significant effect on the motor industry as a whole, with many vehicle manufacturers rethinking their entire lines. Some models and engine types have been withdrawn altogether, while others have effectively been put up for review. This has affected vehicle supply and delivery times. WLTP was also a milestone moment in another way. It represented the first time that company cars would pay no tax at all, as long as they are zero-emission or hybrids with an all-electric range of 130 miles.

This was part of a wider legislative drive that has been gathering momentum for several years and aims to encourage greener motoring. It includes everything from a new system of Vehicle Excise Duty to grants for electric vehicles and charge points. There was also the launch of London's Ultra-Low Emission Zone (ULEZ) and the continuing development of Clean Air Zones (CAZs) around the country, with dozens set to be introduced in 2020 and 2021. It looks likely that they will all will be different from each other in various ways, which leads to an important point; no two fleets will be affected by CAZs in the same way.

At LeasePlan, we are fully committed to the electric revolution. Not only are we a founder member of the EV100 initiative, all our employees will be driving electric cars by 2021 and our entire fleet will be electric by 2030. What I find particularly encouraging is that we're not doing this in the face of opposition from our customers. We're being encouraged all the way.

It helps that the upfront costs of electric vehicles are coming down, while range and vehicle choice are rising and the charging network is expanding. However, there is still a long way to go – and issues to address. One shift that we've seen recently is that people are now less worried about range and more concerned about charging. There's also still confusion about the grants and programmes that are on offer, as well as whether electric vehicles are suited to the day-to-day work of busy, commercial fleets. We plan to address these concerns in the coming months and I would say that although electric vehicles won't be for every fleet just yet, this might be the time to starting considering if they are right for yours.

If you'd like help with this decision, or support with anything else fleet related, please get in touch with our consultants. I also hope you find this guide useful, as it explains tax rules and changes, as well as exploring how these can affect fleets.

Matthew Walters
Head of Consultancy and Data Services - LeasePlan UK

The Finance Bill 2019/20 and rules for company cars

Introduction

The way in which vehicles' emissions are measured has changed – and so too has the tax system. At Autumn Budget 2017, the Government announced that cars registered from April 2020 will be taxed according to the CO_2 figures that result from the newer Worldwide Harmonised Light Vehicle Test Procedure (WLTP). Over the past few years, changes have been made to move towards the full adoption of the new testing regime, with the move to vehicle taxes based on WLTP being one of the final steps.

However, the move to WLTP has resulted in some challenges. For vehicle manufacturers, it has created the challenge of retesting large numbers of vehicles under the new regime, and has led some models and engine types to be withdrawn altogether. For leasing companies and their customers, this has caused supply issues and, in some cases, a rise in company car taxes even during the transition period.

Following feedback from manufacturers, fleets and employees about the issues they were experiencing, the Government announced a review into the impact of WLTP on vehicle taxes at Budget 2018. In July 2019, the Government published the outcome of their review, along with draft legislation intended to manage the final stages of the transition to the new WLTP emissions testing regime. These changes, along with some additional announcements relevant for company cars, were confirmed in the Budget announced on 11 March.

Headlines

The key announcements affecting company cars schemes in the Budget 2020 were:

- The introduction of a new lower rate of company car tax for zero-emission vehicles that is likely to provide a strong financial incentive for employers and employees. There will be no company car tax due for these cars in the 2020/21 tax year, with rates only rising slightly to 1% and then 2% in the following two tax years where they will be frozen for a further two years;
- Plug-in Hybrid Electric Vehicles (PHEVs) with CO_2 emissions at 50g/km or below can also benefit from a considerably lower tax cost than Internal Combustion Engine (ICE) only equivalents;
- For cars registered before 6 April 2020, the company car tax rates will be frozen at the 2021/20 levels for four further tax years (until at 6 least April 2025). These cars will continue to be taxed according to the CO_2 figures achieved under the current New European Driving Cycle (NEDC) testing regime;
- For cars registered on or after 6 April 2020, most company car tax rates will drop by two percentage points for the 2020/21 tax year, before increasing by 1 percentage point in each of the following two tax years, so that by April 20230 they are aligned with the rates for cars registered before 6 April 2020. These cars will switch to being taxed according to the CO_2 figures calculated under the new WLTP testing regime;
- Changes were announced to reduce the CO_2 emissions thresholds affecting corporation tax on company cars from April 2021;
- From 6 April 2021, the van benefit charge for fully electric vans will be nil;
- The existing Vehicle Excise Duty (VED) rates will continue after April 2020, with increases to the published rates announced for the 2020/21 tax year; and
- A call for evidence will be published later in 2019, seeking views on a more dynamic approach to VED that would recognise smaller changes in CO_2 emissions.

Further detail on how company car tax is calculated, as well as full tables of expected future rates, can be found later in this guide.

Observation:

The announcement of the 0% company car tax rate for zero-emission vehicles, as well as lower tax rates for some PHEVs, signals clear support for the Government's 'Road to Zero' objective. In the next five tax years, the maximum rate of company car tax for fully electric vehicles will only be 2%. The low rates of company car tax, as well as other cost savings like fuel and corporation tax relief, are likely to give companies and employees serious cause to consider zero emission Electric Vehicles (EVs) and some PHEVs.

For cars registered before 6 April 2020, the freezing of company car tax rates is likely to be welcomed by businesses and employees who have seen the costs associated with company cars rising steadily over recent years.

Looking ahead to cars registered on 6 April 2020 or later, the announcement of a reduced rate of company car tax for two years is intended to help mitigate from the effect of the move to WLTP for the purposes of taxation. However, the overall impact on tax costs will also depend heavily on the extent to which published CO_2 figures increase as a result of moving to the WLTP testing regime.

With rates now known up to 6 April 2025, there should be a period where companies and employees have clarity and certainty when making choices about their car scheme arrangements.

Taxation considerations for company fleets

The impact of direct and indirect taxation on company car fleets is complex. In the sections that follow, we will explain the key mechanics of taxation affecting company cars, along with worked examples.

What is tax relief?

A company is subject to corporation tax on the taxable profits it makes as a result of doing business. In broad terms, taxable profits are calculated as income less expenses, subject to certain tax adjustments. So, if a company incurs a tax-deductible cost that reduces its profits, this will also reduce the amount of corporation tax it will pay – when this happens we say that the company has obtained 'tax relief'.

If a business is a sole trader or partnership, then it should still receive tax relief when it incurs costs, but because the business is not structured as a 'company', the precise nature of the tax relief differs from that for a company. The end result, however, is broadly the same. Also, there are some organisations, such as charities and some public sector bodies, where tax relief is not applicable as they are not subject to tax on their profits, but the rest of the information will still make a handy guide.

The current main rate of corporation tax, as of 1 April 2019, is 19%. As announced in the Budget, the rate will remain at 19% from 1 April 2020.

On the face of it, the calculation of tax relief for the cost of providing company cars should be relatively simple. However, the devil is in the detail. There are a couple of added complications for a company to consider, depending on whether it leases or buys its cars and on the CO_2 emissions of cars provided.

From 1 April 2019 to 31 March 2020:

Corporation tax rate	
Main Rate	19%

How is tax relief calculated for a company that leases its company cars?

If a company leases its cars, then the finance element of the lease rentals it pays is a cost that can be offset against profits, typically in the year they are incurred. However, if the timing of the lease rentals is uneven (for instance, if there is a large upfront or final payment), the tax relief will be spread evenly throughout the lease period rather than given when the cost of the lease rentals is incurred.

Currently, if the car has CO_2 emissions of 110g/km or below, then the full cost of the finance element of the lease rental will attract tax relief. However, where a car has CO_2 emissions above 110g/km, there is a flat-rate reduction of 15% in the value of the lease rentals that can be considered for corporation tax relief purposes. The end result is that leased cars with CO_2 emissions exceeding this threshold attract less corporation tax relief making them more expensive to provide. In the Budget, it was announced that April 2021, the CO_2 emissions threshold for the leasing rental restriction will drop from 110g/km, to 50g/km.

Leasing rental restriction:

CO_2 emissions (g/km)	Allowed rentals	Disallowed rentals
110 or below	100%	0%
Above 110	85%	15%

Let's look at some examples

To help illustrate how this might look in practice, we have two examples that cover cars both below and above the current CO_2 threshold. These show how tax relief would be calculated and the potential impact on the cost to the company of employees choosing cars with different CO_2 emissions.

Example 1: Tax relief for a leased car with CO_2 emissions of 105 g/km

A company leases a car using contract hire for a 36-month term with monthly lease rentals of £400 (for simplicity, in the examples we will assume the first lease rental is paid in the first month of the company's financial year).
The CO_2 emissions are below the 110g/km threshold and so there is no lease rental disallowance to consider.

The calculation of tax relief for lease rental costs each year is:

	Yr 1 (FY19)	Yr 2 (FY20)	Yr 3 (FY21)	Overall
Lease rentals for tax relief	£4,800	£4,800	£4,800	£14,400
Corporation tax rate	19%	19%	19%	
Tax relief received	£912	£912	£912	£2,736

Example 2: Tax relief for a leased car with CO_2 emissions of 115 g/km

A company leases a car using contract hire for a 36 month term with monthly lease rentals of £400.
The CO_2 emissions are above 110g/km and so there is a 15% lease rental disallowance on the tax relief that can be claimed.

The calculation of tax relief for lease rental costs each year is:

	Yr 1 (FY19)	Yr 2 (FY20)	Yr 3 (FY21)	Overall
Lease rentals for tax relief	£4,800	£4,800	£4,800	£14,400
Corporation tax rate	19%	19%	19%	
Tax relief for lease rentals	£912	£816	£816	£2,544
Less leasing disallowance	(£137)	(£137)	(£137)	(£410)
Tax relief received	£775	£775	£775	£2,326

Observation:

Comparing the tax relief received by the company in the two examples shows that the car with CO_2 emissions below the 110g/km threshold attracts additional tax relief for the company of £410 over the contract term. This means that it would be more expensive, after accounting for corporation tax, to provide the company car in example 2, even though the lease rental costs are the same.

What other tax relief considerations are there for leased cars?

When examining the tax relief implications of leasing company cars, there are some further considerations worth bearing in mind. These include:

Q. What funding methods are considered leases?
A. Where we refer to a lease in this guide, we will be talking about contract hire (also known as operating lease) or finance lease. Further details on these can be found in the section on funding options.

Q. Is tax relief calculated on the VAT exclusive or inclusive lease rental?
A. A company can claim tax relief on the lease rental charges after the recovery of any applicable VAT.

Q. Should I worry about capital allowances for leased cars?
A. Broadly, a company cannot claim tax relief through capital allowances on leased cars as capital allowances can only be claimed on company cars that are purchased.
However, it is important to be aware that where leasing companies purchase cars to lease to their customers the lease rentals charged may reflect the tax relief that the leasing company can claim through capital allowances. Therefore, even if capital allowances do not directly impact the company leasing its cars, there may be some benefit from understanding how capital allowances work.

Q. What is the impact on tax relief if I pay a deposit or a number of lease rentals in advance?
A. Generally, a tax deduction is available for an expense when that expense is included in the company's profit and loss account in its financial statements (under Generally Accepted Accounting Principles [GAAP]).
What is generally not permitted is a tax deduction for lease rentals on the basis of when they are due for payment. This is particularly true for leasing agreements where a large initial payment is made. In such lease agreements, the total lease rentals payable should be spread over the period of the lease (for both accounting and tax purposes).

Q. Can the company own the car at the end of the lease?
A. No. To be treated as a lease there must be no option for the company to purchase the car at the end of the lease term. If a company had such an option, the agreement would change from a lease to a deferred purchase, which would alter the accounting treatment. It is important to note that this does not prevent the individual driver from purchasing the vehicle directly from the lease provider.

How is tax relief calculated for a company that purchases its company cars?

When a company purchases a fixed asset, such as tools, machinery or a car, it is not usually possible to deduct the entire expenditure on the asset from the profits straightaway on the basis that it represents capital expenditure. Instead, tax relief is calculated for qualifying capital expenditure by way of capital allowances, which effectively spreads the amount of tax relief that can be claimed over a number of years; as opposed to the depreciation for accounting purposes, which is generally not deductible for tax purposes.

With company cars, there are special rules dictating the amount of capital allowances that can be offset against profits each tax year. This amount is calculated as a percentage of the car's value, and the specific percentage is known as a Writing Down Allowance (WDA.. Capital allowances are calculated on a 'reducing balance' basis. This means that the WDA percentage is applied each year to the remaining balance of unrelieved expenditure. The value of the car for tax purposes, after the WDA has been applied each year, is known as the Tax Written Down Value (TWDV).

As with leasing, the rules governing the calculation of capital allowances for purchased cars are structured to encourage the use of vehicles with lower CO_2 emissions. The table (on the right) shows the WDA rates applicable from FY19 onwards based on the car CO_2 emissions. It is important to note that, unlike any leasing disallowance, the rules for capital allowances affect the timing of the tax relief a company receives, rather than the total amount of relief a company can claim in all years.

In order to simplify the process of tracking tax relief for cars purchased, all cars that do not receive 100% WDA are put into one of two tax pools (sometimes called an asset pool) based on their CO_2 emissions. The two asset pools used are called the 'main rate pool' where the WDA is 18%, and the 'special rate pool' where the WDA is 6% (this was previously 8% before April 2019). If a car is purchased, the cost is added to the relevant pool. Then, when a car is sold, the sale proceeds are deducted from the relevant pool. The appropriate WDA is then applied to the total value of each pool at the end of the company's tax year.

From April 2019:

g/km of CO_2	WDA rate %
50 or below	100%[1]
51 - 110	18%
Above 110	6%

[1] Relief provided for full purchase price in year 1.

From April 2021:

g/km of CO_2	WDA rate %
0	100%[1]
1 - 50	18%
Above 50	6%

[1] Relief provided for full purchase price in year 1.

Let's look at some examples

To help illustrate how this might look in practice, we have three examples, one for each WDA rate. They show how tax relief would be calculated and the potential impact for the company of employees choosing cars with different CO_2 emissions. The applicable g/km rates are for the tax year 2019/20.

Example 1: Tax relief for a purchased car (CO_2 emissions 50g/km or below)

A company purchases a car for £25,000 outright and keeps it for 36 months, after which it sells the car for £10,000. The CO_2 emissions of the car are 50g/km or below, so it qualifies for 100% first year capital allowances.

The cash flows are as follows:

Year 1: The full purchase price of the car is added to the main pool and 100% of this can be offset against profits to provide tax relief.

Year 2: Full tax relief has already been provided, so no further tax relief is allowed.

Year 3: The car is sold and the sale proceeds are added to the main pool, after which capital allowances for the year are calculated.

Year 4 onwards: The remaining balance of capital allowances due, which in this case is a clawback (as the capital allowances previously claimed are in excess of the fall in value of the car during the ownership period), will continue to be accounted for over time within the main pool.

The cash flows are explained in more detail in the table below:

Year	Yr 1 (FY19) Purchase	Yr 2 (FY20)	Yr 3 (FY21) Disposal	Yr 4 (FY22)	Yr 5 (FY23)
Purchase price	£25,000				
Sale proceeds			(£10,000)		
TWDV	£25,000	£0	(£10,000)	(£8,200)	(£6,724)
WDA rate	100%	0%	18%	18%	18%
Capital allowances	£25,000	£0	(£1,800)	(£1,476)	(£1,210)
Corporation tax rate	19%	19%	19%	19%	19%
Tax relief	£4,750	£0	(£342)	(£280)	(£230)
Cumulative tax relief	£4,750	£4,750	£4,408	£4,128	£3,898
Cumulative tax relief accrued after 75 years[1]			**£2,850**		

[1] Assumes current corporation tax rate of 19% remains unchanged

Example 2: Tax relief for a purchased car (CO_2 emissions 51 - 110g/km)

A company purchases a car for £25,000 outright and keeps it for 36 months, after which it sells the car for £10,000. The CO_2 emissions of the car are between 51g/km and 110g/km and so this attracts a WDA rate of 18%.

The cash flows are as follows:

Year 1: The full purchase price of the car is added to the main pool. Capital allowances will be provided at the main rate of 18%.

Year 2: Capital allowances will continue at the main rate of 18%.

Year 3: The car is sold and the sale proceeds are added to the main pool, after which capital allowances for the year are calculated.

Year 4 onwards: The remaining balance of capital allowances due (which in this case gives further tax relief) will continue to be accounted for over time within the main pool.

The cash flows are explained in more detail in the table below:

Year	Yr 1 (FY19) Purchase	Yr 2 (FY20)	Yr 3 (FY21) Disposal	Yr 4 (FY22)	Yr 5 (FY23)
Purchase price	£25,000				
Sale proceeds			(£10,000)		
TWDV	£25,000	£20,500	£6,810	£5,584	£4,579
WDA rate	18%	18%	18%	18%	18%
Capital allowances	£4,500	£3,690	£1,226	£1,005	£824
Corporation tax rate	19%	19%	19%	19%	19%
Tax relief	£855	£701	£233	£191	£157
Cumulative tax relief	£855	£1,556	£1,789	£1,980	£2,137
Cumulative tax relief accrued after 75 years[1]			**£2,850**		

[1] Assumes current corporation tax rate of 19% remains unchanged

Example 3: Tax relief for a purchased car (CO_2 emissions above 110g/km)

A company purchases a car for £25,000 outright and keeps it for 36 months, after which it sells the car for £10,000. The CO_2 emissions of the car are above 110g/km and so this attracts a WDA rate of 6%.

The cash flows are as follows:

Year 1: The full purchase price of the car is added to the special rate pool. Capital allowances will be provided at the rate of 6%.

Year 2: Capital allowances will continue at the special rate of 6%.

Year 3: The car is sold and the sale proceeds are added to the special rate pool after which capital allowances for the year are calculated.

Year 4 onwards: The remaining balance of capital allowances due (which in this case gives further tax relief) will continue to be accounted for over time within the special rate pool.

The cash flows are explained in more detail in the table below:

Year	Yr 1 (FY19) Purchase	Yr 2 (FY20)	Yr 3 (FY21) Disposal	Yr 4 (FY22)	Yr 5 (FY23)
Purchase price	£25,000				
Sale proceeds			(£10,000)		
TWDV	£25,000	£23,500	£12,090	£11,365	£10,683
WDA rate	6%	6%	6%	6%	6%
Capital allowances	£1,500	£1,410	£725	£682	£641
Corporation tax rate	19%	19%	19%	19%	19%
Tax relief	£285	£268	£138	£130	£122
Cumulative tax relief	£285	£553	£691	£820	£942
Cumulative tax relief accrued after 75 years[1]			**£2,847**		

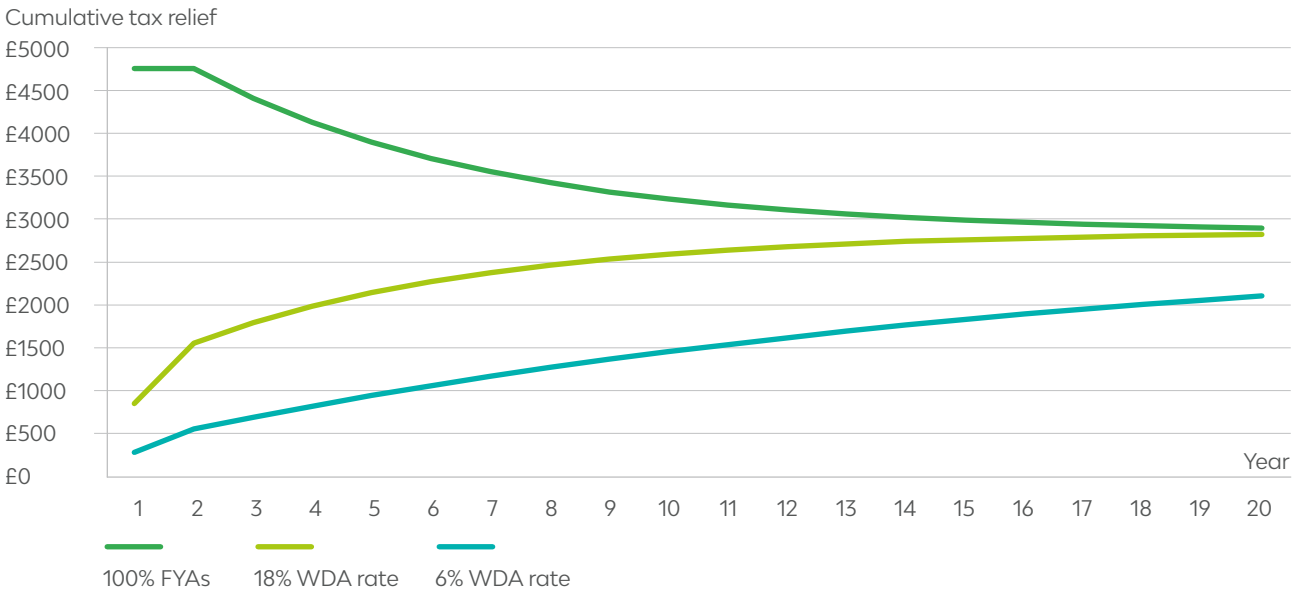
[1] Assumes current corporation tax rate of 19% remains unchanged

Observation:

The tax relief that could be claimed in all three examples will be calculated based on the depreciation in the value of the car. If the rate of corporation tax remains static, the amount of tax relief for each of the three cars will ultimately be the same. However, it is important to note that, because of the way in which capital allowances are calculated, the relief will be provided over a much longer period than the retention period of the vehicle, and so the potential impact on cash flow can be very different.

The chart (below) compares the cumulative tax relief received by the company for the three different rates of WDA and highlights the variations in the timing of tax relief. This can be observed from the lines showing the cumulative relief, which start out at very different levels but, after a number of years, converge at the net cost of the car.

A comparison of tax relief provided via capital allowances



If the main rate of corporation tax was static at 17% for the three examples above, it would take over 70 years for the tax relief received for a car with emissions above 130g/km to catch up with cars with CO_2 emissions of 130g/km or below. This illustrates the degree to which a company's cash flow can be impacted by employees choosing cars with higher emissions.

