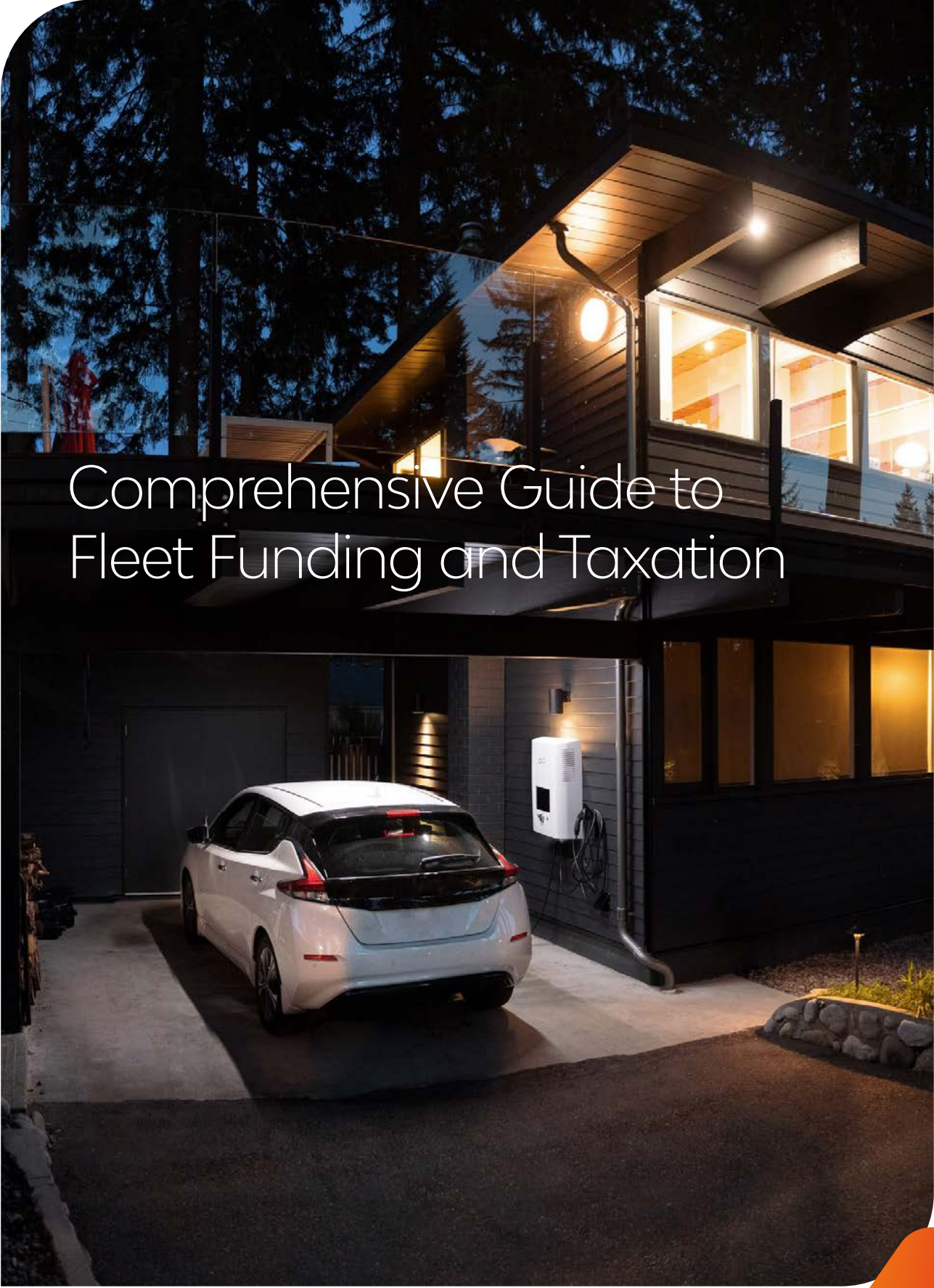




Comprehensive Guide to Fleet Funding and Taxation

2023/24 Guide

leaseplan.com





About this guide

The guide was published on 23.02.2023 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 this guide a useful reference to the key tax and technical issues that you face when you are thinking about your fleet.

Disclaimer

This publication is intended to provide general information and is not an exhaustive treatment of either the topic as a whole, or the subjects raised. Accordingly, it should not be relied on to address specific situations or circumstances and is not a substitute for accounting, tax, legal, investment, consulting or other professional advice. Before making any decision or taking or refraining from any action which might affect you, your employees or any third party in any way, including in relation to finances or business affairs, you should consult a qualified professional adviser.

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Welcome

Welcome to the 2023/24 edition of the LeasePlan guide to funding and taxation, produced in association with Deloitte.

We know this is a tough time for many organisations and their fleets. The UK has faced the effects of Brexit, ongoing problems created by the COVID-19 pandemic and rising energy prices which have been exacerbated by the war in Ukraine. Some challenges are specific to our economy, but many more are being felt around the world. Inflation is at its highest since the late 1970s, while growth remains sluggish, and some of the sharpest rises have been seen in costs that are central to fleets – such as prices for petrol, diesel and electricity – as well as the cost and availability of new vehicles.