It should also be noted that, because the main rate of corporation tax is reducing (by 2% in FY20), this will impact the overall amount of relief available. In summary, the reduction to the corporation tax rate increases the financial benefit of a company providing cars that receive tax relief more quickly.

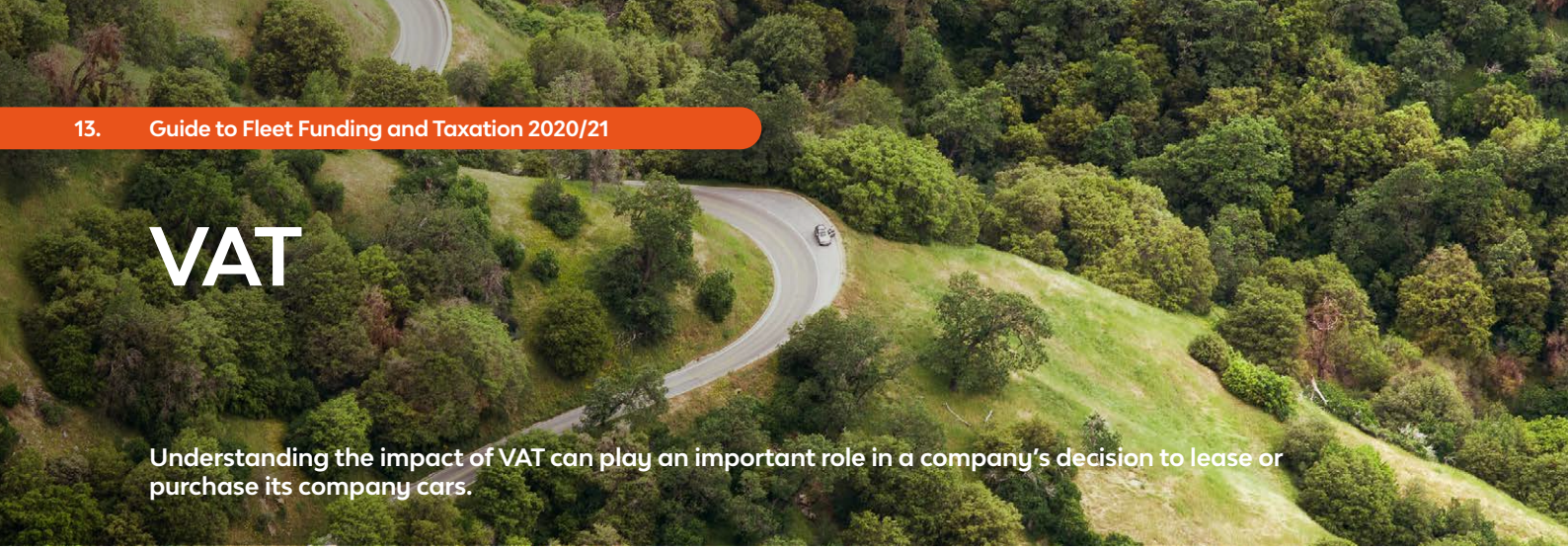
What other tax relief considerations are there for purchased cars?

When examining the tax relief implications of purchasing company cars, there are some further considerations worth bearing in mind. These include:

Q. What funding methods are considered purchases?
A. Where we refer to a purchase in this guide, we will be talking about contract purchase, outright purchase and hire purchase. Further details on these can be found in the section on funding options.

Q. Does the company really get 100% tax relief in the first year on cars with CO_2 emissions of 50g/km or below?
A. Yes, this is correct. The 100% tax relief in the first year is called a first year allowance (FYA. and it is part of a government initiative to encourage companies to purchase cars with lower CO_2 emissions.

Q. Does expenditure on cars qualify for the Annual Investment Allowance (AIA.?
A. No, you cannot claim AIA on cars (this is typically for plant and machinery).



VAT

Understanding the impact of VAT can play an important role in a company's decision to lease or purchase its company cars.

What is the impact of VAT on providing cars?

Following changes to the VAT legislation in 1995, businesses that acquired cars wholly for business use, such as leasing companies, were able to fully recover the VAT element on cars. As a result, the lease rentals charged by leasing companies were reduced and leasing as a funding option became much more popular.

As with tax relief, the impact of VAT for a company providing cars will differ depending on whether the cars are leased or purchased and whether the cars are used exclusively for business purposes.

What does this mean for a business that leases its company cars?

The first step in understanding the VAT treatment for a company that leases its cars is to separate out the cost of funding the car (this will be the lease rentals) and any other expenses related to the car (such as maintenance, repairs etc.) as they are treated differently.

Lease rentals

The first step in understanding the VAT treatment for a company that leases its cars is to separate out the cost of funding the car (this will be the lease rentals) and any other expenses related to the car (such as maintenance, repairs etc.) as they are treated differently.

Other expenses

The agreement that a company enters into for a leased car will frequently include the additional costs of running a car, such as maintenance, repairs and roadside assistance cover. However, as explained above, HMRC currently accepts that the part of the payment that reflects these additional services is not subject to the same block as lease rentals and is eligible for a full VAT reclaim in certain circumstances (again, subject to the company's ability to recover VAT).

To ensure the appropriate balance between lease rental charges and other expenses, HMRC may review any agreements that appear to include a disproportionate element of other expenses. This is to ensure no advantage is made of this concession by inflating the cost of additional services in order to engineer a larger VAT reclaim for the customer overall (and, in effect, lowering the monthly lease rental payments).

It is important to note that the VAT information set out in this section is intended to provide general information only. The VAT treatment may vary depending on specific facts. For example, there are specific rules in relation to VAT recovery for certain public sector bodies. Therefore, specific advice should be sought by taxpayers depending on the use of leased and purchased vehicles.

All references to leases relate to a lease by way of a supply of services (i.e. lease agreements where the lessee has no option to purchase the car).

Let's look at some examples

To help illustrate how this might look in practice we have prepared a couple of examples. These are for businesses with full and partial VAT recovery and show how the leasing costs are treated for VAT purposes.

Example 1: A company with full VAT recovery

A company leases a car using contract hire for a 36-month term with monthly lease rentals of £480 and maintenance costs of £60 (both inclusive of VAT).

VAT recovery rate	**100%**
Lease rentals	
Rental (inc. VAT)	£480
Full VAT recovery	(£80)
50% blocked VAT	£40
Rental (after VAT recovery)	£440
Other expenses	
Maintenance (inc. VAT)	£60
Full VAT recovery	(£10)
Maintenance (after VAT recovery)	£50
Total VAT reclaim	**£50**
Total cost to business after VAT reclaim	**£490**

Example 2: A company with partial VAT recovery

A company leases a car using contract hire for a 36-month term with monthly lease rentals of £480 and maintenance costs of £60 (both inclusive of VAT).

VAT recovery rate	**5%**
Lease rentals	
Rental (inc. VAT)	£480
Full VAT recovery	(£4)
50% blocked VAT	£2
Rental (after VAT recovery)	£478
Other expenses	
Maintenance (inc. VAT)	£60
Full VAT recovery	(£0.50)
Maintenance (after VAT recovery)	£59.50
Total VAT reclaim	**£2.50**
Total cost to business after VAT reclaim	**£537.50**

The monthly cost to the company in example 2, which is only able to reclaim 5% VAT, will be £47.50 higher than the company from example 1, which is able to reclaim 100% VAT, even though the same vehicle is provided in both cases.

What does this mean for a business that purchases its company cars?

The VAT treatment of purchased cars also is different for the purchase of the car and the cost of other expenses incurred, such as repairs and maintenance.

Purchase of the car

No element of VAT can be recovered on payments for a car that is used, or is made available to be used, for private motoring. This broad definition disqualifies most cars from being eligible for a VAT reclaim.

This is a point that a number of companies have contested with HMRC, but with little success. Even in cases where the company has been able to demonstrate that a car was never actually used for private use, the fact that the car was theoretically available for private use has been sufficient to see claims fail at VAT tribunals.

Other expenses

The VAT treatment of other expenses for cars that are purchased follows that of leased cars where a full VAT reclaim can be made on the additional costs of running a car, such as maintenance, repairs and roadside assistance, in certain circumstances.

Understanding company car tax

This section explains why it is important for companies to be aware of the implications of providing company cars to employees and explains how company car tax is calculated.

Why should a company care about company car tax?

In general, where an employee is provided with a benefit paid for by their employer, such as a company car, this is referred to as a Benefit In Kind (BIK). An employee will pay income tax based on the value of the BIKs they receive. In this guide, we refer to the income tax paid on a company car BIK as Company Car Tax (CCT).

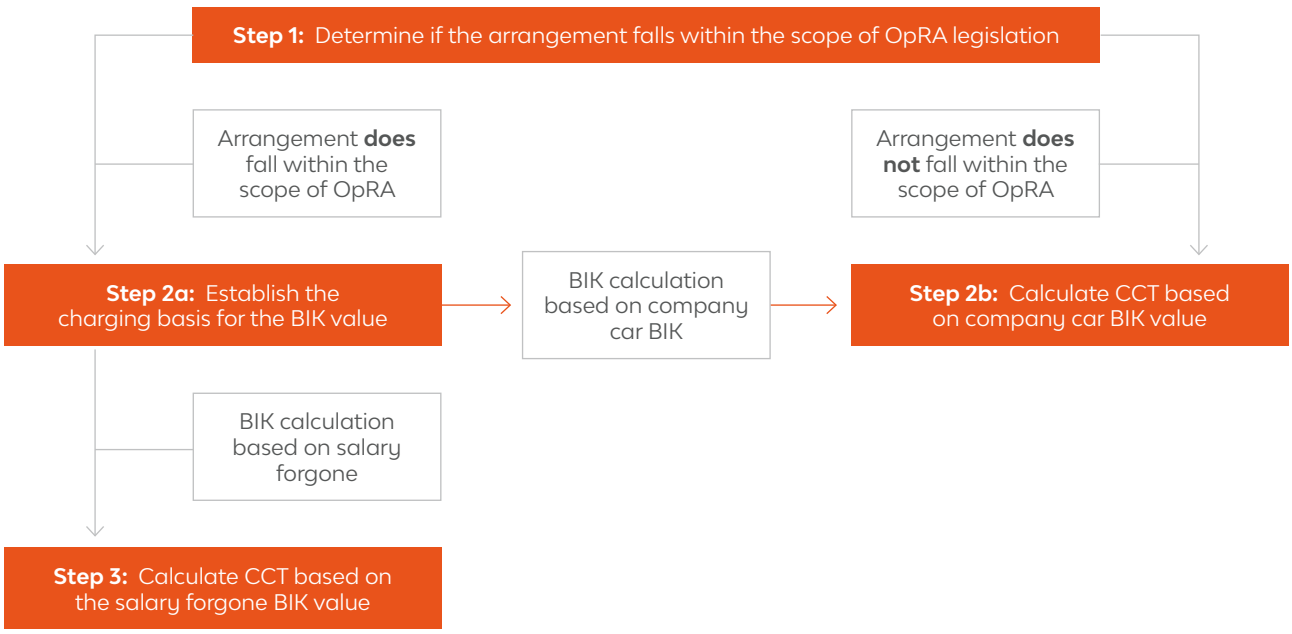
As with other legislation affecting company cars, the current CCT rules are designed to encourage the selection of more environmentally friendly cars with lower CO_2 emissions. Also, with the introduction of the Real Driving Emissions Step 2 (RDE2) standard, the rules now provide a financial incentive to opt for cars with lower Nitrogen Oxide (NO_x) emissions. However, since the introduction of Optional Remuneration Arrangement (OpRA. legislation (in April 2017), the way in which CCT works has become more complex and difficult for companies and their employees to understand.

In general, a company may not normally be too concerned with the amount of tax its employees pay in relation to the benefits they receive. However, where an employer provides a BIK, it will have to pay Class 1A National Insurance Contributions (NICs) based on the value of the benefit provided. So where an employee chooses a company car with higher BIK value, the cost to the business of providing the car will rise, and vice versa. In addition, the rules for calculating the BIK value of company cars can be complex and difficult to understand leaving employees unsure of the financial implications of their choices. Helping employees navigate through this can encourage them to choose cars with lower emissions that can significantly reduce their tax bill, and this in turn can reduce employer costs. Beyond the financial benefits, support and guidance for employees can also lead to a more engaged workforce that better understands and appreciates the benefits they receive.

How do you calculate the company car tax?

At a high-level, the steps involved with calculating CCT can appear to be relatively straight forward although, like choosing a car, it can become much more complicated when you start to look at all the different options available, especially when you take account of the additional rules for OpRA.

The diagram below provides a high-level overview of the steps involved in calculating company car tax



Step 1: Determining if an arrangement car falls within the scope of OpRA

Overview of OpRA legislation

In the Finance Act 2017, new legislation was introduced that changed the way that company car tax is calculated for some company car scheme arrangements. The rules apply for arrangements where an employee has the choice of receiving an amount of earnings (either salary or a cash allowance), which they can opt to forgo in return for the provision of a benefit (the company car). The law describes these as Optional Remuneration Arrangements (OpRAs) and due to the broad reach of these rules, it is important for employers and employees to take the time to understand how the rules work and what it means for them.

Affected arrangements

The two most common types of car scheme arrangements affected by the OpRA legislation are:

- 'Cash or car' type schemes where employees can choose between a company car or a cash allowance; and
- Salary sacrifice schemes used to provide employees with a company car.

In both of these arrangements the employee has the choice between an amount of earnings (either the salary or cash allowance), or the provision of a benefit (the company car). As a result, both types of arrangements fall firmly within the scope of the OpRA legislation. Given how common it is for companies to offer a cash allowance as an alternative to a company car, it is likely that the majority of car scheme arrangements will need to take account of the OpRa legislation in some way.

Also, depending on the way they are designed, OpRA legislation can also affect arrangements that make use of Approved Mileage Allowance Payments (AMAPs) to deliver cost efficiencies. Example of these can include Employee Car Ownership Plans (ECOPs) and optimised cash allowance arrangements. This is because these arrangements are typically structured so as to guarantee the financial position for participating employees by paying employees a mix of AMAPs and an additional cash top-up which may vary each month based on business mileage levels. In certain forms, these arrangements fall within the scope of the OpRA legislation because the employee is participating in an arrangement where they receive a benefit (AMAPs that are treated as a benefit under the OpRA rules) instead of a whole, or part of, a cash allowance (the cash top-up). Therefore, these arrangements fall within the OpRA legislation.

Unaffected arrangements

The OpRA legislation was intended to catch optional remuneration arrangements only. Where employees are provided with a company car and there is no cash allowance offered or salary sacrifice involved then the arrangements fall outside the scope of the legislation and remain unaffected. Examples of these type of schemes seen in practice include:

- Business need fleets, where employees, in a particular job role or grade, are only provided with a company car in order to enable them to carry out their job;
- Segmented fleets, where employees travelling over a specified business mileage threshold are required to take a company car with no option to choose a cash allowance; and
- ECOP arrangements offered by employers to their employees that do not rely on variable cash top ups to meet employee funding requirements.

Ultra-Low Emission Vehicles (ULEVS)

The OpRA legislation includes a carve-out for ULEVs, that is, company cars with CO_2 emissions of 75g/km or less. As a result, these cars are unaffected by the legislation, even if they are provided in a cash or car, or salary sacrifice scheme. The carve-out is intended to promote the adoption of ULEVs by offering employees a financial incentive in the form of lower rates of company car tax, and lower Class 1A NIC costs for employers.

Timetable, transitional rules

The OpRA legislation included transitional rules designed to mitigate the impact of the new legislation for companies and employees already committed to existing arrangements. The transitional rules, also known as 'grandfathering provisions', apply for existing arrangements that were in place before 6 April 2017. The intention of the grandfathering provisions is to allow companies and employees who were already in existing arrangements to see out their commitments under the law that applied when the arrangement was made.

It was accepted by HMRC that an agreement between employee and employer to enter either a salary sacrifice arrangement, or to have ordered a car in a car or cash arrangement before 6 April 2017, would be covered by the grandfathering provisions. Under the grandfathering provisions, arrangements providing company cars continue to be subject to the previous tax rules until the earliest of:

- 5 April 2021 where the benefit provided is a company car;
- The end of the arrangement i.e. when a vehicle lease contract ends; or
- A variation in the terms of the agreement.

Over time, with the churn of company cars being replaced at the end of their contract, the grandfathering provisions have become less relevant, with more cars falling within the scope of the OpRA legislation.

Step 2a: Establishing the charging basis for the BIK value

If a car scheme arrangement falls within the scope of the OpRA legislation then the calculation of the BIK will involve a two-step process to determine the charging basis for the benefit. The two steps involved with the process are:

1. Establishing the charging basis for the BIK; and
2. Calculating the value of the BIK.

While both steps involve the use of calculations that are broadly based on previous company car tax legislation, there are some key differences that need to be taken into account. It is important to note that checking to establish the charging basis company car BIK will have to be performed at least once each tax year if arrangements remain unchanged, and more frequently if any relevant inputs vary mid-year. For example, introducing a revised car scheme policy with changes to cash allowance levels would require a company to reassess how the company car BIK is charged. This process should be relatively simple for cash or car schemes where each tax year can be considered in isolation. However, it is more complex for salary sacrifice because the calculation of the salary sacrifice is typically carried out for a contract term of 24-36 months spanning multiple tax years and during this period the charging basis for company car BIK may change because of increasing CCT rates.

In order to establish the way in which the BIK value should be calculated it is necessary to calculate and compare the following:

1. The amount of salary forgone; and
2. The Modified Cash Equivalent (MCE) of the company car benefit.

If the:

- Amount of salary forgone is greater than the MCE then the company car BIK calculation will be based on the value of the salary forgone.
- Amount of salary forgone is less than the MCE then the company car BIK calculation will be based on company car benefit rules.

The amount of salary forgone

In a cash or car type scheme the amount of salary forgone will typically be the value of the cash allowance given up by the employee when they opt for a company car. In a salary sacrifice scheme the value of the salary sacrifice will be the amount of salary forgone. It is important to note that any trade up payments should be ignored when calculating the amount of salary forgone.

The Modified Cash Equivalent

The method of calculating the MCE is set out in the OpRA legislation and it broadly follows the previous rules for calculating company car BIK. However, it is important to note, the MCE ignores the effect of any private use or capital contributions made. As a result, the MCE value can be higher and in turn this increases the likelihood that the car BIK, rather than the cash value forgone, is used as charging basis for the BIK calculation. It is important to note that the MCE is only used to establish how the company car BIK is calculated and it will not be used in the actual calculation of the company car BIK.

Step 2b: Calculating CCT based on the company car BIK value

Broadly speaking, if it is established that CCT is based on the company car BIK, then this calculated based on the value of the car in question, multiplied by a percentage that is determined by its CO_2 emissions, fuel type and electric range. This calculation gives the value of the BIK provided to the employee, and they will pay CTT tax on this value at their marginal tax rate.

The following table provides further detail in the steps involved with calculating CCT based on the company car BIK value:

Step 1: **Find the price of the car**	The first step is to find the price of the car and for most cars this is the published 'list price' (also called 'taxable list price' or 'P11D value'). The list price is the inclusive price published by the manufacturer, importer or distributor of the car if sold in a retail sale in the open market in the UK on the day before the date of the car's first registration. It includes: • Standard accessories • Any relevant taxes (VAT, car tax (where appropriate), any customs or excise duty and any tax chargeable as if it were a customs duty) • and delivery charges (but excluding the new car registration fee because it's an administration fee, not a tax) It is important to note that for the purposes of the BIK calculation, the actual price paid (that could include discounts or cashbacks) is not relevant.
Step 2: **Add the price of accessories**	The cost of any qualifying accessories is then added to the list price for the calculation of the BIK value to give an interim value. A qualifying accessory is typically an accessory which is: A. made available for use with the car without any transfer of the property in the accessory; b) made available by reason of the employee's employment; and c) attached to the car (whether permanently or not). Accessories can include any type of equipment added to the car, although some are excluded from the BIK calculation. For example, the cost of accessories necessarily provided for the performance of the duties of employment, a mobile phone or equipment to enable a disabled person to use the car are ignored.
Step 3: **Make any deductions for capital contributions made by the employee**	If an employee makes a capital contribution towards the cost of the car (or a qualifying accessory) this contribution reduces the value of the interim sum calculated in step 2. The total amount that can be deducted for a capital contribution is the lesser of: • the total of the capital sums contributed by the employee in that, and any earlier tax years; or • £5,000. It is important to note, the reduction for a capital contribution applies for the tax year in which it is made, and all subsequent years in which the same employee retains the company car. Therefore, if a company car is transferred from one employee to another, the capital contributions made by the first employee are not taken into account when calculating the company car BIK value for the second employee.
Step 4: **Find the appropriate percentage for the car**	The appropriate percentage is a multiplier that is applied to interim sum calculated at step 3 in order to calculate the company car BIK value. The values are published by HMRC and can depend on the CO_2 emissions, fuel type and electric range of the car in question. The rates can also vary between tax years and so may change over the lifetime of the company car. Please see Appendix 1 for tables containing the published appropriate percentages.

Step 5: **Calculating the company car BIK value for the full year**	Once steps 1 to 4 have been completed it is then necessary to calculate the cash equivalent value for the BIK. This is done by multiplying the interim amount, as calculated in steps 1 to 3, by the appropriate percentage identified in Step 4 to give the cash equivalent value of the company car benefit provided.
Step 6: **Reductions for private use**	If an employee makes a payment towards the car for the private use of the vehicle, then this is taken into account for the calculation of CCT (often referred to as 'Private use contributions' or 'PUCs'). In order for the payment to qualify as a deduction the following factors need to apply: • There must be a requirement in the tax year to make payments as a condition of the car being available for private use; • The payment for private use must be paid within the relevant tax year before a deduction can be made; and • The payment must be specifically for private use, it cannot be a payment towards the supply of services, fuel or insurance. A deduction from the cash equivalent value calculated in Step 5 is allowed in respect of payments for private use.
Step 7: **Calculate the income tax due on the company car BIK**	Following steps 1 through to 6 will calculate the cash equivalent of the company car BIK provided. An employee will then pay CCT on this value at their marginal tax rate and this will give the net cost to the employee of the income tax they will pay on their BIK. For example, if steps 1 to 6 generate a cash equivalent value of £8,000, and the employee has a marginal tax rate of 40%, the employee will pay £3,200 in CCT throughout the full tax year.

Please note, the full calculation for company car tax includes additional detail steps, such as reductions for when the car is unavailable or when a car is shared, and historic rules that can apply for older cars. Therefore, it is important that companies and their employees consider the full range of factors affecting the calculation of company car tax when designing and administering company car arrangements, as well as selecting vehicles.

Let's look at some examples

To help illustrate how this might look in practice we have set out five examples, each of which include company cars with different CO_2 emissions and fuel types to show the potential employer and employee tax implications. For the purposes of consistency we have used a listing price of £30,000 and all cars are registered on, or after, 6 April 2020.

Example 1: A pure electric company car with CO_2 emissions of 0g/km

	2020/21	2021/22	2022/23	2023/24	Overall
Appropriate %	0%	1%	2%	2%	1.3%
BIK value	£0	£300	£600	£600	-
CCT at 40%	**£0**	**£120**	**£240**	**£240**	**£600**

The average appropriate percentage over the lifetime of the company car would be 1.3% and the employee would pay a total of £600 in CCT.

Example 2: A Plug-In Hybrid Electric Vehicle (PHEV) with CO_2 emissions of 49g/km and an electric range of 41 miles

	2020/21	2021/22	2022/23	2023/24	Overall
Appropriate %	8%	8%	8%	8%	8%
BIK value	£2,400	£2,400	£2,400	£2,400	-
CCT at 40%	**£960**	**£960**	**£960**	**£960**	**£3,840**

The average appropriate percentage over the lifetime of the company car would be 8% and the employee would pay a total of £3,840 in CCT.

Example 3: A diesel engine company car with CO_2 emissions of 115g/km (non-RDE2)

	2020/21	2021/22	2022/23	2023/23	4Overall
Appropriate %	30%	31%	32%	32%	31.3%
BIK value	£9,000	£9,300	£9,600	£9,600	-
CCT at 40%	**£3,600**	**£3,720**	**£3,840**	**£3,840**	**£15,000**

The average appropriate percentage over the lifetime of the company car would be just under 32% and the employee would pay a total of £15,000 in CCT.

Example 4: A diesel engine company car with CO_2 emissions of 115g/km) (RDE 2 compliant)

	2020/21	2021/22	2022/23	2023/24	Overall
Appropriate %	26%	27%	28%	28%	27.3%
BIK value	£7,800	£8,100	£8,400	£8,400	-
CCT at 40%	**£3,120**	**£3,240**	**£3,360**	**£3,360**	**£13,080**

The average appropriate percentage over the lifetime of the company car would be just under 28% and the employee would pay a total of £13,080 in CCT.

Example 5: A petrol engine company car with CO_2 emissions of 130g/km

	2020/21	2021/22	2022/23	2023/24	Overall
Appropriate %	29%	30%	31%	31%	30.3%
BIK value	£8,700	£9,000	£9,300	£9,300	-
CCT at 40%	**£3,480**	**£3,600**	**£3,720**	**£3,720**	**£14,520**

The average appropriate percentage over the lifetime of the company car would be just over 30% and the employee would pay a total of £14,520 in CCT.

Observation:

The examples shown illustrate the extent to which vehicle selection can affect the cost of company car tax for employees, and in turn the cost of national insurance for a company. Despite the list price of the car in all five examples being the same, the cost of company tax due varies by up to £14,400 (net) over 4 years, which equates to c.£300 per month.

The zero emission company car offers the lowest BIK value out of all five example, with potential CCT savings of 84% when compared to the PHEV, or 95% when compared to the lowest cost combustion engine vehicle.

The comparison between example 3 and 4 shows the impact of opting for an RDE2 compliant diesel company car where the diesel surcharge does not apply. Selecting an RDE2 compliant diesel could reduce tax costs by 15% (£1,920 over 4 years). Currently, there are a limited number of vehicles available that can be provided with an RDE2 compliant diesel engine. However, as more vehicles become available these may be an attractive option for some company car drivers.

It is important to remember that company costs of providing company cars are linked to the value of the BIK for cars selected by employees. Therefore, it is important for companies and their employees to consider current and future company car tax rules when making choices about company cars.

Step 3: Calculating CCT based on the salary forgone BIK value

If it is established that the CCT is based on the value of the salary forgone, then it is necessary to calculate the correct value of the salary forgone and this will depend on the type of arrangement in question.

If it is a cash or car type arrangement, the value of the salary forgone will include:

- The value of the cash allowance offered.
- Any PUCs or capital contributions made by the employee.
- Any trade down payments received by the employee.

The OpRA legislation sets out how the PUCs and capital contributions should be treated when calculating the amount of the salary forgone for the BIK calculation. This broadly follows the way in which these payments were treated under current company car benefit rules.

In the case of a salary sacrifice arrangement, the value of the salary forgone should simply be the gross salary sacrifice amount agreed to by the employee. This is on the basis that trade up or trade down payments are not usually made in salary sacrifice schemes as these are simply treated as a larger or smaller sacrifice amount.

How do employee contribution and trade down payments impact company car BIK?

It is relatively common place in car scheme arrangements for companies to structure arrangements so that they offer employees some flexibility to choose a benefits offering that suits them. An example of this is where an employee is allowed to "trade up" by paying more money in exchange for a better car, or "trade down" and receive additional salary in exchange for taking a lower value car. In some circumstances, the tax system has mechanisms in place that take account of this and deliver adjusted income tax and NICs costs.

Trade up payments

Where an employee makes trade up payments and contributes towards the cost of providing a company car these can be structured as PUCs or capital contributions.

PUCs
If an employee makes contributions as a condition of the car being available for private use, the total amount of the contributions can be deducted from the BIK for the tax year in which they were made. Typically, the payments for private use would be made throughout the time where the car is available. As a result of a tax case, the Government introduced new legislation to ensure individuals make payments for private use of a company car in the relevant tax year. It is important that the car scheme policy documentation is clear that such contributions are for the private use of the car.

Capital contributions
If an employee contributes towards the capital cost of the car, whether that is towards the cost of the car or towards the cost of optional extras, the total contribution is deducted from the P11D value up to a maximum of £5,000. Typically, the payment of capital contribution would be made at or about the time when the car or accessory was provided.

Trade down payments

Where an employee opts to receive a car below their entitlement they may receive an additional payment in return. The correct treatment of trade down payments is quite simple as the payment is usually processed through payroll and will be subject to income tax and NICs.

However, the issue of dealing with trade down payments was not specifically covered in the new OpRA legislation and so there is an element of uncertainty as to how they affect the step to establish the charging basis for company car BIK. The most likely outcome is that where a comparison is made between the taxable value of the car selected, and the cash allowance given up, this reflects the value the trade down payment made. For example:

- An employee is entitled to receive company car or a car allowance of £6,000;
- They opt for a car below their entitlement and receive a trade down payment of £1,000;
- The comparison is made between the taxable value of the company car selected and a car allowance of £5,000 (the original £6,000 car allowance, less the £1,000 trade down payment); and
- The trade down payment (of (£1,000) will be subject to income tax and NI through payroll in the normal way.

Let's look at some examples

To help illustrate how trade up and trade down payments work in practice we have some examples showing how these payments affect company car BIK calculations.

Example 1:
PUC made against a car benefit calculated based on list price and CO_2 emissions

In this example:

- An employee has a company car with a taxable benefit value of £4,800.
- The employee makes PUCs of £600 in a tax year.
- The company car taxable benefit value is reduced to £4,200 (£4,800 - £600).
- The £600 PUCs would result in income tax costs in a year being reduced by:
  - £240 for a higher rate tax payer (£600 x 40%); or
  - £120 for a basic rate tax payer (£600 x 20%).

Example 2:
PUC made against a car benefit calculated based on the value of the salary forgone

Repeating example 1, but for an employee in a cash or car type scheme entitled to a £5,500 cash allowance the result would be:

- An employee has a company car with a taxable benefit value of £4,800.
- The employee makes PUCs of £600 in a tax year.
- The PUC will be ignored for the purpose of establishing whether the benefit will be based on the company car or the salary forgone.
- Therefore, the initial benefit value before taking account of PUCs will be £5,500.
- The benefit value is reduced by the value of the PUCs to £4,900 (£5,500 - £600).
- The £600 PUCs would result in income tax costs in a year being reduced by:
  - £240 for a higher rate tax payer (£600 x 40%); or
  - £120 for a basic rate tax payer (£600 x 20%).

Example 3:
A capital contribution made against a car benefit calculated based on list price and CO_2 emissions

In this example:

- An employee with a company car that has a taxable list price of £25,000.
- The employee makes a capital contribution of £2,000 when the car is delivered.
- The value of the capital contribution is deducted from the taxable list price of the car when calculating the taxable benefit (£25,000 - £2,000).
- The reduced list price for tax purposes will be £23,000 and this will apply for every tax year the car is retained by the employee.
- Based on the fuel type and CO_2 emissions the appropriate percentage for company car tax in 2017/18 is 24%.
- The taxable benefit for the company car is £5,520 (£23,000 x 24%).
- The £2,000 capital contribution would result in income tax costs in a year being reduced by:
  - £192 for a higher rate tax payer; or
  - £96 for a basic rate tax payer.

Example 4:
PUC made against a car benefit calculated based on the value of the salary forgone

Repeating example 4, but for an employee in a cash or car type scheme entitled to a £6,500 cash allowance the result would be:

- An employee with a company car that has a taxable list price of £25,000.
- The employee is also entitled to a cash allowance of £6,500
- The employee makes a capital contribution of £2,000 when the car is delivered.
- The capital contribution will be ignored for the purpose of establishing whether the benefit will be based on the company car or the salary forgone.
- The taxable benefit of the salary forgone (£6,500) is greater than the value of company car (£6,000) and so the tax charge will be based on the value of the salary forgone.
- The value of the capital contribution is adjusted to work with the value of the salary forgone which is done by multiplying it by the appropriate percentage for the company car (24% x £2,000 = £480).
- The taxable benefit of the salary forgone is reduced by the value of the adjusted capital contribution and is £6,020 (£6,500 - £480).
- The £2,000 capital contribution would result in income tax costs in a year being reduced by:
  - £192 for a higher rate tax payer; or
  - £96 for a basic rate tax payer.

What other considerations are there for the company car benefit?

When examining the issue of company car benefit charges there are further considerations worth bearing in mind. These include:

Q. What is the impact of an employee adding optional extras to their company car?

A. If an employee chooses to add optional extras to the car before registration, the P11D value of the car is increased by the list price of the optional extras. It is important to note that even if the manufacturer describes an optional extra as 'free' (for example a free metallic paint or satellite navigation system), the P11D value should still be increased by the list price of the accessory.

If an employee adds optional extras to the car after the car has been registered and the total cost of the optional extras is more than £100, then the cost will be added to the P11D value. This will occur from the beginning of the tax year in which the optional extras were added and the cost of the optional extras will also be taken into account when calculating the MCE under OpRA legislation. If the total cost of the optional extras does not exceed £100 then the total cost will be ignored.

Q. How will an employee know how much CCT they are paying?

A. The BIK amount, calculated as explained earlier, is usually reported on an employee's annual Form P11D. This form reports taxable benefits received by an employee during the tax year.

Q. How is the employee's CCT collected?

A. Typically, the CCT is collected via an adjustment to the employee's PAYE notice of coding. The impact of this is that the employee effectively funds the CCT that is payable to HMRC out of their monthly pay.

Q. Does the diesel surcharge apply to diesel-electric hybrids?

A. HMRC have previously confirmed that diesel-electric hybrid cars would not be subject to the diesel surcharge for CCT. The diesel surcharge has been extended for non RDE2 diesel company cars until April 2021.

Q. What if the company car is off the road for some reason?

A. If a company car is unavailable to the employee for a continuous period of 30 days or more, the benefit charge is reduced by the proportion of the year for which the car is unavailable. This only applies to the car not being available to the employee. It is not sufficient for the employee to be physically unable to drive the car.

If a company car is unavailable for less than 30 consecutive days and a replacement car is made available, no BIK arises on the replacement car provided that it is of similar quality to the car that it is replacing. However a BIK charge will continue to apply based on the original company car throughout the period.

Case study: **Understanding the implications of the new company car tax rules**

Introduction

In July, HMRC published proposed legislation for new company car tax rules that are intended to manage the transition to using WLTP based CO_2 figures for calculating company car tax (from 6 April 2020). The announcements included new lower rates for electric vehicles, a freeze on company car tax rates for existing car and a temporary reduction in the rate of company car tax for cars registered from 6 April 2020 onward.

This case study is designed to explore the potential implications of the new company car tax rules and the move to WLTP emissions figures on the amount of company car tax paid by employees.

Analysis & assumptions

In this case study we have calculated the cost of company car tax for a selection of six company cars that are representative of different segments of a company car fleet. These are:

- A small hatchback car with a list price of £20,000, a petrol engine and CO_2 emissions of 105g/km.
- A medium hatchback car with a list price of £25,000, a diesel engine and CO_2 emissions of 115g/km.
- A saloon car with a list price of £25,000, a diesel engine and CO_2 emissions of 125g/km.
- An SUV with a list price of £35,000, a diesel engine and CO_2 emissions of 140g/km.
- A plug-in hybrid electric vehicle with a list price of £45,000, a petrol/electric hybrid engine, CO_2 emissions of 35g/km and an electric range of 30-39 miles.
- A zero emission electric vehicle with a list price of £60,000 and CO_2 emissions of 0g/km.

The cost of company car tax was then forecast for the following two scenarios:

- Cars acquired before 6 April 2020 with pre-WLTP CO_2 emissions figures (as shown above).
- Cars acquired on 6 April 2020, with post WLTP CO_2 emissions figures that are assumed to be the same as the values above, or to have increased by 10% and 20%.

The forecasts assume a higher rate tax payer keeping the company car for a three year period starting 6 April 2020, and are based on the proposed new rules published by Government in July 2019.

Results

The following table (see next page) shows the cost of company car tax that would be due for the selected cars based on the rules applicable for cars first registered before 6 April 2020 (shown as 'Pre-WLTP'). The table also shows the difference in the forecast Company Car Tax (CCT) cost for the same cars if they were first registered on 6 April 2020 with updated CO_2 emissions figures (shown as 'Post-WLTP')

Selected cars	Pre-WLTP	Post WLTP					
	CCT cost (3 years)	0% inc. in CO_2 emissions		10% inc. in CO_2 emissions		20% inc. in CO_2 emissions	
		Diff' (£s)	Diff'(%)	Diff'(£s)	Diff' (%)	Diff'(£s)	Diff'(%)
Small hatchback	£6,240	(£240)	-3.8%	£240	3.8%	£720	11.5%
Med. hatchback	£9,600	(£300)	-3.1%	£300	3.1%	£900	9.4%
Saloon	£12,240	(£360)	-2.9%	£360	2.9%	£1,080	8.8%
SUV	£15,540	(£420)	-2.7%	£0	0.0%	£0	0.0%
PHEV	£6,480	(£540)	-8.3%	(£540)	-8.3%	(£540)	-8.3%
EV	£720	No change in CO_2 emissions or CCT costs					

The results show that the potential implications for future company car tax costs can vary depending on the choice of car. In summary:

- For the EV, the results show that the cost of company car tax remains the same for both pre and post WLTP scenarios. This is because the proposed rules for a car with CO_2 emissions of 0g/km are set to apply from April 2020 regardless of when the car is first registered. As the CO_2 emissions of a fully electric car will remain the same after moving to WLTP emissions testing, the company car tax cost will be unchanged (although the move to WLTP emissions testing may affect the published range for the EV). It is worth noting that the EV offers a significantly lower company car tax cost when compared to all of the other cars examined, especially when considering it has the highest list price for tax purposes.
- For the PHEV, the results show the cost of company car tax is set to fall for both pre and post WLTP scenarios. This is because the proposed company car tax rates that would apply for the car in question are lower than the current rate of 16%. Due to the way in which the company car tax rates are structured, with a broad CO_2 banding of 1-50g/km, the 10% and 20% increases in CO_2 would not push the car above the upper threshold, and so there is no difference in the company car tax cost in these scenarios. It is important to note that from 6 April 2020, the calculation of company car tax for a PHEV will also take account of the electric range of the car. If the electric range figure falls as a result of moving to WLTP emissions testing, then this could result in the company car rates increasing, although they would still be below the 2019/20 rates.
- For the remaining ICE cars (exc. the SUV), the forecast change in company car tax costs depends on the extent to which their published CO_2 figures are affected by the move to WLTP emissions testing. If there is little or no change in the published CO_2 figures following the move to WLTP, then company car tax costs were forecast to remain broadly the same (with a change in region of +/-£10 per month). However, if CO_2 emissions increase by 20%, the cost of company car tax could rise by £20-£30 per month, even after taking account of the temporary reduction in company car tax rates announced by the Government.
- For the SUV, the pattern of results shown differs to the other ICE cars examined with little or no change shown. This is because the SUV attracts the highest rate of company car tax (37%) and so the move to WLTP is likely to result in a minimal change to the cost of company car tax because the employee is already paying the maximum level of tax (based on pre-WLTP emissions figures).

Observation:

The results highlight the complexity for companies and employees when it comes to understanding the tax implications of choosing company cars. Based on current rules, the cost of company car tax is based on the car list price, CO_2 emissions and fuel type. However, under the proposed rules, company car tax will also take account of electric range and when a car is registered to determine the impact of moving to WLTP emissions testing.

In general, opting for an EV or PHEV is likely to offer the lowest cost of company car tax under the proposed rules, even taking into account the higher list prices for these cars. This would be the case regardless of when the vehicle is first registered.

For ICE vehicles, future tax costs will depend on the impact of moving to WLTP emissions testing. If post WLTP emissions are broadly the same (0%-10% increase), then the temporary reduction in company car tax rates will mitigate this to some extent, with some relatively small in future tax costs. However, if the move to WLTP emissions teasing has a more pronounced impact on CO_2 emissions, this would result in more a more noticeable increase in the future cost of company car tax, even after taking account of the temporary reduction in company car tax rates.

Fuel

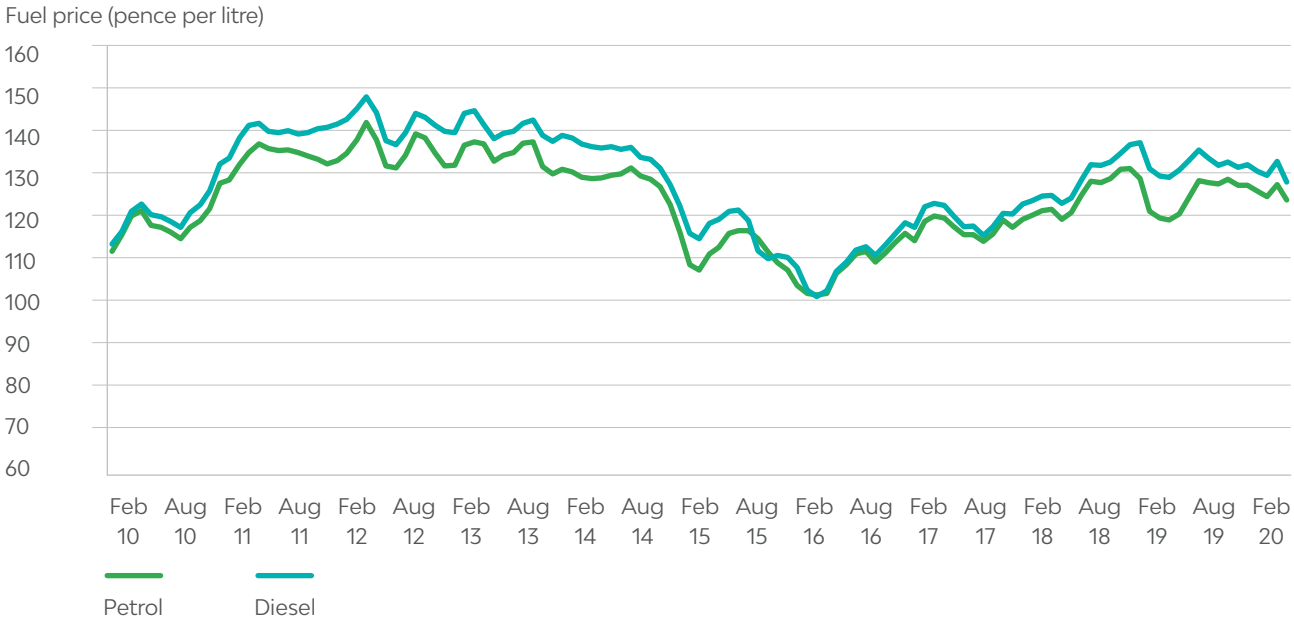
Business mileage results in fuel costs which need to be accounted for. Employers need to take care to ensure they understand the costs and benefits of different methods of fuel reimbursement.

Is the cost of business fuel important?

When employees undertake business mileage on behalf of their company (for example visiting customers) they will generally be entitled to receive reimbursement from the company linked to the cost of the fuel they have used. The issue of business mileage reimbursement has become increasingly important in recent years due to the increased volatility of fuel prices and their impact on businesses.

In the last 10 years, the price of both petrol and diesel has changed significantly as demonstrated by the chart below. With the price at the pump varying by as much as 40% for petrol and 46% for diesel, changing fuel prices can have a noticeable impact in the cost of motoring for both companies and their employees. Since early 2016, there has been a gradual increase in the price of fuel, although currently prices still remain c.13% below their peak (in 2012).

UK fuel prices 2010 - 2020



There have been challenges for companies stemming from the rules that govern the level of reimbursement they can pay without incurring a tax liability. This is because reimbursement rates were not always able to keep pace with the rate at which fuel prices were changing. As a result, some employees felt that the reimbursement they received did not actually cover the cost of the fuel they used for business mileage. This became such an issue that changes were made by HMRC to better deal with the reality of rapidly fluctuating fuel prices.