However, there are some silver linings among the storm clouds. In particular, there's the move to greener motoring, which is good for the planet – and, in our opinion, it's good for companies and fleets as well.

As it stands, sales of new fossil-fuelled cars and vans – excepting some hybrids – will end in the UK in 2030. And even if our Prime Minister decides to turn his back on that Boris Johnson-era policy, the rest of the world will not: many manufacturers, local policymakers, fleets and motorists have already decided that the future is electric.

This is reflected in many of the calculations and case studies in this Guide. Most motoring taxes, from Company Car Tax to Vehicle Excise Duty, have been designed to encourage the uptake of electric vehicles, with lower rates for lower emissions. Other policies, such as Salary Sacrifice, are also geared in favour of clean cars.

The same is true of the wider landscape. Over the past year or so, new Clean Air Zones have been introduced in numerous cities, from Bath to Birmingham to Bradford. Many more are set to follow – the trend is clearly going in one direction.

Of course, this doesn't mean that there won't be blips along the way. In June 2022, for example, the government ended the Plug-In Car Grant – one of the greatest incentives for EVs that there has yet been. But even this abrupt change reflected the fact that, unlike in the past, the market for electric cars is sufficiently mature that it no longer requires so much support.

For us, the important thing to remember in these challenging times is that you don't have to make the difficult decisions on your own. This Guide is a good example of the support you can get. It is designed to help you work out what's next for your fleet – in the months and years ahead. Then, if you find that you need any more assistance, just get in touch with our team. We firmly believe it's our job to provide you with all the help and information you need not just to survive – but to thrive.



M Walters

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Introduction

The last version of this guide was published in April 2020 and since then there have been significant developments affecting car schemes in the UK. As we emerged from the COVID-19 pandemic in 2020, the global economy started to return to a more 'normal' footing. However, we are still seeing the aftereffects of the pandemic and the disruption it had on supply chains with a global shortage of semiconductor chips. The chip shortage has hampered the ability of some vehicle manufacturers to keep up with the demand for new vehicles, especially EVs, and this has increased in the volatility in the UK used car market.

In February 2022, dramatic events unfolded on the global stage with the Russian invasion of Ukraine. The invasion triggered major disruption in the global economy and was a catalyst for the unprecedented rises in fuel and energy prices seen in the UK. During this time, the political situation in the UK was clouded in uncertainty, with the upheaval resulting in three new Prime Ministers in as many months.

Throughout the turmoil, some would argue the need to move to a net zero economy has been the biggest challenge of all. Given everything that has happened, it is hard to see how it has ever been more challenging for companies to deliver a cost effective and sustainable arrangements that will meet their needs, and those of their employees.

Headlines

In 2022 announcements affecting car scheme arrangements were made in the Spring Statement, the Mini-Budget and the Autumn Statement. We have summarised the key headlines made in 2022 affecting cars schemes (that were not undone with later changes):

Company car tax

- The government announced rates affecting the amount of income tax paid on company car benefits for an additional three tax years to provide long term certainty for taxpayers and industry, with rates now published covering 6 April 2025 through to 6 April 2028.
- The announcements set the appropriate percentage used to calculate the income tax due on company car benefit as follows:
 - For electric vehicles with CO₂ emissions of 0g/km - the applicable rate (2% in 2024/25) will rise by 1 percentage point each year for three subsequent tax years up to a maximum of 5% in 2027/28.
 - For ULEVs with CO₂ emissions of 1-74g/km - the applicable rates will rise by 1 percentage point in each of the three subsequent tax years, up to a maximum of 21% in 2027/28.
 - For all other vehicles with CO₂ emissions exceeding 74g/km - the applicable rates will be increased by 1 percentage point in the 2025/26 tax year up to a maximum of 37%. The rate will then remain frozen for a further two tax years until 6 April 2028.

Income tax

- It was announced that the income tax Personal Allowance (PA) and higher rate threshold will remain frozen at £12,570 and £50,270, respectively, until 2027/28, two years longer than originally planned.
- The threshold for the additional rate of income tax will reduce from £150,000 to £125,140 (from 6 April 2023). Employees with income between £125,140 and £150,000 will typically pay an extra 5% income tax on amounts in excess of the new threshold. Existing additional rate taxpayers will typically see an income tax increase of £1,243.
- The basic rate of income tax will be maintained at 20% (this reversed previous plans to reduce the basic rate to 19%).
- For employees paying Scottish income tax, the higher rate of income tax will rise from 41% to 42% from 6 April 2023.

National Insurance Contributions

- In November 2022, the Health and Social Care Levy was reversed and plans to introduce it as a separate tax in April 2023 were scrapped.
- From July 2022, the National Insurance Contributions (NICs) primary threshold and lower profits limit were increased to align with the PA and will now be maintained at this level from April 2023 until April 2028.