How can a company reimburse employees for the cost of fuel used?

If an employee uses their own funds to pay for fuel used on business journeys there are two principal methods for calculating the amount of reimbursement the employee receives. The method chosen can have an impact on costs, cash flow and the level of administration required for both the company and its employees.

Advisory Fuel Rates

Many companies use HMRC's Advisory Fuel Rates (AFRs) to reimburse employees for the cost of fuel used for business mileage as it can be simple to implement and administer. With AFRs, the employee reclaims the cost of business fuel based on an allowed rate as published by HMRC. The rates are updated every quarter and they are intended to reflect actual average fuel costs at the time. The rates apply where employers reimburse employees for business travel in their company cars, or require employees to repay the cost of fuel used for private travel. If the reimbursement rate paid per mile of business travel is no higher than the AFRs, HMRC will accept that there is no profit for the employee on the payment and therefore no additional income tax or National Insurance (NI) liability on top of the reimbursement paid

The table below show the current AFRs published by HMRC:

Advisory Fuel Rates (applicable from 1 March 2020)

Engine size (cc)	Petrol	LPG
1,400cc or less	12p	8p
1,401cc or 2,000cc	14p	10p
Over 2,000cc	20p	14p
Engine size	Diesel	
1,600cc or less	9p	
1,601cc or 2,000cc	11p	
Over 2,000cc	13p	

AFRs are published by HMRC every 3 months so as to ensure that the rates remain up to date with the fluctuation of fuel prices, thus ensuring that employees are adequately reimbursed for business fuel used. Historically, AFRs were not published for fully electric and hybrid vehicles. HMRC have since revised this position. Where an employee utilises a hybrid vehicles, the AFRs as illustrated above, will be applicable.

Advisory Electric Rates

HMRC also publish an Advisory Electric Rate (AER) that applies where employees utilise a fully electric vehicle. The AER took effect from 1 September 2018, and allows employers to pay up to 4p per mile for business miles undertaken in an electric only company car without challenge from HMRC that income tax or NI is due.

> The introduction of the advisory electric rates for vehicles was welcomed as it removed the historic burden of companies having to evaluate electricity costs on a vehicle by vehicle basis. The change helped companies who are moving towards a greener fleet, as it makes easier to administer the fully electric vehicles on their fleet.

Actual cost of fuel

An alternative method of reimbursing employees who undertake business journeys in a company car is to reimburse for the actual cost of fuel based on the miles driven and the fuel consumption of the car. If a company can demonstrate that the reimbursement reflects the cost of fuel used and does not provide any profit to employees then the reimbursement may be higher than the advisory rates without triggering a tax liability. The level of administration involved with this approach is greater than simply paying a set rate per mile for each mile driven, as more information is required and the onus is on the company to demonstrate to HMRC there is no profit to the employee within the reimbursement paid.

What happens if employees have a fuel card to pay for fuel they use?

Another mechanism used by companies to reimburse business mileage is the use of a fuel card. In this situation fuel is paid for by means of a fuel card where the employee charges the cost of any fuel purchased to the card and the bill for the fuel is then paid by the company. The employee will then have to submit records to allow the company to distinguish between the fuel used for business purposes and that used for private mileage. To avoid a tax liability for the private fuel used the employee must reimburse their employer the full cost of this fuel.

There are a number of reasons for using fuel cards, such as the bulk buying power providing a discount on the fuel purchased and the ability to reimburse the actual cost of fuel. However, there is a certain level of administration that is necessary to demonstrate that no private fuel has been paid for by the company. If this cannot be demonstrated then a car fuel benefit charge is likely to apply and this can have significant cost implications for both the company and the employee.

What happens if a company provides private fuel?

Typically, if a company provides private fuel (called car fuel benefit) the fuel is paid for by means of a fuel card, but unlike before there is no requirement for the employee to keep any business mileage records, or to reimburse the private element of fuel used. The cost to the company of providing private fuel in this way will include the cost of fuel purchased, VAT implications and an employer's NIC liability in respect of the car fuel benefit provided to the employee.

From the employee's perspective this might seem to be an attractive benefit as they do not have to pay for their private fuel or keep any mileage records, while their total fuel bill is paid by the company. Where employees are provided with a company car, tax on the car fuel benefit is calculated based on a number of factors including the CO_2 emissions of the car, the type of fuel used and a car fuel benefit charge multiplier set by the Government. It is important for employees to be aware that the calculation of the BIK is a fixed charge that does not take account of the value of any private fuel actually used. In many scenarios the employee may be paying more in income tax to receive the car fuel benefit than the value of the private fuel they use.

Let's look at some examples

To help illustrate the implications of providing car fuel benefit, we have two examples for the 2019/20 tax year showing the cost to the company and the tax implications for the employee where car fuel benefit is provided. Please note, the examples exclude the impact of any fuel purchased for business use.

Example 1: A higher rate employee travelling 10,000 private miles each year

The employee receives private fuel and drives a typical 4 door diesel engine company car with CO_2 emissions of 125g/km and published fuel consumption of 65MPG (adjusted downwards by 15% for real world driving conditions). The assumed cost of fuel for this example is £1.28 p/l.

The results are as follows:

Company perspective

The cost to the company of providing private fuel benefit is:	
Cost of private fuel purchased	£1,053
VAT recovery on fuel	(£176)
VAT fuel scale charge	£148
Employer's NI on fuel benefit	£1,116
Total cost (2020/21 tax year)	£2,141

Employee perspective

The tax cost for the employee as a result of receiving private fuel benefit is:	
Private fuel scale charge	£24,500
Appropriate percentage	33%
Taxable benefit	£8,085
Tax paid at 40% (2020/21 tax year)	£3,234

Observation:

The employee would have paid £3,234 in income tax to receive a car fuel benefit where the value of the fuel provided by the employer would have been £1,053. Therefore, the employee would have saved £2,181 (net) if they had personally purchased the private fuel. The cost to the company of providing the car fuel benefit, which would have left the employee £2,181 out of pocket, would have been £2,141.

Example 2: A higher rate employee travelling 30,000 private miles each year

The employee receives private fuel and drives a typical 4 door diesel engine company car with CO_2 emissions of 125g/km and a fuel consumption of 65MPG (adjusted downwards by 15% for real world driving conditions). The assumed cost of fuel for this example is £1.28 p/l.

The results are as follows:

Company perspective

The cost to the company of providing private fuel benefit is:

Cost of private fuel purchased	£3,160
VAT recovery on fuel	(£527)
VAT fuel scale charge	£148
Employer's NI on fuel benefit	£1,116
Total cost (2020/21 tax year)	**£3,896**

Employee perspective

The tax cost for the employee as a result of receiving private fuel benefit is:

Private fuel scale charge	£24,500
Appropriate percentage	33%
Taxable benefit	£8,085
Tax paid at 40% (2020/21 tax year)	**£3,234**

Observation:

The employee would have paid £3,234 in income tax to receive a car fuel benefit where the value of the fuel provided by the employer would have been £3,160. It is therefore evident that even with substantial private mileage, the tax cost of private fuel benefit is likely to be higher than the value of the private fuel purchased. The cost to the company of providing the car fuel benefit, which would have left the employee £74 out of pocket, would have been £3,896.

What other considerations are there for fuel reimbursement?

When examining the issue of reimbursing for fuel there are further considerations worth bearing in mind. These include:

Q. Can a business recover VAT on the cost of business fuel purchased?

A. If a company pays business mileage reimbursement based on a pence-per-mile rate, such as HMRC's Advisory Fuel Rates, then they can reclaim VAT on the mileage rate paid. It should be noted that if the pence-per-mile reimbursement rate paid is above HMRC's AFRs, the VAT reclaim is usually limited to the amount based on the AFR rates.

If a company reimburses the actual cost of business fuel used then the VAT reclaim is based on the cost of the business fuel purchased.

Q. Can a business recover VAT on the cost of private fuel purchased?

A. It would not normally be possible to reclaim any of the VAT for private fuel used. However, HMRC recognise that for many companies, where a car is used for business and private motoring, the record keeping process to keep the two sets of mileage separate would be cumbersome.

HMRC therefore allow the use of what is known as the VAT fuel scale charge. The impact of the VAT fuel scale charge is that it effectively gives rise to a VAT cost to the company. This is because the company (as stated above) is also recovering VAT on the cost of all fuel purchased, which includes fuel for private mileage where VAT cannot usually be recovered. The VAT fuel scale charge is based on the CO_2 emissions of the car. The higher the CO_2 output of the car, the greater the VAT fuel scale charge.

Q. What information do employees need to submit when recording business mileage journeys?

A. Generally, employees will need to submit a fuel VAT receipt and document the business miles travelled. These items should be supplemented by other supporting evidence, such as the date, the reason for the journey or the postcode to postcode information. A company can keep any range of information, if they feel it will enhance the accuracy of their records. Ultimately, the company is required to demonstrate to HMRC, with supporting evidence, the extent of business mileage undertaken by employees.

Q. Can a company reimburse for business mileage below HMRC's Advisory Fuel Rates?

A. Yes. HMRC's Advisory Fuel Rates are not binding and they are intended to reflect average fuel costs. A company may reimburse fuel costs at less than these rates if they feel that this more appropriately reflects the actual fuel costs of their fleet, for example, their fleet may be comprised of fuel efficient cars, therefore requiring less fuel. Clearly, the rationale of any such decision would need to be carefully communicated to employees.

Vehicle Excise Duty

Vehicle Excise Duty ("VED"), which is also referred to as road fund licence or car tax, is a tax that is paid for most vehicles which are used or kept on public roads in the UK.

Is the cost of vehicle excise duty important?

Vehicle Excise Duty ("VED"), which is also referred to as road fund licence or car tax, is a tax that is paid for most vehicles which are used or kept on public roads in the UK. Depending on how a car is provided, the cost of VED may be incurred by a fleet provider and then passed on to its customers in a finance or maintenance charge, or it might be a cost incurred directly by a business. Either way, a business providing cars to its employees should be aware of the rules governing VED.

On 1 April 2017 the Government introduced a system for calculating VED for cars registered on, or after, that date. The transition worked on a grandfathered basis, with the old rules remaining in place for vehicles registered on or before 31 March 2017, and the new rules applying for cars registered after this date.

Under this system, the first year rate remains linked to the CO_2 emissions of the vehicle, but with different thresholds and increased rates. Under the new rules, the standard rate of VED for subsequent years will no longer be linked to CO_2 emissions and will be a flat rate (now £150). In addition, a new rule was introduced for cars with a list price exceeding £40,000 where there is a £310 a year supplement to the standard rate for the first 5 years in which the standard rate is paid. The following table shows current rates and thresholds for cars (these apply for any cars registered on 1 April 2017 or later).

Cars registered on or after 1 April 2017 (rates 2020/21 tax year)

CO_2 emissions (g/km)	First Year Rate (petrol and diesel RDE2)	First Year Rate Diesel (non-RDE2)	Standard Rate
0	£0	£0	£0
1 - 50	£10	£25	£150
51 - 75	£25	£110	
76 - 90	£110	£135	
91 - 100	£135	£155	
101 - 110	£155	£175	
111 - 130	£175	£215	
131 - 150	£215	£540	
151 - 170	£540	£870	
171 - 190	£870	£1,305	
191 - 225	£1,350	£1,850	
226 - 255	£1,850	£2,175	
Over 255	£2,175	£2,175	

Before 1 April 2017, VED rates depended on when the vehicle was registered, its CO_2 emissions and fuel type. The table below shows the VED rates due for cars registered between 1 March 2001 and 31 March 2017.

Registered on or after 1 March 2001 to 31 March 2017

VED Band	CO_2 emissions (g/km)	2020/21 standard rate
A	Up to 100	£0
B	101 - 110	£20
C	111 - 120	£30
D	121 - 130	£125
E	131 - 140	£150
F	141 - 150	£165
G	151 - 165	£205
H	166 - 175	£240
I	176 - 185	£265
J	186 - 200	£305
K	201 - 225	£330
L	226 - 255	£565
M	Over 255	£580

Future VED rules

The Government's review of WLTP and the impact of changing CO_2 emissions on vehicle taxes included VED within its scope. As VED rates feed directly into the cost of a vehicle, any changes to VED would have a direct impact on the overall cost of a vehicle for a company.

The review acknowledged that WLTP could impact the VED liability for individuals, however, based on a study undertaken, increases in WLTP values were shown to have variable impacts on VED liabilities for identical cars selected after April 2020.

In the Government's response to the review, no immediate changes to the rules for VED were announced and it was confirmed that existing VED rates will be maintained following the introduction of WLTP. The review did note that a call for evidence would be due to seek views on a more dynamic approach to VED that would recognise smaller changes in CO_2 emissions.

Vehicle funding

When a company is looking to provide cars to its employees there are a number of different funding options it can consider – within this section we explore all the options.

What options are there for a company providing cars to its employees?

When a company is looking to provide cars to its employees there are a number of different funding options it can consider and the choice of funding route can have a significant impact on the cost as well as wider issues like administration and exposure to residual value risk. It is important for a company to look at all of these when looking to choose a funding option for its company car fleet.

Blended Solutions

It is often the case that a 'blend' of the following funding options can deliver the optimal cost solution for a company. However, operating a blended policy can give additional administrative complexity which often drives companies to choose a single financing method for all the cars in their fleet.

Contract Hire

Contract hire is a lease funding option that is structured so the company simply hires the car for a predetermined period and mileage at a fixed monthly rental. The ownership of the car, and all associated risks, rewards and responsibilities are retained by the leasing provider. The lease rentals are fixed by the leasing provider at the outset of the agreement and usually take into account all costs associated with the car with the exception of maintenance costs, which can be included in an optional maintenance agreement if required.

The company will pay the agreed lease rental charges and maintenance costs if they were included and then at the end of the agreed term the company will hand the car back and settle any end of contract charges due based on the mileage and condition of the car.

There is no option for the company to purchase the vehicle at the end of the lease period and it must be handed back to the lease provider, although some leasing providers may under a discretionary arrangement allow an employee to purchase the car directly from them as a sale to a private individual.

The benefits of contract hire are:

- A fixed cost making budgeting more simple;
- A small initial cost;
- No exposure to residual value rise;
- VAT recovery on the lease rentals (subject to 50% block);
- VAT is payable on each lease rental (as opposed to upfront);
- Corporation tax relief available against the lease rental charges;
- Eliminates most of the stresses and financial risks of vehicle ownership; and
- Reduced car fleet administration.

The potential downsides to contract hire are:

- The company will be tied into a fixed contract;
- No ability to profit directly from residual values (however some fleet providers offer profit share arrangements which can share an element of any profit made on residual values);
- It will be necessary to forecast the expected term and mileage for the car at the outset of the contract; and
- There is no option for the company to purchase the vehicle.

Finance lease

Finance lease is a lease funding option that allows the company to lease a vehicle for a fixed monthly fee. The structure of the arrangement also means that it transfers substantially all the risks and rewards of ownership of the vehicle to the company.

There are two main types of finance lease product that are offered, usually selected depending on the cash flow needs of the company, and these are known as a "fully amortised finance lease", or a "finance lease with a balloon payment".

Finance lease (fully amortised)

The lease rentals are based on the full cost of the car spread over the term of the contract and take no account of any anticipated residual value for the car. At the end of the agreement the car must be sold to a third party and the company will receive an element of the sale proceeds as agreed with the leasing provider at the outset.

It is also possible with a fully amortised finance lease to take up the option of a secondary rental agreement for continued use of the car if this is required by the company. Generally, the capital cost and interest has been covered within the primary period and then a nominal "peppercorn rental" is charged for the secondary period which will be much less than the previous payments.

Finance lease (with balloon)

The lease rentals are based on part of the cost of the car, with a balance (the balloon) being offset towards the end of the agreement, usually to reduce the lease rentals paid. At the end of the agreement the car must be sold to a third party and sale proceeds that are in excess of the balloon payment can be retained by the company. If the sale proceeds fall short of the balloon payment the company will be responsible for any shortfall.

The benefits of acquiring a car under a finance lease are:

- The option to choose a fully amortised or balloon agreement to suit the cash flow needs of the company
- A small initial cost;
- Usually, provided acquisition of title is optional rather than obligatory, VAT should be payable on each lease rental;
- VAT recovery on the lease rentals (subject to 50% block); and
- Corporation tax relief available against the lease rental charges.

The potential downsides to a finance lease are:

- The company will be tied into a fixed contract; and
- Exposure to residual value risk for the company.

Contract purchase

Contract purchase is a deferred purchase funding option that is structured so the company makes fixed monthly payments for a predetermined period and mileage and at the end of the agreement it has the option to purchase the car or hand it back to the leasing provider. The ownership of the car and some of the associated risks, rewards and responsibilities are retained by the leasing provider until the final balloon payment is made.

The monthly payments are fixed by the leasing provider at the outset of the agreement and usually take into account all costs associated with the car and the forecast balloon payment. As with contract hire, it is possible to include an optional maintenance agreement if required.

The company will pay the contracted payments and then at the end of the agreed term the company will have the option of meeting the balloon payment and owning the car or selling it back to the leasing provider at the price agreed at the outset. If the latter option is chosen there may be end of contract charges due based on the mileage and condition of the car.

The benefits of contract purchase are:

- A fixed-cost method of financing a vehicle purchase making budgeting more simple;
- A small initial cost;
- No exposure to residual value risk (if the car is sold back to the leasing provider);
- Potential residual value profit if the residual value is greater than the balloon payment due;
- Tax relief provided via capital allowances;
- Eliminates most of the stresses and financial risks of vehicle ownership; and
- Reduced car fleet administration.

The potential downsides to contract purchase are:

- Upfront VAT cost, as supply of goods, not services;
- VAT is ordinarily fully blocked; and
- It will be necessary to forecast the expected term and mileage for the car at the outset of the contract.

Hire purchase

Hire purchase is a deferred purchase funding option that is structured so the company makes fixed monthly payments for a predetermined period and mileage. At the end of the agreement it has typically paid the full cost of the car and interest and ownership of the car transfers to the company. The ownership of the car is retained by the leasing provider until the final payment is made, however, the associated risks, rewards and responsibilities rest with the company.

The company will typically pay a deposit and then the balance of the cost of the car and any interest charges are spread evenly over an agreed term. As with other funding options, it is possible to include an optional maintenance agreement if required.

The benefits of contract purchase are:

- Greater degree of flexibility within the agreement;
- No end of contract charges; and
- Potential residual value profit (compared to funding option with fixed residual value/balloon).

The potential downsides to hire purchase are:

- Upfront VAT cost, as supply of goods, not services;
- VAT is ordinarily fully blocked;
- Exposure to residual value risk;
- Uncertain costs making budgeting more complex; and
- Management of the vehicles (purchase, disposal and maintenance) can be time consuming.

Outright purchase

An outright purchase describes the straightforward situation where the company directly buys the car. The purchase is usually either funded through borrowings or use of the company's own cash resources. The ownership of the car and all of the associated risks, rewards and responsibilities rest with the company.

An outright purchase involves a large upfront payment when the company purchases the car and when it is sold the company will receive the full amount of the sale proceeds. A company can request fleet management services to support ownership of a car in areas like servicing, roadside assistance and vehicle sale from a fleet provider if required.

The benefits of contract purchase are:

- The flexibility provided by full ownership of the car and no fixed contract; and
- No end of contract charges.

The potential downsides to outright purchase are:

- Upfront VAT cost, as supply of goods, not services;
- VAT is ordinarily fully blocked;
- Exposure to residual value risk;
- Uncertain costs making budgeting more complex;
- Cash flow implication of the large upfront purchase cost; and
- Management of the vehicles (purchase, disposal and maintenance) can be time consuming

How do the funding options compare to each other?

The table provides a simple way of comparing some of the key characteristics of the funding method explained above.

	Contract Hire	Finance Lease (fully amortised)	Finance Lease (with balloon)	Contract Purchase	Hire Purchase	Outright Purchase
What is the upfront payment/deposit?	Typically 3 months advance rentals (c.8% of car cost)	Typically 10%-15% of car cost	Typically 10%-15% of car cost	Typically 3 months advance payments (c.8% of car cost)	Typically 10%-15% of car cost	100% of car cost
Who owns the car?	The leasing provider	The leasing provider until the final payment is made	The leasing provider until the final payment is made	The leasing provider until the final payment is made	The leasing provider until the final payment is made	The company
Typically, who meets maintenance costs?	Leasing provider (assuming optional maintenance agreement is taken)	The company	The company	Leasing provider (assuming optional maintenance agreement is taken)	The company	The company
Who retains the residual value risk?	The leasing provider	The company	The company	The leasing provider	The company	The company
Typically, who is responsible for administration of the car? e.g. Arranging road fund licence and disposal	The leasing provider	The company	The company	The leasing provider	The company	The company
Does the company own the car at the end of the contract?	No, it is returned to the leasing provider	No, it is sold to a third party	No, it is sold to a third party	Yes, subject to making the final payment	Yes, subject to making the final payment	Yes
Is the car treated as on, or off balance sheet?	On balance sheet[1]	On balance sheet	On balance sheet	On balance sheet	On balance sheet	On balance sheet
How does the company claim tax relief for car costs?	Monthly rental can be offset against profits for tax relief	Monthly rental can be offset against profits for tax relief	Monthly rental can be offset against profits for tax relief	Tax relief is provided via capital allowances	Tax relief is provided via capital allowances	Tax relief is provided via capital allowances
Can the company recover VAT on the rentals/payments made?[2]	Yes, subject to a 50% restriction	Yes, subject to a 50% restriction	Yes, subject to a 50% restriction	No	No	No
Can the company recover VAT on an optional maintenance agreement?	Yes, 100% of VAT can be recovered	Yes, 100% of VAT can be recovered	Yes, 100% of VAT can be recovered	Yes, 100% of VAT can be recovered	Yes, 100% of VAT can be recovered	Yes, 100% of VAT can be recovered

[1] The balance sheet treatment of contract hire has changed as a result of reforms to lease accounting. Please see the following lease accounting section for further detail.
[2] Assumes that the car is made available for private use.

How are the different funding options accounted for?