Vehicle Excise Duty (VED)

- From April 2025 measures will be introduced so that electric cars and vans will begin to be subject to VED in the same way as petrol and diesel vehicles.

Corporation tax

- The main rate of corporation tax will increase from 19% to 25% from 1 April 2023 as planned.
- The small profits rate for companies with taxable profits of less than £50,000 will remain at 19%, with a graduated increase up to 25% for companies with taxable profits between £50,000 and £250,000.
- The changes to the Bank Corporation Tax Surcharge which are legislated to take effect from 1 April 2023 will go ahead as planned. Therefore from April 2023, banks will be charged an additional 3% rate (instead of an additional 8%) on their profits above £100 million.

Other announcements

- Advisory Electric Rate (AER) – On 1 December 2022 the AER for fully electric cars rose from 5p to 8p per mile. From 1 March 2023 HMRC increased the AER again to 9p per mile.
- Energy Price Guarantee (EPG) – In October the government introduced the EPG to protect customers from increases in energy costs by limiting the amount suppliers can charge per unit of energy used. In the Autumn Statement it was announced that the EPG will be extended from April 2023 until April 2024.

Observation:

In the last 12 months there have been numerous significant developments affecting company cars and vans in the UK. The extension of the low tax rates for Electric Vehicles (EVs) will give greater certainty and a longer-term financial incentive for businesses and their employees to help boost the take up of EVs. However, the coming changes to VED will reduce some of the financial incentive currently available for people making the move to an EV. The unprecedented fluctuation in fuel and electricity price rises have caused a number of headaches, although the introduction of the EPG to limit electricity prices rises has helped to alleviate some of the issues.

On balance, there can still be a strong business case for making the move to electric with significant environmental and financial benefits on offer with robust and well-designed arrangements. Currently, the design of the tax system means employers are uniquely placed to enable and accelerate the switch to electric vehicles, and in some cases, make it a financially viable option that otherwise would not be open to some employees. However, in the coming years there will be challenges to overcome, especially as the government may seek to replace much needed revenue from tax on company cars, fuel duty and VED as more people make the switch to EVs.

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.

From 01 April 2023, the main rate of corporation tax will increase from 19% to 25% and the small profits rate for companies with taxable profits of less than £50,000 will remain at 19%, with a graduated increase up to 25% for those with taxable profits between £50,000 and £250,000. 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 CO₂ emissions of cars provided.

Corporation tax rate

From 1 April 2023 onwards:

Main rate (profits over £250,000)	25%
Small profits rate upper threshold	£250,000
Small profits rate lower threshold	£50,000
Small profits rate (profits under £50,000)	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.

Since April 2021, if a car has CO₂ emissions of 50g/km or below, then the full cost of the finance element of the lease rental will attract tax relief. However, where a car has CO₂ emissions above 50g/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 CO₂ emissions exceeding this threshold attract less corporation tax relief making them more expensive to provide.

Leasing rental restriction

From April 2021:

CO₂ emissions (g/km)	Allowed rentals	Disallowed rentals
50 or below	100%	0%
Above 50	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 CO₂ 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 CO₂ emissions.

Example 1: Tax relief for a leased car with CO₂ emissions of 50 g/km

A company leases a car using contract hire for a 36-month term with monthly lease rentals of £450 (for simplicity, in the examples we will assume the first lease rental is paid in the first month of the company's financial year which ends on 31 March). The CO₂ emissions are below the 50g/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 (FY24)	Yr 2 (FY25)	Yr 3 (FY26)	Overall
Lease rentals for tax relief	£5,400	£5,400	£5,400	£16,200
Corporation tax rate	25%	25%	25%	
Tax relief received	£1,350	£1,350	£1,350	£4,050

Example 2: Tax relief for a leased car with CO₂ emissions of 60 g/km

The same company leases a car using contract hire for a 36-month term with monthly lease rentals of £450. The CO₂ emissions are above 50g/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 (FY24)	Yr 2 (FY25)	Yr 3 (FY26)	Overall
Lease rentals for tax relief	£5,400	£5,400	£5,400	£16,200
Corporation tax rate	25%	25%	25%	
Tax relief for lease rentals	£1,350	£1,350	£1,350	£4,050
Less leasing disallowance	(£203)	(£203)	(£203)	(£608)
Tax relief received	£1,148	£1,148	£1,148	£3,443

Observation:

Comparing the tax relief received by the company in the two examples shows that the car with CO₂ emissions within the 50g/km threshold attracts additional tax relief for the company of £608 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.

Q. Are the corporation tax rules for leased vans the same as for leased cars?

- A. No. The CO₂ emissions-based leasing disallowance for cars does not apply to vans. In the case of vans, the cost of the lease rental can be deducted from profits for corporation tax purposes in full.

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 CO₂ emissions. The table (on the right) shows the WDA rates applicable from FY22 onwards based on the car CO₂ 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 CO₂ 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%. 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.

Writing down allowances

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 CO₂ emissions.

Example 1: Tax relief for a purchased car (CO₂ emissions 0g/km)

A company purchases a car for £35,000 outright on 1 April 2023 and keeps it for 36 months, after which it sells the car for £17,500. The CO₂ emissions of the car are 0g/km, 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:

Financial Year (ended 31 March)	Yr 1 (FY24) Purchase	Yr 2 (FY25)	Yr 3 (FY26) Disposal	Yr 4 (FY27)	Yr 5 (FY28)
Purchase price	£35,000				
Sale proceeds			(£17,500)		
TWDV	£35,000	£0	(£17,500)	(£14,350)	(£11,767)
WDA rate	100%	0%	18%	18%	18%
Capital allowances	£35,000	£0	(£3,150)	(£2,583)	(£2,118)
Corporation tax rate	25%	25%	25%	25%	25%
Tax relief	£8,750	£0	(£788)	(£646)	(£530)
Cumulative tax relief	£8,750	£8,750	£7,963	£7,317	£6,787
Cumulative tax relief accrued after 25 years ⁽¹⁾			£4,421		

⁽¹⁾ Assumes corporation tax and WDA rates are unchanged in future years

Example 2: Tax relief for a purchased car (CO₂ emissions 1-50g/km)

A company purchases a car for £35,000 outright on 1 April 2023 and keeps it for 36 months, after which it sells the car for £17,500. The CO₂ emissions of the car are between 1g/km and 50g/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:

Financial Year (ended 31 March)	Yr 1 (FY24) Purchase	Yr 2 (FY25)	Yr 3 (FY26) Disposal	Yr 4 (FY27)	Yr 5 (FY28)
Purchase price	£35,000				
Sale proceeds			(£17,500)		
TWDV	£35,000	£28,700	£6,034	£4,948	£4,057
WDA rate	18%	18%	18%	18%	18%
Capital allowances	£6,300	£5,166	£1,086	£891	£730
Corporation tax rate	25%	25%	25%	25%	25%
Tax relief	£1,575	£1,292	£272	£223	£183
Cumulative tax relief	£1,575	£2,867	£3,138	£3,361	£3,543
Cumulative tax relief accrued after 25 years ⁽¹⁾			£4,359		

⁽¹⁾ Assumes corporation tax and WDA rates are unchanged in future years

Example 3: Tax relief for a purchased car (CO₂ emissions above 50g/km)

A company purchases a car for £35,000 outright on 1 April 2023 and keeps it for 36 months, after which it sells the car for £17,500. The CO₂ emissions of the car are above 50g/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:

Financial Year (ended 31 March)	Yr 1 (FY24) Purchase	Yr 2 (FY25)	Yr 3 (FY26) Disposal	Yr 4 (FY27)	Yr 5 (FY28)
Purchase price	£35,000				
Sale proceeds			(£17,500)		
TWDV	£35,000	£32,900	£13,426	£12,620	£11,863
WDA rate	6%	6%	6%	6%	6%
Capital allowances	£2,100	£1,974	£806	£757	£712
Corporation tax rate	25%	25%	25%	25%	25%
Tax relief	£525	£494	£201	£189	£178
Cumulative tax relief	£525	£1,019	£1,220	£1,409	£1,587
Cumulative tax relief accrued after 25 years ⁽¹⁾			£3,566		

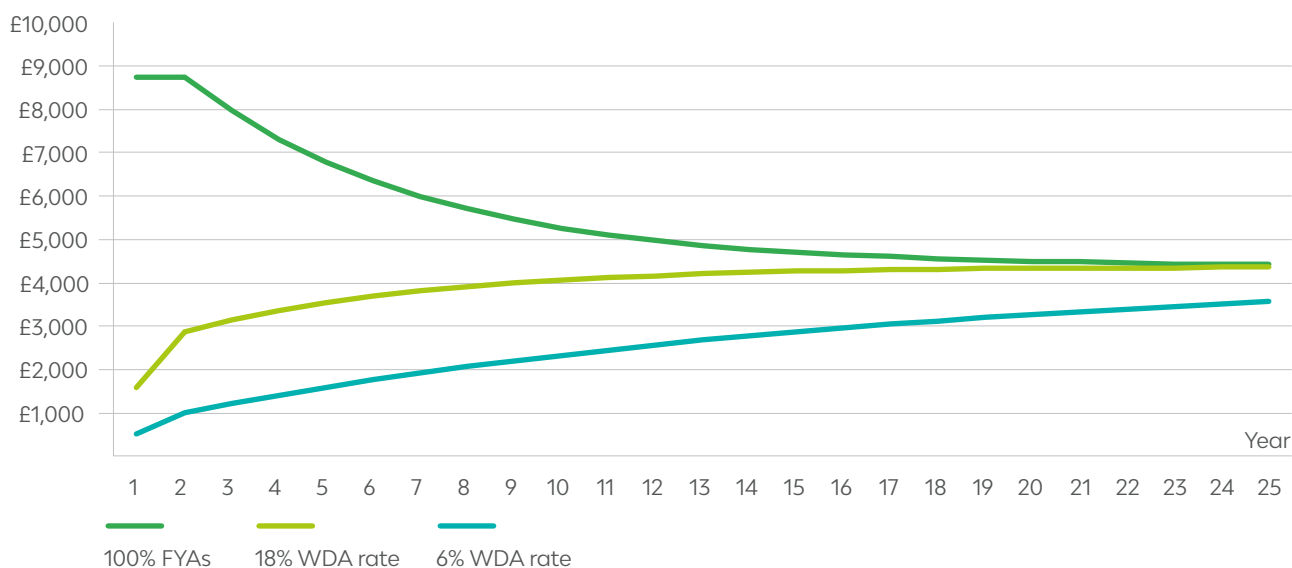
⁽¹⁾ Assumes corporation tax and WDA rates are unchanged in future years