The funding option chosen will ultimately determine the accounting treatment and this can be a significant part of the decision-making process for some companies, particularly for those with large company car fleets. Leasing provides the benefit of having a set monthly cost as well as being more flexible and avoiding working capital becoming tied up compared to an outright purchase. The decision as to whether to opt for contract hire or a finance lease or hire purchase arrangement currently makes a significant difference as to how the arrangement is treated within company accounts.

Contract hire

Under a contract hire agreement, the car (an asset) is leased for a defined period and returned to the leasing provider (the legal owner) at the end of the agreed lease term. The lease agreement will specify the fixed monthly lease rentals to be paid, along with any other additional components, for example, an optional maintenance element. The lessee will not be exposed to residual value risk under contract hire as this rests with the lessor. Whilst contract hire agreements were previously off balance sheet for lessees under IAS17, IFRS 16 requires lessees to recognise a right-of-use asset and a lease liability on their balance sheet.

Finance lease

Under finance lease contracts, the car is treated as if it has been purchased outright and initially capitalised in the balance sheet at cost. It is then subject to an annual depreciation charge based on the estimated useful economic life and estimated residual value.

The lessee recognises an obligation to pay the future rentals in the balance sheet and the rentals payable are allocated between the finance charge and the capital amount (which equates to the fair value of the asset).
The total finance charge is allocated to accounting periods during the primary lease term on a constant yield basis and recorded as an expense in the profit and loss account.

Contract purchase

This has the same accounting treatment as finance lease.

Hire purchase

These typically have the same accounting treatment as finance lease, although it will depend on the option to buy at the end of the contract and whether it is reasonably certain at the outset that the vehicle will be purchased.

Outright purchase

The cost of the car is capitalised in the balance sheet and an annual depreciation charge based on the estimated useful economic life of the car and the estimated residual value is shown in the profit and loss account. The car is recognised in the balance sheet at cost less accumulated depreciation.

Lease accounting (IFRS 16)

Is effective for annual reporting periods beginning on or after 1 January 2019.

How will lease accounting be affected by the new Standard?

Lease accounting update

The International Accounting Standards Board ("IASB") issued IFRS 16 in January 2016. The new Standard replaces IAS 17 and applies to annual reporting periods beginning on or after 1 January 2019.

Lessees have a choice as to whether to apply IFRS 16 with full retrospective effect or alternatively to recognise the cumulative effect of initial adoption as an adjustment to opening equity at the date of initial application.

The timing of any UK GAAP convergence with IFRS has yet to be specified and therefore when these changes will impact those companies not reporting under IFRS, or whether they ever will, is currently unknown.

The following section provides an outline of the accounting implications for companies leasing company cars ("lessees"), other consequences for consideration and why contract hire will continue to play an important role in vehicle leasing.

Overview

IFRS 16 specifies how leases are recognised, measured, presented and disclosed. The Standard provides a single lessee accounting model, resulting in a change to lessee accounting. The distinctions between operating leases (often called Contract Hire) and finance leases are removed with assets and liabilities recognised in respect of all leases (subject to limited exceptions for short term leases and low value assets). It is important to recognise that this change is from an accounting treatment perspective only and that the operational benefits of contract hire remain.

Lessee accounting

Upon lease commencement a lessee is required to recognise a right-of-use asset and a lease liability, with the right-of-use asset initially measured at the amount of the lease liability plus any initial direct costs incurred by the lessee.

The right-of-use asset, which represents the right to control the asset over the lease term is recognised as a non-financial asset in the balance sheet and depreciated over the term of the lease.

The lease liability is initially measured at the present value of the lease payments payable over the lease term, excluding variable payments (unless based on an index or rate), discounted at the rate implicit in the lease (if that rate cannot be reliably determined, the lessee shall use their incremental borrowing rate).

The lease liability is recognised separately and interest recognised in the income statement on a constant yield basis, resulting in a front-loaded expense profile in the same manner as existing finance leases. Any rental payments are split between capital and interest and reduce the outstanding lease liability.

For contracts that contain a lease component and a non-lease component, such as the lease of car and the provision of a maintenance service, lessees shall allocate the consideration payable on the basis of the relative standalone prices, which shall be estimated if observable prices are not readily available. However, as a practical expedient, a lessee may elect, by class of asset, not to separate non-lease components from lease components and instead account for all components as a lease.

Whilst the accounting impact on existing finance lease arrangements for lessees will be minimal, operating lease arrangements such as traditional contract hire agreements, may be impacted as demonstrated in the example overleaf.

Let's look at some examples

A company signs up to a 36 month contract hire agreement with a leasing company for the lease of a company car.

The agreement is for monthly lease rentals of £370 (£4,440 per annum) and a maintenance charge of £30 per month (£360 per annum). The lessee's incremental borrowing rate is 5% and the implicit rate is not readily determinable.

IAS 17 accounting treatment

Under IAS 17 the lessee would have recognised no asset or liability in the balance sheet (on the basis that substantially all of the risks and rewards have not passed to the lessee) and in the income statement a total of £4,800 would be recognised each year as follows:

Year	Lease rentals	Maintenance Cost	Total P&L charge
1	£4,440	£360	£4,800
2	£4,440	£360	£4,800
3	£4,440	£360	£4,800
Total	**£13,320**	**£1,080**	**£14,400**

IFRS 16 accounting treatment

Under IFRS 16 the lessee recognises a right-of-use asset in the balance sheet on commencement of the lease with the associated interest expense recognised as a finance charge and the straight line depreciation expense recognised within administrative expenses.

Year	Lease liability	Interest expense (5%)	Right-of-use asset	Depreciation expense	Maintenance Cost	Total P&L charge
0	£12,416	-	£12,416	-	-	-
1	£8,478	£501	£8,277	£4,139	£360	£5,000
2	£4,342	£305	£4,139	£4,139	£360	£4,803
3	0	£98	0	£4,139	£360	£4,597
Total	-	**£904**	-	**£12,416**	**£1,080**	**£14,400**

The cumulative income statement charge under IAS 17 and IFRS 16 are identical, however, IFRS 16 results in a front-loaded interest expense and a straight line depreciation expense and maintenance cost compared to a straight line total cost under IAS 17. In addition the total cost under IAS 17 was presented within operating profit, while under IFRS 16 the depreciation and maintenance expense is shown within operating profit and the interest expense presented below operating profit within interest payable.

What does this mean for lessees?

- Accounting is potentially more complex for lessees and they will need to monitor and record lease liabilities and right-of-use assets for their fleet vehicles as well as calculating the associated interest, depreciation and maintenance expense separately.
- Changes in the recognition of assets and liabilities has the potential to impact key financial performance indicators, such as earnings before interest, taxes, depreciation and amortisation ("EBITDA"), operating margin and debt to equity ratios. As a result debt covenants may need to be renegotiated if they are not based on a 'frozen' GAAP.
- Regardless of these changes companies will continue to lease vehicles and the loss of the current off balance sheet treatment of operating leases under IAS 17 is unlikely to be a key consideration for many. It is important to note that the cash costs of leasing will remain the same despite the change in accounting and the existing economic benefits of contract hire will remain in that it:
  - is available at a fixed monthly cost;
  - is a flexible and cost effective option of financing vehicle fleets;
  - limits exposure to residual value risk; and
  - provides the option of an integrated fleet management service.

Whilst the new Standard results in changes it is important to remember that investors and analysts may have previously made their own estimates of off balance sheet lease liabilities (certain disclosures around the extent of operating lease commitments is currently required under IAS 17) and therefore the impact on company balance sheets may not be totally unexpected. In fact in some cases it may be that those estimates were somewhat prudent and in fact much larger than the extent of the lease liabilities that will come onto the balance sheet under IFRS 16.

Case study: Adopting Electric Vehicles & WLC

Introduction

From 6 April 2020, the proposed rates of company car tax published by HMRC for Electric Vehicles (EVs) and Plug-in Hybrid Electric Vehicles (PHEVs) should offer a significant discount when compared to those for Internal Combustion Engine (ICE) cars. However, despite the potential company car tax incentives on offer, the business case for these vehicles may not be clear cut because they are typically more expensive for a company to finance than petrol or diesel cars due to the cost of the new technology used. However, with a well-designed WLC policy it may be possible to leverage the tax efficiency of these cars to make them a financially viable proposition.

This case study is designed to explore the potential cost implications of adopting EVs and PHEVs on a company car fleet from both the company and the employee perspectives.

Discover later in the guide the opportunities of adopting electric vehicles under Salary Sacrifice.

Analysis & assumptions

In this case study three representative 'types of car' that are frequently found on many company car fleets were analysed. These were, a hatchback, a saloon and a Sports Utility Vehicle (SUV). For each type of car, the company and employee WLC was calculated for a three year contract term using:

- A petrol and diesel version;
- A PHEV alternative; and
- An EV alternative.

The PHEV and EV alternatives were selected so that they are broadly comparable in terms of the type and size of car, although due to the additional cost of electric vehicle technology, these were more expensive cars.

The analysis carried out was based on cars acquired on 6 April 2020 and operated for a three year contract term with an annual mileage profile of 10,000 business and 10,000 private miles. The policy for business mileage reimbursement was set to be HMRC's advisory fuel rates or advisory electric rate as applicable.

In the 'With employee contribution' scenarios, it was assumed employees would pay a contribution towards the cost of the car so that the company WLC was fixed at the level of the lowest cost ICE car. The employee contribution was calculated on WLC basis and would be taken as a deduction from net pay by the company and would be treated as a private use contribution for income tax purposes.

For example, in the Hatchback analysis, an employee opting for a PHEV would be charged an employee contribution of just over £145 (net) per month if they picked this car. This payment was calculated so that the company WLC of funding the PHEV, when taking account of the employee contribution, would be reduced from £21,658 to £16,879 (the same cost of the petrol engine equivalent).

Results

The tables below shows the WLC for the company based on providing the three types of car analysed with and without an employee trade-up payment taken into consideration. The tables also show the employee's WLC if they opted to receive these cars and pay any applicable trade-up payment due.

Hatchback car				Company WLC		Employee WLC
	List price	CO_2 (g/km)	Electric range	Without employee contribution	With employee contribution	With employee contribution
Diesel engine	£21,390	92	n/a	£17,587	£16,879	£6,849
Petrol engine	£20,310	98	n/a	£16,879		£5,543
PHEV alternative	£31,960	38	31	£21,658		£6,672
EV alternative	£34,440	0	n/a	£17,773		£3,139

The results show:

- The most cost effective hatchback car for the company to provide would be the petrol engine hatchback, with a WLC of £16,879 over 36 months (assuming no employee contribution).
- The PHEV and EV alternatives would cost the business more to fund than the lowest cost ICE version (by 28% and 5% respectively).
- However, if the employee paid a contribution, it may be possible to offer all of the cars modelled at broadly the same WLC to the business (£16,879).
- If an employee contribution was introduced and calculated to leave the company funding a WLC equal to that of the lowest cost ICE car, then the company could offer:
  - a PHEV alternative with an employee cost similar to the diesel engine hatchback; or
  - an EV alternative, that could offer significant employee savings when compared to the lowest cost ICE car, with potential savings of c.£2,400 over 3 years (43%).

Saloon car				Company WLC		Employee WLC
	List price	CO_2 (g/km)	Electric range	Without employee contribution	With employee contribution	With employee contribution
Diesel engine	£26,670	106	n/a	£22,643	£22,643	£9,590
Petrol engine	£26,570	122	n/a	£23,846		£9,281
PHEV alternative	£39,925	37	37	£23,922		£3,567
EV alternative	£51,350	0	n/a	£26,550		£4,501

The results show:

- The most cost effective hatchback car for the company to provide would be the diesel engine version, with a WLC of £22,643 over 36 months (assuming no employee contribution).
- The PHEV and EV alternatives would cost the business more to fund than the lowest cost ICE version (by 6% and 17% respectively).
- However, if the employee paid a contribution, it may be possible to offer all of the cars modelled at broadly the same WLC to the business (£22,643).
- If an employee contribution was introduced and calculated to leave the company funding a WLC equal to that of the lowest cost ICE car, then the company could offer:
  - an PHEV alternative, that could offer significant employee savings when compared to the lowest cost ICE car, with potential savings of c.£5,700 over 3 years (62%); or
  - an EV alternative, that would also offer significant employee savings when compared to the lowest cost ICE car, with potential savings of c.£4,700 over 3 years (52%).
  - It is worth noting that a well as being offering the lowest employee cost, the PHEV and EV alternatives also have a significantly higher list price and therefore may be perceived as more 'valuable' by employees.

SUV				Company WLC		Employee WLC
	List price	CO_2 (g/km)	Electric range	Without employee contribution	With employee contribution	With employee contribution
Diesel engine	£31,590	165	n/a	£26,605	£26,605	£15,310
Petrol engine	£30,440	208	n/a	£27,207		£16,044
PHEV alternative	£52,060	49	31	£35,994		£10,576
EV alternative	£64,440	0	n/a	£30,979		£5,011

The results show:

- The most cost effective hatchback car for the company to provide would be the diesel engine version, with a WLC of £26,605 over 36 months (assuming no contribution).
- The PHEV and EV alternatives would cost the business more to fund than the lowest cost ICE version (by 16% and 35% respectively).
- However, if the employee paid a contribution, it may be possible to offer all of the cars modelled at broadly the same WLC to the business (£26,605).
- If an employee contribution was introduced and calculated to leave the company funding a WLC equal to that of the lowest cost ICE car, then the company could offer:
  - an PHEV alternative, that could offer significant savings when compared to the lowest cost ICE car, with potential savings of c.£4,600 over 3 years (31%); or
  - an EV alternative, that would also offer significant savings when compared to the lowest cost ICE car, with potential savings of c.£10,200 over 3 years (67%).
- It is worth noting that a well as being offering the lowest employee cost, the PHEV and EV alternatives also have a significantly higher list price and therefore may be perceived as more 'valuable' by employees.

Observation:

The results of the case study demonstrate some of the challenges and opportunities facing companies considering the adoption of electric vehicles.

On first glance, the PHEV and EV alternatives do not appear to be a cost effective option with the WLC of these vehicles being greater than the ICE equivalents. As a result, some car scheme policies would prohibit the selection of these vehicles and this could leave employees unable to access the potential savings they can offer.

However, in a car scheme policy with an employee contribution structured on a WLC basis, it is possible for a company to offer the PHEV and EV alternatives so that the cost to the business is broadly the same as the ICE equivalents. In this scenario, the significant employee savings on offer can be leveraged to make the provision of these vehicles cost effective for the company. Even after taking account of the cost of making a personal contribution towards the cost of the car, the PHEV and EV vehicles can still offer significant employee savings.

With the right policy and selection of vehicles, it may even be possible go one step further and offer PHEVs and EVs with employee contributions calculated to generate savings for the business (when compared to the cost of funding ICE equivalents). However, it will be important for to consider the optimum balance of how potential savings are shared between the company and employees, so these vehicles can still offer an effective option.

It is important to note that while the financial argument for adoption electric vehicles can be quite compelling, there are other issues for businesses and employees to consider in respect of adopting electric vehicles. For example, the availability of charging points and the suitability of the vehicles available for different driving behaviours, may be important issues to consider and deal with through an appropriate car scheme policy.

Electric Vehicles

The announcement of the 0% Company Car Tax rate for zero-emission vehicles, as well as lower tax rates for some plug-in hybrid electric vehicles (PHEVs), signals clear support for the Government's 'Road to Zero' objective. When other potential cost savings are also taken into account, employers and employees are likely to have good reason to consider zero-emission vehicles and PHEVs.

We explore some of the considerations in this section

It's fair to say that electric vehicles (EVs) really are becoming a viable alternative to petrol and diesel vehicles (often referred to together as ICE – internal combustion engine). By the end of last year, there were 265,000 plug-in cars and 8,700 plug-in vans on the road, while most mainstream car makers now offer high-quality electric models. As of 2020, there are more than 120 fully or partly electric vehicles available to buy or lease in the UK. The choice of electric vans is more limited than electric cars, yet their number is set to increase in the next few years (source: ZAP-Map). In the most recent set of SMMT figures, plug-in models made up 6.3% of total UK new car registrations.*

This ties in closely with the Government's own priorities; in particular, its Road to Zero initiative. This aims for net-zero greenhouse gas emissions by 2050, with a ban on new diesel and petrol cars from 2040. However, the date could be bought forward, as the Conservative manifesto promised to "consult on the earliest date we can phase out the sale of new conventional petrol and diesel cars, while minimising the impact on drivers and businesses".

At the same time, the manifesto promised £1 billion for rapid chargers, so that no driver will be more than 30 miles from one, an EV battery "Gigafactory" and a £4 billion R&D plan for decarbonisation.

Why fleets matter

More than half of all new cars in the UK are bought by fleets (source: SMMT), so fleet decision makers have a major role to play in the EV revolution. The good news is that there is a lot to like about modern EVs, such as lower running costs, less noise and reduced tailpipe emissions.

They're also popular with drivers – and not just for the 'on the road' experience. Many people want to work for companies that show they're taking sustainability seriously. This is part of a wider trend across the UK, where consumers are making clear they want greener options – and to buy from brands with stronger environmental credentials.

There are tax advantages to choosing EVs, such as the 0% benefit in kind tax in April 2020. There is even a range of grants to help companies get started, such as those for charging and plug-in vans.

Infrastructure is sometimes more of a sticking point; particularly as we're noticing a shift from 'range anxiety' (how far the car can go) to 'charging anxiety' (finding somewhere to charge it). However, charging points are being installed more widely – not least across cities – with the support of both local and national government. According to Zap-Map, there were 10,500 charging locations, 16,900 charging devices and 29,500 connectors in January 2020.

Seeing costs differently

The other big challenge for EV take-up is the way the costs are perceived. Although ICE and electric cars can seem much the same when you look at them from a distance, their cost structures are very different.
This is why a whole life cost (WLC) perspective is absolutely essential. This goes beyond the 'ticket' price (which is typically higher for an EV) and takes into account taxes, subsidies, fuel and electricity use, battery lifetime, repair, maintenance and tyres and length of ownership.
Our Car Cost Index revealed that when the full picture is seen, EVs and ICE vehicles often have roughly similar costs, so purchasing decisions can take the wider benefits into account. The Index also showed that the UK is now the second cheapest country to own an EV in – out of the 22 we surveyed – while our EV Readiness Index places the UK third out of 22 (up from seventh last year).
The benefits of EV are clearer if your business is likely to be operating anywhere that's proposing a Clean Air Zone (CAZ) or within London's ULEZ, particularly as many have financial penalties for driving more polluting vehicles into the zone.

If an ECOS arrangement is correctly implemented and operated in a compliant manner, then it can offer a cost effective alternative to providing company cars. However, implementing and operating an ECOS can be a complex process. It is important for any company considering an ECOS to ensure that it carefully considers the benefits and risks of the arrangement in detail before committing to any changes.

Taking the first step

One way to get started with EVs, which removes some of the challenges surrounding them, is to lease your vehicles. This moves any uncertainty around future residual values over to the leasing provider and gives them the responsibility for maintenance costs. It also allows you to reduce the impact of their main downside (the higher upfront price) by effectively spreading it over several years.

Sources:
* https://www.nextgreencar.com/electric-cars/statistics/
Source for additional statistics: https://www.leaseplan.com/en-gb/fleet-management/electric-driving

Discover more

Listen: Fleet Navigator Electric Vehicles Podcast
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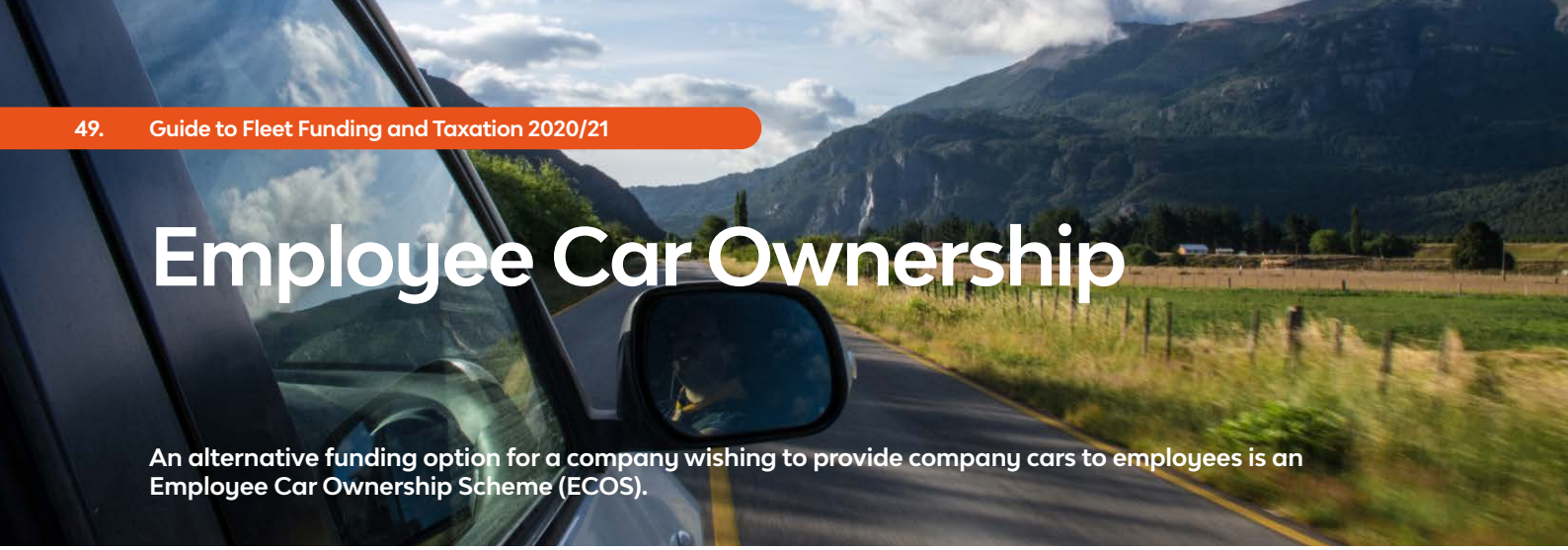
Good to know: GreenFleet Award Winner 2018 and 2019 'Green Leasing Company of the year'



Employee Car Ownership

An alternative funding option for a company wishing to provide company cars to employees is an Employee Car Ownership Scheme (ECOS).