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 over time towards the net cost of the car.

A comparison of tax relief provided via capital allowances

Cumulative tax relief



If the main rate of corporation tax remains static at 25% for the three examples above, the cumulative tax relief for the cars attracting 100% FYAs and the 18% WDA rate would broadly be the same after 25 years (at c.£4,400). However, the tax relief for the car attracting a 6% WDA rate would be lagging significantly behind (at £3,600). This illustrates the degree to which a company's cash flow can be impacted by employees choosing cars with higher emissions.

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 zero CO₂ emissions?

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 zero CO₂ 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).

Q. Are the corporation tax rules for purchased vans the same as for purchased cars?

A. The rules for purchased cars and vans are similar, but there are some differences. Zero emission vans qualify for 100% FYAs in the same way as cars. Vans with non-zero CO₂ emissions (at any level) are allocated to the main pool where they will be eligible for writing down allowances at 18%.

There is also an additional benefit for the purchase of new vans purchased between 1 April 2021 and 31 March 2023, as these are eligible for the 130% super-deduction on new main rate plant and machinery. This super-deduction does not apply to cars or second-hand vans.

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?

Understanding the impact of VAT can play an important role in a company's decision on whether it should lease or purchase its company cars. As with tax relief, the impact of VAT for a company providing company cars to its employees 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?

Typically, 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

In most circumstances, and subject to its own ability to recover VAT (i.e., full or partial VAT recovery), a company is only able to recover all the VAT on lease rentals if the car is used entirely for business purposes.

In reality, few leased cars meet this requirement because most will have some element of private use. Therefore, there is a statutory 50% block in the VAT that would otherwise have been recovered. HMRC accepts that the 50% block on VAT reclaims for leased car payments only applies to the 'basic rental' element of the lease rental payments (i.e., not including any add-ons such as repair and maintenance).

The 50% block on VAT recovery only applies to leased cars and not vans. Therefore, VAT on the cost of van leases can be recovered in full. However, care should be taken in determining whether a vehicle is a car or van for VAT purposes. See the later chapter 'Understanding company van benefit' for more details.

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). You can find the HMRC guidance on the VAT treatment of these services on the following web pages:

- <https://www.gov.uk/guidance/vat-on-motoring-expenses-notice-70064>
- <https://www.gov.uk/guidance/vat-administrative-agreements-with-trade-bodies-notice-70057>

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 £600 and maintenance costs of £90 (both inclusive of VAT).

VAT recovery rate	100%
Lease rentals	
Rental (inc. VAT)	£600.00
VAT recovery	(£100.00)
50% blocked VAT	£50.00
Rental (after VAT recovery)	£550.00
Other expenses	
Maintenance (inc. VAT)	£90.00
VAT recovery	(£15.00)
Maintenance (after VAT recovery)	£75.00
Total VAT reclaim	(£65.00)
Total cost to business after VAT reclaim	£625.00

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 £600 and maintenance costs of £90 (both inclusive of VAT).

VAT recovery rate	5%
Lease rentals	
Rental (inc. VAT)	£600.00
VAT recovery	(£5.00)
50% blocked VAT	£2.50
Rental (after VAT recovery)	£597.50
Other expenses	
Maintenance (inc. VAT)	£90.00
VAT recovery	(£0.75)
Maintenance (after VAT recovery)	£89.25
Total VAT reclaim	(£3.25)
Total cost to business after VAT reclaim	£686.75

The monthly cost to the company in example 2, which is only able to reclaim 5% VAT, will be £61.75 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.

It is very difficult to get VAT recovery on purchased cars. However, VAT on the cost of purchased vans can typically be recovered in full where the vans are purchased for business use. But care should be taken in determining whether a vehicle is a car or van for VAT purposes. See the later chapter 'Understanding company van benefit' for more details.

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 non-cash 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 at their marginal rate based on the value of the BIKs they receive, and the employer will also pay NICs based on the BIK value.

For company cars, the BIK value is broadly calculated based on the list price of the car in question, multiplied by a percentage that is determined by its CO₂ emissions, fuel type and electric range. In this guide, for simplicity, we refer to the income tax paid on a company car BIK as Company Car Tax (CCT).