What is an employee car ownership scheme?

Introduction

An alternative funding option for a company wishing to provide company cars to employees is an Employee Car Ownership Scheme (ECOS). Broadly, an ECOS is an arrangement put in place by a company that allows its employees to acquire a car, usually within a specified framework and from a single fleet provider. The arrangement is usually designed to offer similar benefits to a company car from the employee's perspective with the policy often remaining comparable in terms of how issues like car selection, support and servicing and reallocation are dealt with.

It is important to be aware that the term "Employee Car Ownership Scheme" is only one of many used by providers to describe arrangements of this type. There are a range of different car ownership arrangements available and although they broadly offer the same benefit, the arrangements can also differ in terms of some of the detail of implementation and operation.

How did the OpRA legislation affect employee car ownership schemes?

Due to the way it was structured, the introduction of the OpRA legislation impacted most ECOS arrangements in place at the time because they were typically designed to make use of a variable cash top-up. Under the OpRA rules, the AMAP payments made in an ECOS with a variable cash top-up were no longer exempt from income tax. With this loss of the tax efficiency, this type of ECOS ceased to be effective. However, it is worth noting that if an ECOS is structured so that it does not rely on a variable cash top-up, it can fall outside the scope of the OpRA legislation, and offer a viable alternative to providing company cars.

What are the implications of using an employee car ownership scheme?

The most common reason for a company to consider the use of an ECOS is the level of potential saving it could offer when compared to providing cars through a traditional company car scheme. If the correct fleet profile is present, which can broadly be defined as high levels of business mileage and a low cost of car provision, potential employer savings could be significant. However, it is critical to be aware that where an ECOS is operated and the correct fleet profile is not present, it can potentially cost significantly more than a traditional, well designed, company car scheme.

When it comes to the implementation and operation of an ECOS it is likely to be much more complex than a traditional company car scheme for a number of reasons. This may include:

- The fact that an employee will sign a contract to take ownership of the car which can involve complications such as credit checks on employees;
- Whether the employee wants to own the car their company provides;
- The funding within an ECOS tends to be a mix of AMAP and gross salary and it is important to correctly calculate all of the PAYE and NIC due to ensure HMRC compliance; and
- Due to the complexity of ECOS arrangements they can be difficult to explain to employees, so that greater resources are needed for administration.

If an ECOS arrangement is correctly implemented and operated in a compliant manner, then it can offer a cost effective alternative to providing company cars. However, implementing and operating an ECOS can be a complex process. It is important for any company considering an ECOS to ensure that it carefully considers the benefits and risks of the arrangement in detail before committing to any changes.

Cash allowances

Offering cash allowances in lieu of company cars increases employee choice but care is needed to ensure the cash policy does not create added costs and uncertainty for the employer.

What about offering a cash allowance instead of a company car?

Offering a company car was once a relatively straight forward and tax efficient way of providing a benefit to employees. However, the changing tax landscape and a desire by some companies to give employees more flexibility has meant the case for providing company cars, especially cars provided as a perk rather than for a business need, has become less clear-cut. As an alternative, many companies offer employees the choice of a company car or a cash allowance in lieu of the car (often referred to as a 'cash or car' type arrangement).

The popularity of providing cash allowances increased following their inception and based on the general consensus from market surveys, a significant majority of companies now offer a cash allowance in some form or another. However, since the introduction of the OpRA legislation, the complexity and administration involved with operating a cash or car arrangement has increased. As a result, some businesses have decided taken the opportunity to reconsider the choice of car scheme arrangements they offer to employees.

In recent years, there's been an increase in the number of companies offering employees cash allowances to their employees. This is especially true for perk populations, where employees typically pay higher rates of company car tax making the cash alternative an attractive option. In some cases, companies have even moved to a cash only policy for certain populations in order to remove the administrative burden of the OpRA legislation.

To accommodate the increasing demand, a number of new leasing products and services have been introduced for employees opting to receive a cash allowance. For instance, a range of affinity schemes are now available for employees who take a cash allowance in lieu of a company car. The term 'Affinity scheme' can cover a broad range of products, but in general, it is where an company links its employees to a fleet provider and that provider then makes cars available to the employees for use of their cash allowance. As with most car scheme arrangements, it is important to ensure that an affinity scheme is correctly implemented and administered on a HMRC compliant basis. For example, depending on the way the scheme is operated, there could be a potential risk of challenge that the cars provided are deemed a company car (because they are provided without transfer of title and by reason of employment).

Another point to consider, is the introduction of low company car tax rates for low or zero emission company cars. Prior to this, the cost of company car tax may have made cash allowances an attractive option. With the low tax rates now offering a significant financial incentive, the decision on whether to opt for a company car, or cash allowance, has become more complex because of there are more variable to consider. However, as with many arrangements care needs to be taken to make sure they are right for the company and provided in a well-structured way that takes accounts of current and future legislation.

What are the benefits for an employee?

Where employees are provided with the choice of a company car or a cash allowance they have a greater ability to choose a benefits package that suits their needs and lifestyle. With the recent tax cost rise there may be a financial benefit to employees in receipt of a cash allowance. They may opt for the cash allowance to fund a car that is not available on the car scheme, or spend less than their full allowance and receive more income. Also, employees using the allowance to fund a car will own it and are free to make choices about how and what they do with it, such as replacing it more or less frequently than the company car they would have been entitled to.

However, employees must balance this freedom of choice with the costs and risks associated with running their own car, particularly in light of the new rules around emission testing and the change in CO_2 charges. With a company car, normally the company will cover the running costs of the vehicle, such as servicing, road fund licence and insurance. An employee needs to remember that they will be responsible for these costs and factor them into their financial calculations when choosing a car.

What are the implications for a company offering cash allowances instead of a company car?

For some companies providing cash allowances in place of a car may have negative as well as positive consequences. For example, providing a cash allowance should reduce or remove the administrative burden of providing company cars. However, there is a greater risk of the unknown for companies providing cash allowances as they have less control over the cars employees use for business purposes. Also, with the new OpRA legislation the act of offering a cash allowance as an alternative increases the complexity of administering the company car scheme, even if no-one actually opts to receive a cash allowance.

In another scenario, a company could introduce cash allowances as an alternative to company cars to try and reduce benefit provision costs. However, if employees opt out of the car scheme this could reduce volume support and manufacturer discounts received on remaining company cars, pushing those costs higher. This might negate any cost savings from introducing cash allowances. Therefore it is important that a company fully considers all of the issues and makes sure that cash allowances are an appropriate choice.

Whether a company introduces cash allowances, or offers a choice between a company car or a cash allowance, the policy on cash allowances should be set by reference to the whole life cost after tax of the company car. This will ensure that the post-tax cost to the company will remain at the same level regardless of whether the employee selects a company car or cash allowance.

How do you determine the level of a cash allowance?

While it is relatively easy to understand how much cash allowances cost a company, the key question becomes where to set the level of the cash allowance offered to employees. The company should be confident in what it is seeking to achieve at the outset and offer allowances set at a level to deliver this. Will it, for example, be looking to save costs or simply match what is spent on providing company cars? Is the company comfortable that, inevitably, some employees will gain more under cash allowances, while some will lose out?

If cash allowances are offered alongside a company car scheme, with the objective to be cost neutral to the company on a post-tax basis, it is advisable that any company seeking to introduce such a policy should optimise its company car scheme, before it introduces such changes.

These and other equally important issues relating to the design of a cash allowance system need to be addressed, before core questions relating to the cash calculations are addressed, such as:

- Will the cash allowance be calculated to leave the company in a neutral financial position?
- Will the cash allowance be calculated to leave the employee in a neutral financial position?
- Will the same cash allowance be calculated for each grade of employee?
- Where should the cash allowance levels be positioned when compared to those offered by competitors?
- What rate of business mileage reimbursement should be paid to employees receiving a cash allowance?
- If cash allowances are optional, what can be done to stop employees ‘cherry picking’ the best option for them, which is usually the most costly for the company?
- If an employee chooses a cash allowance, what degree of control will the company try and retain over vehicle selection, etc.

So the simple question of what is the correct level of cash allowance can become quite complex. When you consider the scale of the sums involved and the number of employees this can be an expensive benefit to provide and one where mistakes could be costly.

How can a company reimburse employees for the cost of business miles travelled in their own car?

As with company cars, employees undertaking business mileage on behalf of their employer will generally be entitled to receive reimbursement from the company for the cost of the fuel they have used. However, unlike company cars, where only the cost of fuel is reimbursed, there are other costs to consider with private cars. The reimbursement for employees using their own car for business mileage will be set to cover costs like servicing, insurance, depreciation etc. that may be higher as a result of travelling business mileage.

Approved Mileage Allowance Payments

HMRC publish guidance for the rates a company can pay to employees who use their own car for business journeys undertaken. The Approved Mileage Allowance Payments (AMAP) rates set out the maximum amount per mile that may be reimbursed to employees without triggering an income tax or National Insurance charge. The current rates are as follows:

From 2011/12 to present date	First 10,000 business miles in the tax year	Each business mile over 10,000 in the tax year
Cars and vans	45p	25p

Where employees receive no funding to pay for a car i.e. employees without a cash allowance who undertake insignificant levels of business mileage, companies will typically reimburse for business mileage at the full AMAP rates. However, where employees receive a cash allowance, companies often reimburse for business mileage below AMAP rates. Otherwise there is a risk employees will profit on the rate reimbursed and this could encourage unnecessary business mileage.

For example, if an employee is driving a private car with fuel consumption of 50MPG and a fuel price of £1.19/litre (equivalent to £5.41/gallon) each mile travelled would cost approximately only 11p per mile in fuel costs. If the driver were being reimbursed 45p per mile, this would leave 34p per mile to cover the additional cost of servicing, insurance and depreciation resulting from the extra mileage driven. It may be that the additional costs are not 34p and the employee is profiting from the reimbursement they receive for business mileage.

Many companies address this by reimbursing below HMRC's AMAP rates to have greater control over costs while removing the incentive for driving excessive mileage. Using HMRC's Advisory Fuel Rates (AFRs) is a popular alternative as one set of rates is easier to administer and the rate is set at a level designed to cover the cost of fuel used.

What is Mileage Allowance Relief?

If a company reimburses for business mileage below the AMAP rates an employee is entitled to claim tax relief, but not National Insurance relief, on the difference between what they actually received and what they were entitled to based on permitted rates. This is known as the Mileage Allowance Relief (MAR) and depending on the level of business mileage driven, this can equate to a significant amount for an employee.

For example, if an employee drives 6,000 business miles per year they are entitled to AMAPs of 45p per mile which equates to a total approved amount of £2,700. If the reimbursement rate received was actually 14p per mile they would only receive £840, a shortfall of £1,860 compared to what they can claim tax relief on. The employee can therefore claim tax relief at the end of the tax year for this amount and assuming a 40% tax payer, the relief would be worth an additional £744 (£1,860 X 40% = £744).

In order to claim MAR from HMRC the employee will have to provide sufficient proof to demonstrate the number of business miles driven, the amount of reimbursement received and the value of any MAR due. There are a number of ways in which an employee can claim MAR which includes submission of the required information on their self-assessment return, use of a Form P87, or even requesting that HMRC reflect MAR in their personal tax code.

Let's look at some examples

To help illustrate the implications of providing cash allowances to employees, we have detailed below some examples showing the cost to the company and the financial position for the employee where cash allowances are provided.

Example 1: A perk employee

In this example the employee is a higher rate tax payer travelling 5,000 business miles and 5,000 private miles each year. The vehicle provided is a diesel engine car with CO_2 emissions of 113g/km and a list price of c.£36,000. The employee is reimbursed for business mileage at HMRC's AFRs.

The table below shows the annual cost to the company of funding a company car, or a cash allowance that is used to fund the same car via a personal lease (with the cash allowances calculated on an employer and an employee neutral basis).

Perk employee		Company			Employee		
		Annual cost[1]	Diff' £s	Diff' %	Annual cost[1]	Diff' £s	Diff' %
Company car		£7,428	-	-	£5,008	-	-
Cash allowance	Employer neutral	£7,428	£0	0%	£3,395	(£1,614)	(32%)
	Employee neutral	£4,792	(£2,636)	-35%	£5,008	£0	0%

[1] cost shown is the annualised WLC for a 4 year replacement cycle.

The cost to the business of providing the company car, or a company neutral cash allowance, would be £7,428 per annum. In this scenario, the cash allowance was calculated so that the cost to the company would be the same whether they provided the company car or cash allowance.

When looking at the employee position, there would be a saving of just over £1,600 net per annum (-32%) from opting to receive the company neutral cash allowance instead of the company car. This comparison is based on the employee using the cash allowance to fund the same car privately via a personal lease.

However, if the cash allowance was calculated so that it would be cost neutral for the employee (i.e. the employee was no better or worse off when compared to their position in a company car) the cost to the company of funding a cash allowance would fall to £4,792 per annum. This would equate to reduction in costs of £2,636 (-35%) when compared to the cost of funding the company car.

It is important to note that the employee forecasts above assume that the employee also makes a full claim to HMRC for Mileage Allowance Relief (MAR) worth £660 (net) per annum. If the employee fails to make a MAR claim, which many do, this would leave them financially disadvantaged compared to the level of funding they are entitled to when undertaking business mileage in a private car.

Example 2: A business need employee

In this example the employee is a basic rate tax payer travelling 15,000 business miles and 5,000 private miles each year. The vehicle provided is a diesel engine car with CO_2 emissions of 93g/km and a list price of just over £21,000. The employee is reimbursed for business mileage at HMRC's AFRs.

Business need employee		Company			Employee		
		Annual cost[1]	Diff' £s	Diff' %	Annual cost[1]	Diff' £s	Diff' %
Company car		£5,863	-	-	£1,396	-	-
Cash allowance	Employer neutral	£5,863	£0	0%	£1,795	£364	26%
	Employee neutral	£6,370	£507	9%	£1,396	£0	0%

[1] cost shown is the annualised WLC for a 4 year replacement cycle

The cost to the business of providing the company car, or a company neutral cash allowance, would be £5,863 per annum. As above, the cash allowance was calculated so that the cost to the company would be the same whether they provided the company car or cash allowance.

When looking at the employee perspective, the outcome is quite different from example 1, with the employee actually worse off by just over £360 net per annum (26%) if opting to receive the company neutral cash allowance instead of the company car.

If the cash allowance was calculated so that it would be cost neutral for the employee (i.e. the employee was no better or worse off when compared to their position in a company car) the cost to the company would be £6,370 per annum. This would equate to a cost increase of £507 (+9%) when compared to the cost of funding the company car.

As with example 1, the figures above assume that the employee also makes a full claim to HMRC for MAR and in this example it would be worth £863 (net) per annum. As before, if the employee fails to make a MAR claim, this would leave the employee financially disadvantaged compared to the level of funding they are entitled to when undertaking business mileage in a private car.

Observation:

The two examples shown illustrate some of the dynamics of calculating cash allowances as well as the challenge of balancing company and employee costs.

In the case of the perk employee, the high cost of company car tax and low private mileage, means that opting for a cash allowance can be financially beneficial for employees. Also, depending on the level of cash allowance offered, this can also be beneficial for the company as well.

However for the business need example the situation is reversed. The increased cost of a personal lease due to higher mileage levels, as well as a lower company car tax bill, means that the employee would be financially advantaged opting for the company car. A company car would also be cheaper to provide than the employee neutral cash allowance in these circumstances.

Case study: **Understanding the choice of company cars and cash allowances**

Introduction

According to figures from HMRC, since 2009/10, the number of company car drivers remained relatively stable (at just under 1 million drivers). However, provisional figures forecast a noticeable decline for the 2017/18 tax year, with numbers expected to fall from c.940k to 890k, a drop of 5.3%. One of the possible reasons for the expected decline is likely to be the trend for some employees and businesses to move to cash allowances instead of company cars.

Over the past few years, a number of issues have affected the provision of company cars making cash allowances a relatively more attractive option in comparison. Since 2015, the company car tax rates have increased, with tax on for a typical fleet car rising by 33% and adding almost £60 a month to the cost of tax (for a higher rate tax payer). In the same period new legislation was introduced that increased the cost and complexity of administering of some company car scheme arrangements. Also, in the absence of future rates published by the Government, there was uncertainty about the future rules and rates for company car tax, especially for electric vehicles.

However, with the announcement of company car tax rules up to 2023 that includes frozen or reduced rates for most cars, and a significant financial incentive for electric vehicles, the choice of company car or cash allowance is now very different.

This case study is designed to explore the financial implications of companies and employees choosing between company cars and cash allowances.

Analysis & assumptions

In this case study, a selection of perk and job need cars were modelled to illustrate the financial implications of choosing between company cars and cash allowances. The analysis compared:

- Company cars funded using contract hire; and
- Cash allowances used to fund the same car privately via a personal lease.

The cash allowances were set at a company neutral level so that the WLC would be the same regardless of how the car was funded. This leaves the employee position to provide an indication of the financial implications of choosing between a company car and cash allowance.

The analysis was based on all the cars being acquired in April 2020 and kept for a period of three years under the proposed new tax rules. The perk car analysis assumed drivers would be higher rate tax payers and cover 10,000 miles per annum, with 5,000 miles as business mileage. For the job need analysis, it was assumed drivers would be basic rate taxpayers and cover 20,000 miles per annum, with 15,000 miles as business mileage. All drivers were reimbursed for business mileage at HMRC's advisory rates for company cars with employees claiming mileage allowance relief where applicable.

The table below shows the results for the perk cars analysed.

Car description				Company	Employee			
	List price	CO_2	Fuel type	WLC	Company car	Private car	Diff' (£s)	Diff' (as %)
Executive saloon	£35,240	127	Petrol	£22,617	£12,057	£9,852	(£2,205)	(18%)
	£38,060	113	Diesel	£24,596	£13,518	£10,758	(£2,760)	(20%)
	£39,925	37	PHEV	£19,502	£4,012	£10,068	£6,056	151%
	£42,850	0	EV	£18,753	£514	£13,139	£12,625	2,456%
Large executive saloon	£49,605	130	Petrol	£28,331	£17,763	£12,040	(£5,723)	(32%)
	£49,200	143	Diesel	£35,698	£21,185	£14,583	(£6,602)	(31%)
	£50,065	38	PHEV	£25,327	£3,072	£14,937	£11,865	386%
	£56,350	0	EV	£22,977	£676	£16,919	£16,243	2,403%
Executive SUV	£44,320	154	Petrol	£27,486	£18,274	£11,049	(£7,225)	(40%)
	£44,660	146	Diesel	£28,310	£19,958	£11,312	(£8,646)	(43%)
	£49,680	49	PHEV	£22,860	£5,672	£12,884	£7,212	127%
	£64,440	0	EV	£25,995	£773	£19,069	£18,296	2,367%

The results show fairly clear and consistent results for the perk cars analysed:

- For the petrol and diesel cars:
  - It is more cost effective for an employee to opt for a cash allowance to fund these cars privately via a personal lease (with savings of 18% to 43% compared to company car).
  - The main reason for this is the relatively high cost of company car tax making these cars expensive to select as a company car (due to the list price and company car tax rates).
  - Also, with an annual mileage of 10,000 miles, the cost of funding a personal lease and maintenance will be relatively modest.
- For the PHEV and EV:
  - It is more cost effective for an employee to opt to receive these cars a company car (with savings of 127% to 2,456% compared to a private car funded with a cash allowance).
  - The main reason for this is the low rates of company car tax for these vehicles, especially the EV where there would be a negligible amount of tax to pay over the three year period (as opposed to paying 40% income tax and 2% employee NI on the full value of any cash allowance received).
  - Also, the cost of personal leasing a PHEV or EV is typically highly then a petrol or diesel equivalent due to higher cost of the technology involved with these vehicles.

The table below shows the results for the job need cars analysed.

Car description				Company	Employee			
	List price	CO_2	Fuel type	WLC	Company car	Private car	Diff' (£s)	Diff' (as %)
Small hatchback	£18,115	106	Petrol	£18,232	£2,564	£5,102	£2,538	99%
	£19,410	96	Diesel	£18,766	£5,870	£8,239	£2,369	40%
Medium hatchback	£21,350	115	Petrol	£21,885	£1,558	£4,408	£2,850	183%
	£20,845	92	Diesel	£20,349	£2,361	£5,361	£3,000	127%
	£31,640	28	PHEV	£22,772	£971	£3,160	£2,189	225%
Large hatchback/ saloon	£23,835	150	Petrol	£23,828	£3,145	£4,446	£1,301	41%
	£25,235	123	Diesel	£23,651	£4,635	£6,725	£2,090	45%
	£36,335	34	PHEV	£27,223	£7,590	£17,257	£9,667	127%
Large hatchback/ saloon	£28,090	128	Petrol	£26,372	£4,368	£7,437	£3,069	70%
	£29,430	142	Diesel	£27,729	£7,156	£7,857	£701	10%
	£37,865	37	PHEV	£27,806	£7,691	£17,637	£9,946	129%

As above, the results show fairly clear and consistent results for the job need cars analysed:

- For all cars, it is more cost effective for the employee to opt to receive the car as a company car (with employee costs being between 10% and 225% higher funding the same cars with a cash allowance).
- This is due to the combined impact of relatively low costs of company car tax and high costs of funding a private car.
- With less expensive cars that have lower CO_2 emissions, the benefit in kind value for the cars analysed is relatively low. In addition, with employees paying the basic rate of income tax (20%), this can result in a relatively low cost of company car tax.
- In the job need analysis the cars were assumed to be covering 20,000 miles per annum and the higher levels of mileage are likely to result in higher costs for depreciation and maintenance. As a result, the personal lease and maintenance costs for higher mileage contracts can become quite expensive.
- As above, the cost of personally leasing a PHEV is likely to be greater than petrol and diesel equivalents. This is demonstrated by the results above that show the PHEV is the most expensive option to fund with a cash allowance.

Please note, EVs were not included in the analysis of job need company cars due to the selection and range of cars available unlikely to meet the needs of as heavy use job need fleet at this point. However, the position is likely to change in the coming years as manufacturers introduce a wider selection of EVs with longer range capabilities.

Observation:

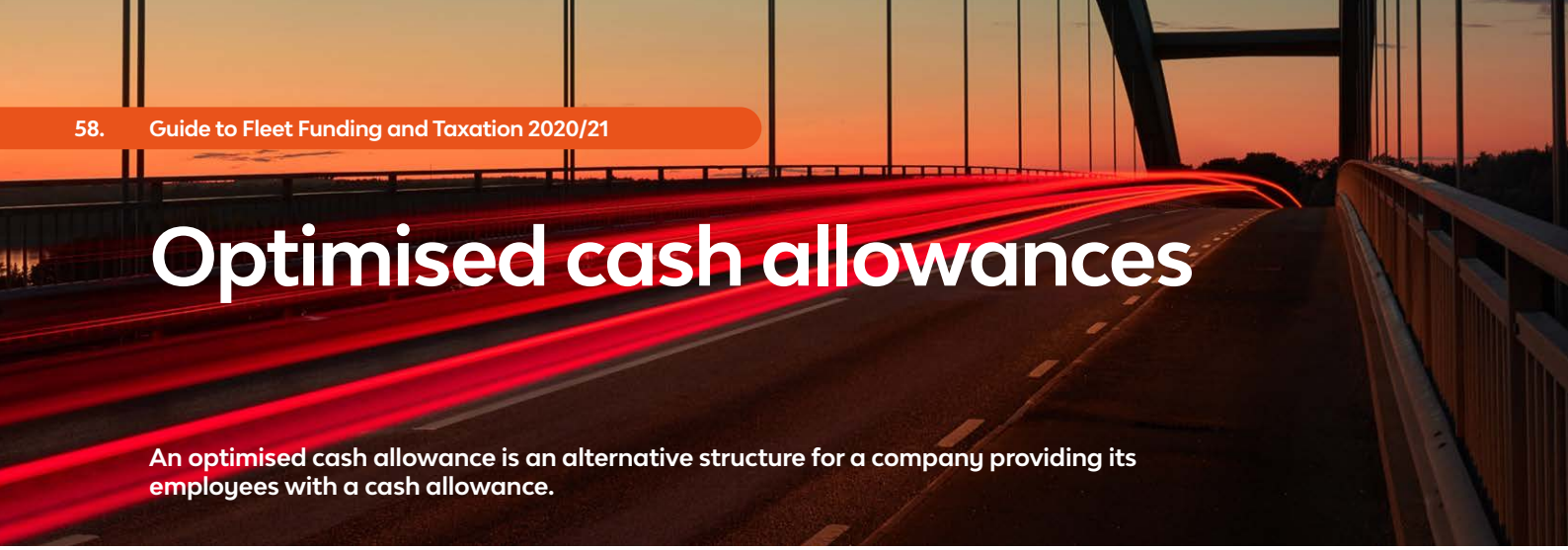
The results of the case study provide insight into the financial implications for companies and employees considering the choice between company cars and cash allowance.

With perk car fleets, where employees are typically higher rate tax payers and can choose higher value cars, switching to use a cash allowance can be a more cost effective approach (if the car in question has a petrol or diesel engine). This dynamic is likely to be one of the reasons that a number of companies have moved away from providing company cars to perk employees in recent years.

However, with lower rates of company car tax set to take effect in April 2020 for PHEV and EV vehicles, it is much more cost effective to opt for a company car instead of funding private car funded with a cash allowance for these vehicles. Introducing the PHEVs and EVs as an option for perk fleet may present an interesting opportunity for companies and employees.

When looking at job need fleets the picture is quite different, with company cars shown as being the most cost effective option in the examples shown. The reasons for this are the relatively low cost of company car tax, and high cost of personal leasing for high mileage contracts. It is worth noting that some of the potential challenges for adopting PHEVs and EVs, such as range anxiety and charging times, may be more pronounced for employees needing to spend a lot of time on the move and cover long distances as part of their job.

Overall, the results show that there is no simple answer to choosing the most cost effective option when given the choice of a company car or a cash allowance. It is important for companies and employees to consider a wide range of factors such as personal tax position, car value, CO_2 emissions, contract mileage etc. if they are to make an informed choice and deliver a policy that works for the business and its employees.



Optimised cash allowances

An optimised cash allowance is an alternative structure for a company providing its employees with a cash allowance.

What is an optimised cash allowance?

Introduction

An alternative funding option for a company providing cash allowances to employees is an optimised cash allowance arrangement. Typically, these arrangements are implemented by a business where its employees receive a cash allowance and undertake business mileage in their own car where the business mileage reimbursement rates for these employees are below HMRC's AMAP rates.

How did the OpRA legislation affect employee car ownership schemes?

How did the OpRA legislation affect employee car ownership schemes?
Due to the way in which optimised cash allowance arrangements worked historically, they were be affected by the OpRA legislation in much the same way as ECOS arrangements. As a result, most optimised cash allowance arrangements ceased to be effective where AMAPs were no longer be exempt from income tax when paid by an employer as part of an OpRA arrangement. However, as with ECOS arrangements, it is possible to structure an optimised cash allowance arrangements so it no longer falls within the scope of the OpRA legislation.

What are the implications of using an optimised cash allowance?

The objective of implementing an optimised cash allowance arrangement is typically to deliver a cost reduction for the company. With a good sized population of employees and, the right profile of business mileage, an optimised cash allowance arrangement can deliver worthwhile savings when compared to providing traditional fixed cash allowances. One advantage of an optimised cash allowance arrangement is that it carries a relatively low financial risk because if the right profile of business mileage is not present, then the cash allowance and business mileage reimbursement paid will be the same as a traditional fixed cash allowance.

Depending on the way in which an optimised cash allowance arrangement is structured, it can also deliver a financial benefit to employees through reduced NI costs. Also, it can help to ensure employees receive the full value of any Mileage Allowance Relief (MAR) they are entitled to thus reducing employee administration. If employees have not previously been claiming MAR, this can then result in a further increase in take home pay.

When it comes to the implementation and operation of an optimised cash allowance arrangement it typically involves additional administration when compared to traditional fixed cash allowances. This may include:

- The work involved with communicating how the arrangement works to employees.
- Answering any employee queries about the arrangement
- The additional administration involved with the monthly processing of business mileage claims.
- Seeking assurance from HMRC in respect of the income tax and NI treatment of payments in the arrangement.

If an optimised cash allowance arrangement is correctly implemented and operated in a compliant manner, then it can offer a cost effective alternative to providing traditional fixed cash allowances. It can also offer advantages to employees that can result in an increase in take home pay. However, there will additional work required to implement the arrangement as well as additional administration involved with the ongoing operation of the arrangement. It is important for any company considering an optimised cash allowance arrangement to ensure that it carefully considers the benefits and risks of the arrangement in detail before committing to any changes.

What non-financial factors should also be examined when providing cash allowances?

A company needs to consider other non-financial factors when moving from a company car scheme to a cash allowance scheme.

Corporate image

Giving employees the freedom to spend money on their choice of vehicle is great, but what boundaries need to be set? For example, if an employee arrives at work driving a new, two-seater sports car, this raises questions as to what message this sends out to company clients when they visit them. The correct image is important to a company and a car that sends an inappropriate message is not helpful in this regard.

Corporate risk

Replacing a company car with a cash allowance relieves the company of the ability to control such things as maintenance, insurance and MOTs and these instead become the responsibility of the employee. However, many companies are battling with how to deal with what is sometimes referred to as the "grey fleet", where cars are termed 'grey' because it is often unclear as to where responsibilities lie for such matters as insurance and maintenance. The lack of control can give rise to concerns around corporate manslaughter legislation which provides for some very severe measures against companies that are not ensuring employees are properly insuring and maintaining private vehicles used for business purposes.

Car scheme policy and administration

The above two issues highlight areas where a company would have to issue guidelines and become involved in administrative matters.

In the example regarding corporate image, it may be necessary to issue guidelines for all cars (e.g. all cars must have 4 doors, or the boot must be large enough to carry standard company equipment). It will become someone's responsibility to check that an employee's choice of car conforms to these criteria prior to approval.

In the example on corporate risk, it may be necessary to introduce a system whereby copies of a driver's insurance, MOT and VED certificates are all recorded. Again, it will become someone's responsibility to monitor this system, record all the information and chase drivers when certificates held on file are out of date.

Companies may be ill-prepared to deal with these new administrative tasks and may not have the appropriate systems in place to do so. Inevitably, this would lead to an increased level of administration. The introduction of such systems may not suit every organisation but they are an integral part of introducing a cash allowance scheme.

What other considerations are there when providing cash allowances?

When examining the provision of cash allowances there are further considerations worth bearing in mind. These include:

Q. Is it possible to reclaim VAT on reimbursement paid for business mileage?

A. A company can reclaim VAT on the reimbursement paid to employees travelling business mileage in a private car. However, if the company reimburses at a rate in excess of the equivalent AFR then the VAT is typically capped at the level of AFRs

Q. What happens if a company reimburses employees for private mileage?

A. If an employee is reimbursed for the cost of private fuel used in a private car the impact on the company and employee is quite different to that in a company car as there is no fixed private fuel scale charge and the cost is related to the amount of fuel used. The employee will pay tax on the value of the fuel used and this will generally be reported to HMRC on the Form P11D at the end of the year. The company will pay for the private fuel purchased, any applicable VAT and employer's NI based on the value of the private fuel used.

Q. What happens if an employee has not claimed Mileage Allowance Relief (MAR)?

A. If employees have not previously made a claim for any MAR in respect of business mileage they have undertaken in a private car they may be able to claim relief for earlier years, but normally only where those years are still open for tax adjustment and subject to having the required supporting documentation.

Salary sacrifice

Salary sacrifice is a contractual agreement between employee and employer to give up the right to receive an element of salary in exchange for some form of non-cash benefit in kind.

Salary sacrifice is integral to many corporate flexible benefits arrangements in the UK. Employees can typically choose from a range of benefits for which to sacrifice salary, including for example health insurance, bikes for work and pension contributions.

The attractiveness of this particular type of arrangement to an employee stems ordinarily from a reduction of the income tax and NICs chargeable to the total remuneration package. Employees give up taxable salary and receive non-cash benefits that could be exempt from tax, or at least subject to lower levels of tax. The employer's costs of providing the benefits are covered by no longer paying the salary and employer's NIC thereon. Savings for the employer could also arise, depending on the arrangement design.

Salary sacrifice for company cars

Provision of a fully maintained and insured company car as part of a salary sacrifice arrangement became increasingly popular in the decade leading up to 2017. The overall cost to an employee of no longer receiving the salary, plus paying tax on the company car BIK was often lower than leasing the same brand new car privately.

The introduction of the OpRA legislation had a dramatic impact on the popularity of salary sacrifice for company car arrangements. The government's stated objectives for OpRA was to remove the income tax and employer's NIC advantages of salary sacrifice arrangements for most benefits, including cars. Salary sacrifice arrangements for the most popular cars lost much of their financial efficiency and the numbers of cars taken via salary sacrifice arrangements began to fall.

The government did, however, agree with industry lobbying to exempt Ultra Low Emission Vehicles ("ULEVs") from these rules. Importantly, this exemption maintains the financial attractiveness of salary sacrifice for ULEVs, which are vehicles that emit 75g/km of CO_2 or less. ULEVs are typically plug-in hybrid petrol/electric and pure electric cars in this context. This is, of course, squarely in line with the government's low carbon agenda.

What are the financial advantages of salary sacrifice for an ULEV?

There are a number of reasons why a salary sacrifice arrangement for ULEVs may be attractive for employers and employees. These include:

- **Low rates of company car tax**

  With the introduction of low rates of CCT for zero emission EVs, as well as some PHEVs, this can result in very low BIK values for these cars. When compared to the income tax and NI that would have otherwise been due on the sacrificed salary, these arrangements can offer employees a financial advantage.

- **National insurance efficiencies**

  The employers Class 1A NI liability for a company car is calculated based on the BIK value for the car in question. As noted above, the BIK value for a ULEV can be very low and so there may be a minimal NI cost associated providing a ULEV company car. In contrast, an employer would pay Class 1 NI in respect of the value of the salary sacrificed which is likely to be much higher than the BIK for the company car. As a result, salary sacrifice for a ULEV can generate an NI efficiency for the business that can be kept as a saving, or passed on to employees in the form of a reduced cost.

- **Bulk buying power**

  Where an employer provides company cars to employees it can usually negotiate discounts based on the number of cars it will order from a particular provider or vehicle manufacturer. In general, the bulk buying power of an employer will result in greater discounts and lower prices for cars when compared to an individual employee on the high-street. Therefore, salary sacrifice arrangements can allow employees not typically entitled to a company car to access the bulk buying discounts of employers.

Let's look at some examples

To help illustrate the potential benefits of salary sacrifice for ULEV arrangements, we have included some examples below. The examples show the net employee cost of taking a ULEV via salary sacrifice compared to the cost of the same vehicle funded privately using a personal lease, or a comparable ICE car also funded using a personal lease.

The net employee cost calculation for:

- Salary sacrifice is the net value of the salary sacrificed (after taking account of the income tax and employee NI that would have been due on the salary) plus the amount of CCT due on the company car Bik.
- Personal lease is the net cost to the employee of funding the car via a personal lease paid for some salary (after taking account of the income tax and employee NI due).

In all the examples the cars were provided over a 3 year term assuming 10,000 miles per annum and included maintenance and motor insurance.

Example 1: Medium hatchback

The cars used in this example are:

- A zero emission ULEV with a list price of £33,785; and
- A diesel engine car with a list price of £28,565 and CO_2 emissions of 118g/km.

	Zero emission ULEV		ICE equivalent
	Salary sacrifice	Personal lease	Personal lease
Net employee cost	£10,232	£20,034	£20,985
Saving of salary sacrifice (36 months)	-	£9,802	£10,753
Saving of salary sacrifice (per month)	-	£272	£299

The example shows that opting to receive the ULEV via a salary sacrifice is forecast to be £272 (net) more cost effective than personally leasing the same car. In addition, the salary sacrifice arrangement is forecast to be £299 (net) per month more cost effective than personally leasing a comparable ICE version of the car.

Example 2: Premium SUV

The cars used in this example are:

- A zero emission ULEV with a list price of £86,550; and
- A diesel engine car with a list price of £70,300 and CO_2 emissions of 181g/km

	Zero emission ULEV		ICE equivalent
	Salary sacrifice	Personal lease	Personal lease
Net employee cost	£28,718	£54,666	£51,264
Saving of salary sacrifice (36 months)	-	£25,948	£22,564
Saving of salary sacrifice (per month)	-	£721	£626

The example shows that opting to receive the ULEV via a salary sacrifice is forecast to be £721 (net) more cost effective than personally leasing the same car. In addition, the salary sacrifice arrangement is forecast to be £626 (net) per month more cost effective than personally leasing a comparable ICE version of the car.

Example 3: Executive saloon

The cars used in this example are:

- A zero emission ULEV with a list price of £49,840;
- A diesel engine car with a list price of £39,960 and CO_2 emissions of 113g/km

	Zero emission ULEV		ICE equivalent
	Salary sacrifice	Personal lease	Personal lease
Net employee cost	£14,649	£28,805	£28,908
Saving of salary sacrifice (36 months)	-	£14,156	£14,259
Saving of salary sacrifice (per month)	-	£393	£396

The example shows that opting to receive the ULEV via a salary sacrifice is forecast to be £393 (net) more cost effective than personally leasing the same car. In addition, the salary sacrifice arrangement is forecast to be £396 (net) per month more cost effective than personally leasing a comparable ICE version of the car.

Observation:

The examples show that salary sacrifice for a ULEV can offer a significant financial advantage for employees when compared to funding the same car using a personal lease. In addition, the analysis also shows that salary sacrifice for a ULEV can also offer large cost savings when compared to the cost of personally leasing a comparable ICE car. As a result, a salary sacrifice arrangement has the potential to offer an engaging car scheme arrangement for employees that can deliver significant financial benefits as well as an opportunity to reduce carbon emissions.

It will be important for companies and employees to carefully consider the pros and cons of a salary sacrifice arrangement to make sure it will deliver the desired benefits. For example, the practical implications of EV/PHEV use, or the time and cost involved with scheme design and ongoing administration will need to be thought through and managed.

What other the other benefits for salary sacrifice?

For employers, providing access to ULEVs to their employees in such a financially beneficial way can create a positive impact in a more flexible and engaging benefits package, which can aid recruitment and retention. As these cars are publicly perceived as environmentally considerate, it could appeal to corporate social responsibility agendas, as well as the growing public desire to drive 'greener' cars.

As the cars are acquired under corporate leases, their cost can be further mitigated through the company's corporate buying power, if leasing cars at some scale across the business. This reduces the salary sacrifice required to cover the employer's cost of providing the car, which in turn reduces the cost to the employees.

Many business operators might also consider it more convenient, visible and controlled to manage individuals driving occasional business mileage in these brand new and fully managed company cars, rather than in private cars. Such an arrangement could reduce the number of "grey fleet" drivers, where management and tracking of health and safety obligations can prove problematic.

For employees, it is incredibly attractive to be able to access these 'greener' cars at much lower cost than in the retail environment, together with fixed corporate insurance and no requirements for personal credit assessments. As these cars are company cars, they will be maintained in accordance with manufacturer guidelines, managed by the car lessor. For employees who have never experienced a company car before, they would no doubt appreciate the reduced hassle of car 'usership'.

What is HMRC's approach to salary sacrifice arrangements?

Salary sacrifice is a longstanding concept and is widely used in modern flexible benefits arrangements for a variety of benefits. Fundamentally, it is an agreement between employer and employee for the particular structure of that employee's remuneration package. HMRC's jurisdiction to such arrangements is limited to whether or not each element of the total remuneration package is correctly subject to tax and NIC. In addition, HMRC must be content that the sacrifice arrangement results is an 'effective sacrifice' on each occasion. This means that once the sacrifice arrangement has been entered, the employee cannot then easily ask for the right to the sacrificed salary to be reinstated down the line.

The usual approach to seeking clearance from HMRC is for the employer to provide details of a particular arrangement with an employee that is already in place and operating. Typically, the details provided include the document that the employee signs to enter the agreement, which should set out clearly what the arrangement includes. HMRC will review the clearance submission and provide its opinion of whether or not the sacrifice is effective and whether or not tax and NIC is being correctly reported and collected.

As these types of arrangement are subject to relatively recent law, i.e. the OpRA legislation that took effect in April 2017, employers should expect scrutiny in the operation of their arrangements. It is important to note that HMRC reviews arrangements on a case-by-case basis. There is no mechanism for a blanket approval for an "off the shelf" arrangement that may be marketed by car lessors.

What other considerations are there for salary sacrifice?

When examining the merits of salary sacrifice for company cars arrangements, there are may be further considerations, such as:

Q. Is the exemption from OpRA for low emission vehicles set to end in April 2021 when the transitional rules no longer apply?

A. No. The OpRA exemption for low emission vehicles is not dependent on the transitional rules and so is set to apply after April 2021.

Q. Does this benefit have to be available to all staff in a company?

A. Because the company car is taxed in the conventional way in all cases and does not rely on a tax exemption on condition of it being made available to all staff, a company can make this benefit available to subsets of staff as it see fit.

Q. Where might this benefit not work so well for staff?

A. It may be less suitable to a population if there is high staff turnover. This is generally because the contracts for the cars are terminated early, which generates charges to the business. These charges can be mitigated through early termination insurance, if available, or the business could build an internal accrued fund to pay the charges.

Q. Does salary sacrifice for company cars generate a saving for the company?

A. Salary sacrifice can generate a saving for a company, or the cars can be provided in cost neutral fashion. It is important to note that if the employer makes cost savings from the arrangement, then the cost to the employee is higher than it would otherwise be. The cost to the employee must remain attractive, or there would be limited take-up of the benefit, which would in turn hit corporate savings, so it is important to carefully assess the population and cars available. Given the significance of the potential savings available for employees for ULEVs, there is ample scope for employer savings in our view.

Q. Can a traditional company car scheme run alongside salary sacrifice?

A. Generally, cars are leased from car providers via contract hire (operating lease) for both corporate company car schemes and salary sacrifice for cars schemes. However, the distinction is usually that for a corporate scheme, an employee has entitlement to a company car benefit or cash allowance as part of their benefits package, whereas in a salary sacrifice arrangement, an employee has to sacrifice salary in return for the company car benefit. These two arrangements can co-exist quite happily, as they are generally intended for different populations.

Q. What are the risks to the company from implementing salary sacrifice for company cars?

A. The key risks are:

- Tax compliance: a salary sacrifice arrangement must correctly subject the constituent elements of remuneration to tax and NIC and it must be an 'effective sacrifice'. HMRC clearance of a live arrangement is recommended;
- Charges: not being effectively mitigated/ apportioned (early termination, excess mileage, damage etc); and
- Low take-up: usually a result of poor and uncoordinated communications to the employees.

Understanding company van benefit

This section explains why it is important for companies to be aware of the practicalities of providing company vans to employees and explains how van benefit is calculated.

Why should a company care about van benefit?

Sometimes, it is necessary for employers to provide their employees with a company van in order to carry out the duties of their job. This is especially true for jobs that involve carrying equipment and supplies, where it's not practical or desirable to provide a company car or use alternative transport options. In some sectors, due to the nature of the work involved, the van fleets operated are significantly larger than company cars and can be critical for a business to operate effectively.

In general, the provision of a company van is usually closely linked to the work carried out by an employee and may be viewed as a 'tool of trade', rather than an employee benefit. However, there are some circumstances where the provision of a company provided van is treated as a BIK. As a result, this can have implications to consider for both the business and its employees.

Where a company van is treated as a BIK this will result in an additional cost for the company because there will be an employer Class 1A NI cost associated with the vans provided. Also, from an employee perspective, there will be the issue of income tax due on the BIK value as well.