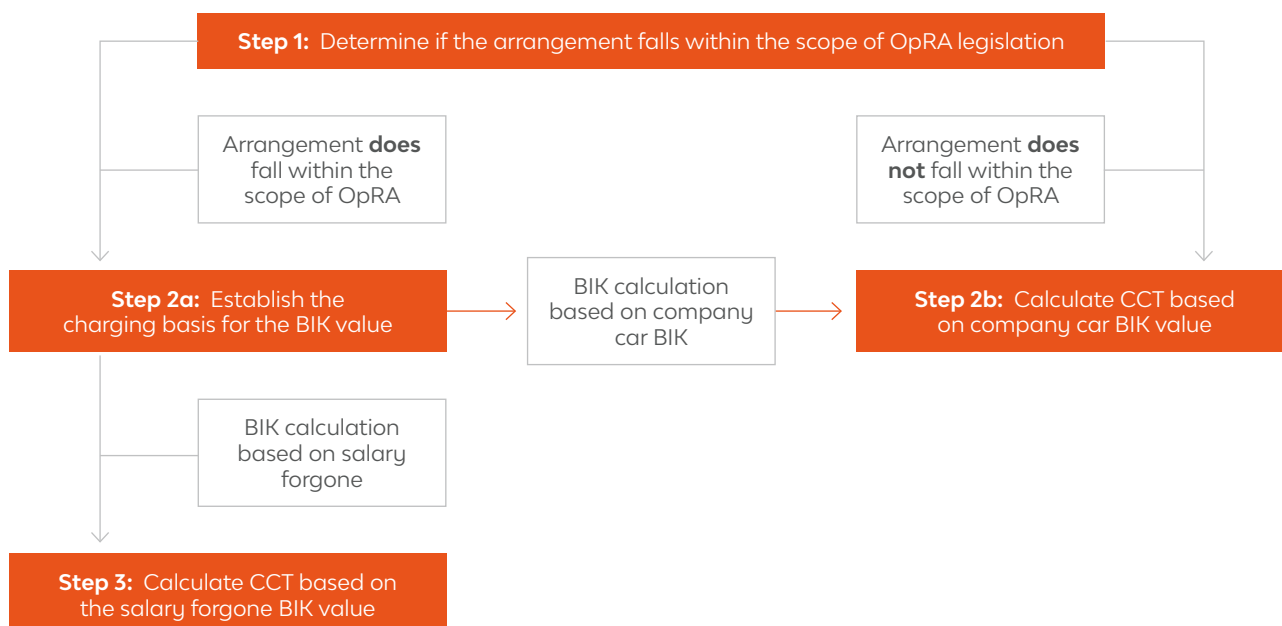
The rules for company cars are designed to encourage the selection of cars with lower CO₂ emissions because this will result in a lower BIK value and less CCT to pay (and the employer NICs cost will also be lower). However, this is an added layer of complexity with the Optional Remuneration Arrangement (OpRA) legislation that can make understanding CCT more complex and difficult for companies and their employees to understand.

It is worth noting that under CCT legislation, an employer can provide additional benefits in connection with the company car without incurring a further tax charge (if they meet certain conditions). As a result, it is possible for an employer to provide motor insurance, maintenance and other benefits associated with a company car, without triggering an additional BIK charge and further CCT and employer NICs costs.

Helping employees understand the financial implications of their choices 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, 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 the regime 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 most 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 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 types 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 CO₂ 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 CCT and employer NICs costs.

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 considered. It is important to note that checking to establish the charging basis 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. It is important to note that any trade down payments should be excluded from the value of the salary forgone because they are received by the employee and paid subject to income tax and NICs. However, any trade up payments should be ignored when calculating the amount of salary forgone. In a salary sacrifice scheme, the value of the salary sacrifice will be 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 CO₂ 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. 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 to the employee; 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 to arrive at the 'interim sum'	If an employee makes a capital contribution towards the cost of the car (or a qualifying accessory) this contribution reduces the value calculated in step 2 and the result is called the 'interim sum'. 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 CO₂ 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:**Payments 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 four examples, each of which include company cars with different CO₂ 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 £35,000 and all cars are registered on, or after, 6 April 2020.

Example 1: Battery Electric Vehicle (BEV) company car with CO₂ emissions of 0g/km

Tax year	2023/24	2024/25	2025/26	2026/27	Overall
Appropriate %	2%	2%	3%	4%	2.8%
BIK value	£700	£700	£1,050	£1,400	£3,850
CCT at 40%	£280	£280	£420	£560	£1,540

The average appropriate percentage over the lifetime of the company car would be 2.8%. The employee would pay a total of £1,540 in CCT which equates to an average monthly cost of £32.

Example 2: A Plug-In Hybrid Electric Vehicle (PHEV) with CO₂ emissions of 49g/km and an electric range of 41 miles

Tax year	2023/24	2024/25	2025/26	2026/27	Overall
Appropriate %	8%	8%	9%	10%	8.8%
BIK value	£2,800	£2,800	£3,150	£3,500	£12,250
CCT at 40%	£1,120	£1,120	£1,260	£1,400	£4,900

The average appropriate percentage over the lifetime of the company car would be 8.8%. The employee would pay a total of £4,900 in CCT which equates to an average monthly cost of £102.

Example 3: A diesel engine company car with CO₂ emissions of 115g/km (RDE 2 compliant)

Tax year	2023/24	2024/25	2025/26	2026/27	Overall
Appropriate %	28%	28%	29%	29%	28.5%
BIK value	£9,800	£9,800	£10,150	£10,150	£39,900
CCT at 40%	£3,920	£3,920	£4,060	£4,060	£15,960

The average appropriate percentage over the lifetime of the company car would be 28.5%. The employee would pay a total of £15,960 in CCT which equates to an average monthly cost of £333.

Example 4: A petrol engine company car with CO₂ emissions of 130g/km

Tax year	2023/24	2024/25	2025/26	2026/27	Overall
Appropriate %	31%	31%	32%	32%	31.5%
BIK value	£10,850	£10,850	£11,200	£11,200	£44,100
CCT at 40%	£4,340	£4,340	£4,480	£4,480	£17,640

The average appropriate percentage over the lifetime of the company car would be just under 28% and the employee would pay a total of £17,640 in CCT which equates to an average monthly cost of £368.

Observation:

The examples shown illustrate the extent to which vehicle selection can affect the cost of CCT for employees. Despite the list price of the car in all four examples being the same, the cost of company tax due varies by up to £16,100 over four years which equates to £335 per month.

The BEV offers the lowest BIK value, with potential CCT savings of 69% when compared to the PHEV, or 90% when compared to the lowest cost combustion engine vehicle.

It is important to remember that the company cost of employer NICs is also linked to the value of the BIK for cars selected by employees. Based on the current Class 1A NIC rate of 13.8%, the business would pay employer NICs of £531 for the BEV over four years, or £1,691 for the PHEV. In contrast, the cost of employer NICs for the diesel and petrol cars would be significantly higher, at £5,506 and £6,086 respectively.

These examples should help to demonstrate why 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 commonplace in car scheme arrangements for companies to structure arrangements so that they offer employees some flexibility to choose a benefit 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 capital contributions or Private Use Contributions (PUCs). It is important to note the appropriate tax treatment of employee contributions depends on the design of the car scheme policy and it is important to seek suitable advice in relation to the treatment that should apply.

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. The deduction is made for the year in which the contribution is made and all subsequent tax years the employee receives that car as a benefit. If the same car is transferred to another employee, the first employee's contributions are not taken into account when calculating the tax due on the company car for the second employee. Typically, the payment of capital contribution would be made at or about the time when the car or accessory was provided.

PUCs

If an employee makes contributions as a condition of the car being available for private use, the total amount of the PUCs 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.

It is important that the car scheme policy documentation is clear that such contributions are for the private use of the car. HMRC guidance states that in order for a contribution to be considered a private use contribution, it cannot be made for a reason other than for private use of that vehicle. In particular, HMRC guidance states that where a payment is made for “the use of a more expensive car”, these do not qualify as a private use payment unless certain conditions are met. In the calculation of a company car BIK, a PUC is subtracted at a different stage of the process than the capital contribution and this means that it can offer a greater level of income tax and NI efficiency.

A PUC is a more complex structure than a capital contribution and we would typically recommend seeking HMRC assurance about the proposed income tax and NICs treatment of employee contributions to be treated as a PUC when a new company car policy is implemented.

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.

The issue of dealing with trade down payments was not specifically covered in the OpRA legislation, however, typical market practice to date is where a comparison is made between the taxable value of the car selected and the cash allowance given up, this reflects the value of 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:

A capital contribution made against a car benefit calculated based on list price and CO₂ 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 CO₂ emissions the appropriate percentage for company car tax in 2023/24 would be 25%.
- The taxable benefit for the company car is £5,750 (£23,000 x 25%).
- The £2,000 capital contribution would result in income tax costs for the tax year being reduced by:
 - £200 for a higher rate taxpayer; or
 - £100 for a basic rate taxpayer.

Example 2:

PUC made against a car benefit calculated based on list price and CO₂ emissions

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 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 taxpayer (£600 x 40%); or
 - £120 for a basic rate taxpayer (£600 x 20%).

Example 3:

A capital contribution 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 £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 benefit (£25,000 x 25% = £6,250) 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 (25% x £2,000 = £500).
- The taxable benefit of the salary forgone is reduced by the value of the adjusted capital contribution and is £6,000 (£6,500 - £500).
- The £2,000 capital contribution would result in income tax costs in a year being reduced by:
 - £200 for a higher rate taxpayer; or
 - £100 for a basic rate taxpayer

Example 4:

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

Repeating example 2, 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 taxpayer (£600 x 40%); or
 - £120 for a basic rate taxpayer (£600 x 20%)

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 are not subject to the diesel surcharge for CCT.

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 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.