In terms of administration, it is important for a business to keep a close watch on what type of vehicles are being provided and how they are being used in order to administer the arrangements in an income tax an NI compliant manner. This is necessary to make sure a business can demonstrate whether a van should be treated as a BIK or not. In some cases, carefully management of van fleets is important for a business to make sure the vehicles provided fall within the HMRC definition of a van instead of a company car, and errors here can have significant cost implications.

This section explores the definition of a van, what constitutes private use in respect of vans that will trigger a BIK charge and how the BIK charge is calculated for the van as well as van fuel BIK.

Definition of a van

The first point to consider in respect of commercial vehicles is to determine whether the vehicles provided fall within the definition of a 'van' according to the tax legislation. Based on the legislation, a 'Van' means:

- "A mechanically propelled road vehicle which:
  a) Is a goods vehicle, and
  b) Has a design weight not exceeding 3,500 kilograms.
  And which is not a motor cycle"

The legislation goes on to explain that a 'goods vehicle' means "a vehicle of construction primarily suited for the conveyance of goods or burden of any description". On first glance, identifying the vehicles that should be treated as vans appears to be a relatively straightforward process. However, there are key details that need to be considered in order to come to the correct conclusion.

One example of the potential issues can be seen in a recent tax case focused on tax treatment of vehicles to decide if they should be treated as a company car or company van. The case involved some specific vehicles provided by a company which were based on a panel van design, although they included additional seating and windows behind the driver. The company originally treated the vehicles in question as vans, although HMRC challenged this and argued that the vehicles actually fall within the definition of a company car. The court decision in the Upper Tribunal was split, with result being one of the vehicles viewed as a van, while the other vehicle was found to be company car. The case has been appealed to the Court of Appeal, and so the result has not been finalised at this stage, however, it goes to show the complexity involved.

Double cab pickups

Double cab pickups have presented a challenge when assessing whether they fall within the definition of a van. The double cab pickup has both qualities of being suitable for private use and being able to carry goods or burden. When considering the factors relating to the construction of a double cab pickup, within this category, the view can be taken that they have a predominant purpose of carrying goods or burden.

To resolve some of the uncertainty, HMRC released guidance a number of years back to confirm their view of whether a double cab pickup falls within the category of a company car or a van. The HMRC guidance follows the definitions used for VAT purposes where a vehicle that has a payload of 1 tonne (1,000kg) or more is accepted as a van for benefit in kind purposes (for this purpose payload means gross vehicle weight). The guidance does point out that it is not possible to come up with a single blanket rule for all makes and model of double cab pickup and so each case will depend on the facts and exact vehicle specification involved.

The HMRC guidance also covers the issue of double cab vehicles provided with a hard top because this can affect the payload weight and potentially the tax treatment to apply. HMRC have agreed that a hard top consisting of metal, fibre glass or similar materials will be afforded a generic weight of 45kg. Therefore, adding a hard top to a double cab vehicle with a payload of 1,010kg will convert the vehicle into a company car (because the 45kg hard top reduces the payload to 965kg).

Determining if a van benefit charge should apply

Once it is established that a vehicle falls with the definition of a van, a business needs to look at how the van is used in order decide whether it should be reported as a BIK. If the use of the van meets certain conditions, then the cash equivalent of the van BIK is reduced to nil. In effect, this means the provision of a company van is not treated as a benefit, although there will still be record keeping requirements.

In summary, a company van is not considered to be a benefit where:

- The van is mainly used for business travel and commuting; and
- Any private use is 'insignificant'.

While there is no specific definition setting out what is 'insignificant' private use, the guidance published by HMRC does include some useful examples (see below) to help businesses understand what may, or may not, be considered insignificant private use.

Examples of insignificant use are an employee who (using the van):	Examples of use which is not insignificant are an employee who:
• takes an old mattress or other rubbish to the tip once or twice a year	• uses the van to do the supermarket shopping each week
• regularly makes a slight detour to stop at a newsagent on the way to work	• takes the van away on a week's holiday
• calls at the dentist on the way home	• uses the van outside of work for social activities

Source: HMRC 480(2019) Expenses and benefits: A tax guide

It is important to note that regardless of the chosen tax treatment for a company provided van, it will be necessary for a business to be able to demonstrate the required conditions for the chosen treatment have been complied with in practice as well as in theory. Companies will need a robust policy in place and will need to keep records to be able to substantiate the position taken and to complete end of year benefit reporting obligations, including any vans where there is a nil benefit.

Calculating a van benefit charge

If a company provided van is used for more than insignificant private use and reported as benefit, then the value of the benefit is based on a fixed charge published by HMRC to apply for a specified tax year. Currently, for the 2019/20 tax year, the value of the van benefit charge is £3,430 (a 2.4% increase over the prior tax year).

Where a van benefit charge applies, this will result in a Class 1A NI cost for the business as well as an income tax liability for the employee. Based on the full 2019/20 tax year, providing a company van with private use would result in:

- A Class 1A NI cost of £473.34 for the company (£3,430 x 13.8% Class 1A NI rate); and
- An income tax cost of £686 for the employee (£3,430 x 20% income tax rate).

To provide an incentive to use zero emission vehicles, the van benefit charge is reduced if the vehicle is an electric van that emits no CO_2. The table below shows the discounted van benefit published by HMRC that applies for electric vans. In Budget 2020, it was announced that from 6 April 2021, there will be a nil benefit charge for fully electric vans.

Tax year	% of van benefit
2019/20	60%
2020/21	80%
2021/22	0%

Van fuel benefit

If an employee is provided with fuel as well as a company van, then a fuel benefit charge also arises if the van is treated as a benefit. If there is only insignificant private use for a company van, then the fuel provided is considered as being available for business travel and there is no charge. Where the van fuel benefit charge applies, this works in the same way as the van benefit itself, with HMRC publishing a fixed charge for the tax year. Currently, for the 2019/20 tax year, the van fuel benefit charge is £655 (a 3.5% increase over the prior tax year).

What other considerations are there for fuel reimbursement?

When examining the provision of company vans, there are further considerations worth bearing in mind. These include:

Q. Does optional the optional remuneration arrangement legislation also cover vans?

A. Yes. The provision of a company van and fuel can fall within the scope of optional remuneration arrangement legislation if salary sacrifice is involved, or where a cash alternative is offered.

Q. How are car derived vans treated?

A. There are some car derived vans that HMRC will accept can be treated as a van instead of a company car. However, as noted above, the tax treatment of the vehicle will depend on the exact specification. Typically, a car derived van may look like a car from the outside, but inside it will have the look and function of a van because:

- there will be no rear seats, rear seat belts or mountings;
- there will be a payload area with floor panel in the rear of the vehicle; and
- there will be no side windows in the rear of the vehicle - or if present, side windows will be opaque and fixed (with no means of opening or closing).

Q. Do vans have the same corporation tax and VAT treatment as cars?

A. No. Vans will fall within the definition of plant and machinery for the purposes of corporation tax and so will have a different treatment to cars. From a VAT perspective, there will also be differences to the way in which

Appendix 1 – Company car tax rates

The following tables show the appropriate percentage values to be used in the calculation of the BIK for company cars.

Please note: In the Budget 2020, it was announced, that company car tax rates will be frozen at the 2022/23 rates for a further two tax years until 5 April 2025.

Company car percentage values for cars registered before 6 April 2020

		Appropriate percentage[2]			
CO_2 emissions (g/km)	Electric range[1]	2019-20	2020/21	2021/22	2022/23
0	N/A	16	0	1	2
1-50	>130	16	2	2	2
1-50	70-129	16	5	5	5
1-50	40-69	16	8	8	8
1-50	30-39	16	12	12	12
1-50	<30	16	14	14	14
51-54		19	15	15	15
55-59		19	16	16	16
60-64		19	17	17	17
65-69		19	18	18	18
70-74		19	19	19	19
75		19	20	20	20
76-79		22	20	20	20
80-84		22	21	21	21
85-89		22	22	22	22
90-94		22	23	23	23
95-99		23	24	24	24
100-104		24	25	25	25
105-109		25	26	26	26
110-114		26	27	27	27
115-119		27	28	28	28
120-124		28	29	29	29
125-129		29	30	30	30
130-134		30	31	31	31
135-139		31	32	32	32
140-144		32	33	33	33
145-149		33	34	34	34
150-154		34	35	35	35
155-159		35	36	36	36
160-164		36	37	37	37
165+		37	37	37	37

[1] Electric range is the number of miles which is the equivalent of the number of kilometres specified in an EC certificate of conformity, an EC type-approval certificate or a UK approval certificate on the basis of which a car is registered, as being the maximum distance for which the car can be driven in electric mode without recharging the battery.

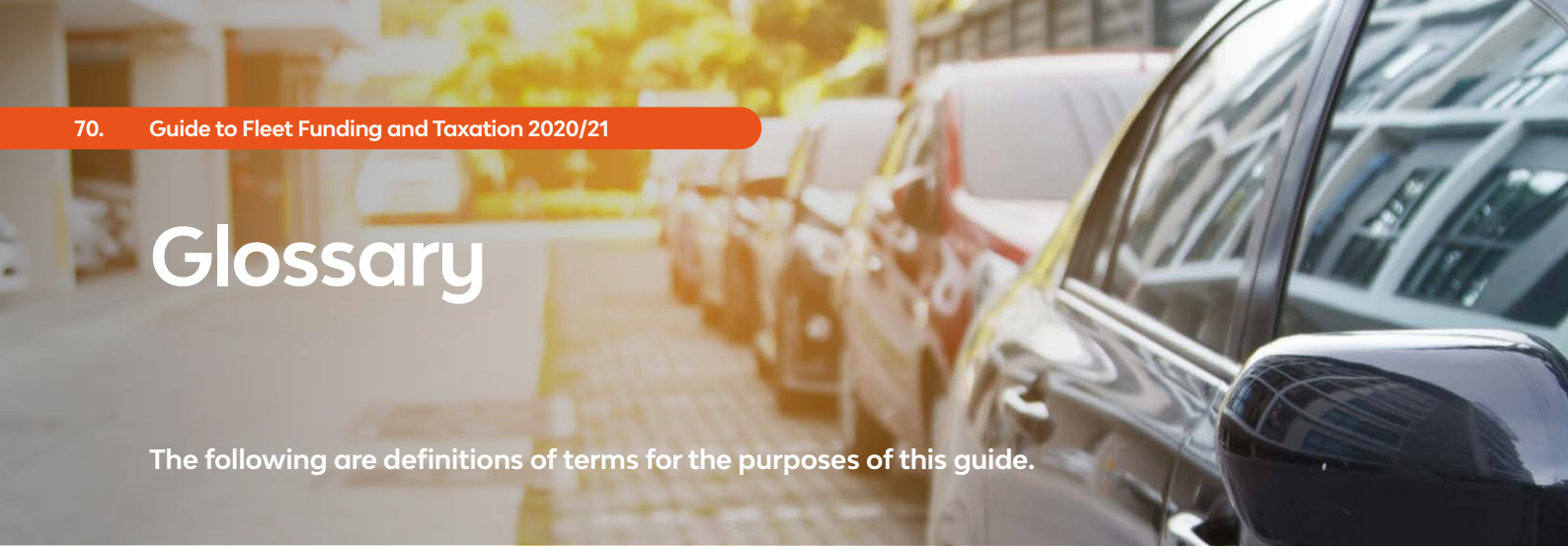
[2] Add the 4% supplement to the '% list of price' if the car runs solely on diesel (up to the limit of 37%). Do not add the supplement if the car is also certified to the Real Driving Emissions Step 2 (RDE2) standard.

Company car percentage values for cars registered on, or after, 6 April 2020

		Appropriate percentage[2]			
CO_2 emissions (g/km)	Electric range[1]	2020/21	2021/22	2022/23	2023/24
0	N/A	0	1	2	2
1-50	>130	0	1	2	2
1-50	70-129	3	4	5	5
1-50	40-69	6	7	8	8
1-50	30-39	10	11	12	12
1-50	<30	12	13	14	14
51-54		13	14	15	15
55-59		14	15	16	16
60-64		15	16	17	17
65-69		16	17	18	18
70-74		17	18	19	19
75-79		18	19	20	20
80-84		19	20	21	21
85-89		20	21	22	22
90-94		21	22	23	23
95-99		22	23	24	24
100-104		23	24	25	25
105-109		24	25	26	26
110-114		25	26	27	27
115-119		26	27	28	28
120-124		27	28	29	29
125-129		28	29	30	30
130-134		29	30	31	31
135-139		30	31	32	32
140-144		31	32	33	33
145-149		32	33	34	34
150-154		33	34	35	35
155-159		34	35	36	36
160-164		35	36	37	37
165-169		36	37	37	37
170+		37	37	37	37

[1] Electric range is the number of miles which is the equivalent of the number of kilometres specified in an EC certificate of conformity, an EC type-approval certificate or a UK approval certificate on the basis of which a car is registered, as being the maximum distance for which the car can be driven in electric mode without recharging the battery.

[2] Add the 4% supplement to the '% list of price' if the car runs solely on diesel (up to the limit of 37%). Do not add the supplement if the car is also certified to the Real Driving Emissions Step 2 (RDE2) standard.



Glossary

The following are definitions of terms for the purposes of this guide.

A

Approved Mileage Allowance Payments (AMAPs)

The statutory reimbursement rates for employees undertaking business mileage in a private car.

Advisory Fuel Rates (AFRs)

The rates published by HMRC for reimbursement for employees undertaking business mileage in a company car. If the rate paid per mile of business travel is no higher than the advisory rate for the particular engine size and fuel type of the car, HMRC will accept that there is no taxable profit and no Class 1 NICs liability.

Air Quality Plan (AQP)

The government is legally obliged to publish an Air Quality Plan when air pollution limits are breached. The most recent plan was published in July 2017. It announced a ban on the sale of new petrol and diesel cars and vans by 2040 (since brought forward to 2035) and ordered numerous local authorities to develop their own plans for cleaner air.

B

Balloon

A large final payment under a financing agreement that is normally set in-line with the forecast residual value of the car.

Benefit in kind (BIK)

A reward for services that an employee receives from the company they work for, other than their usual cash pay. Company car is the main example within this guide.

Business mileage

A journey that the employee is obliged to undertake in the performance of their duties. Home to a permanent place of work travel is not deemed business mileage.

C

Capital Allowance

A means of obtaining a tax relief for the depreciation of an asset spread over a number of years.

Capital contribution

A capital sum an employee contributes towards the expenditure on the provision of a company car or qualifying accessory. The amount of the contribution is deducted from the list price when calculating the income tax due on the Benefit in Kind.

Car fuel benefit

The reportable value of fuel provided for private use in a company car.

Company Car Tax (CCT)

A form of Benefit-in-Kind taxation paid on any company car an employee receives in addition to his or her salary. CCT rates are based on the car's list price and its CO_2 emissions, with a supplement for diesel vehicles. A new system is set to be introduced in 2020-21, which will mean lower rates for low-emission vehicles.

Company car benefit

The amount chargeable to tax on an individual for a company car in a tax year.

Contract hire

The leasing of a car for a fixed monthly cost over a pre-agreed contract term and mileage (sometimes described as operating leases). The car is returned to the owner (the fleet provider) at the end of the contract term. The agreement may include the provision of services such as maintenance.

Contract purchase

A deferred purchase agreement normally with a balloon payment. The agreement may include the provision of services such as maintenance.

Contributions for private use

The amount an employee is required to pay as a condition of the car being available for private use. The amount of the contribution is deducted from the company car benefit for the year in which payments were made.

D

Depreciation

The loss in value between the purchase price and sale value of a car. This may differ from the depreciation for tax or accounting purposes.

E

Electric vehicle (EV)

Hybrid vehicles involve a degree of electric power – but 'EV' is generally considered to refer to pure, battery-electric vehicles. These are vehicles powered entirely by an electric battery, which is charged by plugging it into the grid. EVs emit no CO_2 on the road, although CO2 may be emitted during the production of the electricity they consume.

Employee Car Ownership Plans (ECOP)

An arrangement that allows employees to acquire a car, usually within a specified framework and from a single fleet provider. The arrangement is usually designed to offer similar benefits to a company car from the employee's perspective with the policy often remaining comparable in terms of how issues like car selection, support and servicing are dealt with.

F

Finance lease

Generally, a lease that transfers substantially the risks and rewards of ownership of an asset to the lessee. The agreement may include the payment of a balloon payment or may be a fully amortised with no balloon.

Fuel card

A method of payment whereby the business pays for the fuel used by an employee.

Fuel scale charge

The taxable benefit where an employee is provided with free fuel for private use.

First-year allowance (FYA)

A type of capital allowance that applies for the year in which an asset was first purchased. Companies are able to deduct the cost (or some portion of the cost) of a qualifying asset from their profits before any tax liability is calculated.

H

Hire purchase

A purchase agreement where the title (ownership) does not pass until an option to purchase has been satisfied. This is normally a nominal payment.

HM Revenue and Customs (HMRC)

The government department that's responsible for collecting taxes and for paying some types of benefit. It doesn't have its own minister in the Cabinet, although the Financial Secretary to the Treasury does assume responsibility for matters relating to HMRC.

I

IFRS16

A new accounting standard for companies that are signed up to the International Finance Reporting Standard (IFRS). It was published in 2016 and took effect for accounting periods beginning on or after 1st January 2019. Under IFRS, most leases will need to be reported on balance sheet.

L

Lease

An arrangement where the customer has use of goods but does not legally own them.

Lease rental

The payment under a lease agreement.

Lessee

The customer in a lease agreement.

Lessor

The owner of the goods in a lease agreement.

List price

See P11D Value.

M

Modified Cash Equivalent

This is calculated using the same method as a company car tax calculation for a BIK. However the effect of any private use or capital contributions on the car is removed. It is compared against the amount of cash or salary forgone to calculate the basis for charging tax on a company car caught by the new OpRA legislation.

N

National Insurance contributions (NICs)

Effectively a tax on income, which secures an employee's right to certain benefits, such as a state pension. Employees and employers pay NICs on their earnings. But employers also pay them on certain Benefits-in-Kind provided to employees, including company cars – these are known as Class 1A NICs.

New European Driving Cycle (NEDC)

The previous regime for testing a vehicle's emissions and fuel efficiency. It has since been replaced by WTLP and RDE tests. Because NEDC took place entirely within a laboratory setting, and didn't account for many driving scenarios, its results were regarded as insufficiently accurate.

Nitrogen oxide (NOx) emissions

Oxides of nitrogen, such as nitrogen dioxide (NO2) and nitrogen oxide (NO), are emitted when nitrogen is burnt in the presence of oxygen. They are harmful for human health, and particularly for the human respiratory system. Diesel vehicles emit more NOx than non-diesel vehicles, which is why legislators are currently focussing on them.

O

Operating lease

A lease where the risks and rewards of ownership are borne by the lessor. Normally defined as a lease other than a finance lease. Normally referred to as 'contract hire'.

Optional Remuneration Arrangements (OpRAs)

An arrangement where an employee can forgo an amount of cash for a non-cash BIK or is offered a cash allowance as an alternative to a particular BIK. Common OpRAs mentioned in this guide are cash or car, salary sacrifice or employee car ownership schemes. The Finance Act 2017 has introduced new charging provisions on these arrangements.

P

P11D Value

The list price of a company car used in the calculation of company car tax.

Private mileage

Any mileage that does not constitute business mileage.

Plug-in hybrid electric vehicle (PHEV)

These are vehicles which are powered by both an ICE and a battery-electric motor. The range of the battery is typically between 15 to 40 miles, with most PHEVs running on pure electric up to 70 mph. To fully charge the battery, the vehicle must be plugged in to a vehicle charge point or a 3-pin socket.

Private use contributions (PUCs)

A payment made by an employee for the private use of an asset; in this case, a company car. PUCs are taken into account when calculating CCT.

R

Real Driving Emissions (RDE) tests

These have been developed by the European Commission to more accurately record a car's emissions, especially of harmful air pollutants such as NOx. Unlike WLTP and the old NEDC regime, the RDE tests take place on real roads. As of January 2021, all new car types will need to be compliant with RDE Step 2 – meaning that they cannot emit more than 126mg of NOx per kilometre.

Rental

See lease rental.

Residual Value

The amount for which a car is sold for at the end of the contract.

T

Tax year

For an individual, the tax year ends on 5 April. Therefore, the 2017/18 tax year runs from 6 April 2017 to 5 April 2018.

Tax written down value (TWDV)

As it relates to company cars, the TWDV is the value of the car for tax purposes, after the WDA has been applied each year.

U

Ultra-low emission vehicles (ULEVs)

Vehicles that emit less than 75 grammes of CO_2 per kilometre. They enjoy numerous tax breaks and exemptions, including lower rates of CCT.

V

Vehicle Excise Duty (VED)

An annual tax on cars used on the road. For cars registered on or after 1 April 2017, the first-year rate is based on the car's CO_2 emissions, then a standard rate is paid in subsequent years, with supplements for diesel cars and more expensive cars. Zero-emission vehicles are exempt from VED.

W

Worldwide Harmonised Light Vehicle Test Procedure (WTLP)

The new regime for measuring a new car's CO_2 emissions and fuel consumption. WLTP is considered to be more accurate than the previous NEDC regime, not least because it involves longer tests featuring a wider range of realistic driving scenarios. It has applied for all newly registered cars from 1st September 2018.

Whole Life Cost (WLC)

The post corporation tax cost of funding a company car or cash allowance which includes all commercial costs (such as payments, maintenance, business fuel, etc.) as well as all direct and indirect tax costs.

Writing Down Allowance (WDA)

The amount of capital allowances that may be claimed in any single year, calculated as a percentage of the car's written down value for which a deduction may be taken in the company's tax computation.

Written down value

The residual tax value of a car in a company's tax computation. It is the original value of the car less the sum of capital allowances given since its purchase.

V

Value Added Tax (VAT)

VAT is charged on taxable supplies of goods and services.

Vat Fuel Scale Charge

Where a business pays for road fuel on behalf of its employees a method of dealing with the VAT charged on the fuel is to reclaim all of the VAT and pay the appropriate fuel scale charge. This is a way of accounting for output tax on fuel that a business buys but that is then used for private motoring.

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