Further information:

HMRC guidance on the company car benefit rules and calculating the cash equivalent can be found here:

- Company car benefit rules: <https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim23000>
- Calculating the cash equivalent: <https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim24000>



Case study: Introduction of VED for electric vehicles

Introduction

Making the move to EVs and driving the uptake of the cleanest new vehicles is a key part of the road to net zero strategy published by the Department for Transport. To help achieve its ambitions and increase the uptake of EVs, the government introduced a range of financial incentives. Originally these incentives included grants for buying vehicles, low rates of company car tax, an exemption from VED, and grants for the installation of home charge points.

However, there are challenges for the government when balancing its ambition to boosting EV uptake with the cost of its incentives for the public finances. This cost pressure has already resulted in the reduction or removal of some of the EVs incentives, with the grants for buying EVs or installing charge points being removed or scaled back. In the Autumn Statement in 2022 it was announced that VED will be introduced for zero emission cars and vans from April 2025, thus removing another one of the EVs incentives previously available.

This case study is designed to explore the financial implications of the introduction of VED for BEVs and how it will affect the overall cost effectiveness of opting for a BEV as a company car.

Analysis & assumptions

In this case study the WLC was calculated for a sample of example cars from a job-need and perk population of drivers. The cars modelled included:

- A petrol or diesel car where the changes to VED would have no effect.
- A BEV with the cost of VED excluded to replicate the current exemption.
- A BEV with a cost of VED included to reflect the rules that will apply from April 2025.

All calculations were based on the following:

- The business pays the main rate of corporation tax and has no restriction on its VAT recovery.
- All cars are acquired in April 2023 and kept for a replacement cycle of 48 months.
- Fuel and electricity costs based on current prices at the time of writing the guide.
- The cost of business mileage was reimbursed using HMRC's AFRs for fuel and actual cost of electricity for the BEV (this is to avoid employees being out of pocket using the AER).
- Electricity costs were based on a 75%/25% split of home and public charging.

In addition, the calculations for job-need drivers were based on the following:

- The employee is a basic rate taxpayer driving 15,000 business and 5,000 private miles p/a.
- The BEV having a list price below £40,000 and no additional rate VED supplement.

In addition, the calculations for perk drivers were based on the following:

- The employee is a higher rate taxpayer driving 2,500 business and 7,500 private miles p/a.
- The BEV having a list price above £40,000 where the additional rate VED supplement applies.

Results

The following table shows the results of the analysis carried out.

Car description	Power train	List price	CO ₂	WLC	Saving £s	Saving %
Job-need (hatchback)	Petrol	£26,275	121	£31,803	-	-
	BEV (No VED cost)	£31,290	0	£28,185	£3,618	11%
	BEV (VED cost)	£31,300	0	£28,691	£3,112	10%
Perk (Exec. Saloon)	Petrol	£40,310	138	£33,427	-	-
	BEV (No VED cost)	£42,450	0	£29,189	£4,238	15%
	BEV (VED cost)	£42,460	0	£30,494	£2,933	10%

The results for the job-need analysis show that:

- The BEV eligible for the current VED exemption would offer a saving of £3,618 or 11% when compared to the petrol engine alternative modelled.
- However, with the introduction of the VED for BEVs:
 - The list price of the car will increase slightly to reflect cost of the first year VED.
 - The WLC of the BEV will also rise by £506 and so the saving of the BEV compared to the petrol car will drop to £3,112 or 10%.

The results for the perk analysis show that:

- The BEV eligible for the current VED exemption would offer a saving of £4,238 or 15% when compared to the petrol engine alternative modelled.
- However, with the introduction of the VED for BEVs:
 - The list price of the car will increase slightly to reflect cost of the first year VED.
 - The WLC of the BEV will also rise by £1,305 and so the saving of the BEV compared to the diesel car will drop to £2,933 or 10%.

Observation:

The results of the case study provide insight into the expected implications of introduction of VED on the financial business case for switching to BEVs.

A key finding from the case study is that the additional rate VED supplement for cars with a list price over £40,000 will have a material impact on the costs involved. At the time of writing, the additional VED supplement adds £355 p/a to the cost of VED starting after the first year. Over a 48-month replacement cycle, this would add at least £1,065 to the overall cost of VED (although this number is likely to be higher after accounting for inflation).

The results for the job-need cars show that the introduction of VED for BEVs will increase the WLC of funding these cars, and this will reduce the potential saving these vehicles offer when compared to petrol or diesel alternatives. However, the cost increase is relatively low meaning the saving offered by the BEV modelled would fall from 11% to 10%, which is unlikely to have a material impact on decision making.

The results for the perk cars follow a similar pattern, where the introduction of VED for BEVs will increase the WLC of funding these cars and reduce the potential savings compared to petrol or diesel alternatives. However, the additional rate VED supplement will increase the financial impact of VED being introduced, with the saving offered by the BEV modelled falling from 15% to 10%. It is worth noting that despite the more material increase in WLC for the BEV, it still offers a significant saving compared to the diesel engine alternative modelled.

The removal of the VED exemption for BEVs in April 2025 will see costs increase, with a more noticeable impact for any cars attracting the additional rate VED supplement. The change will remove one of the incentives used by the government to increase the uptake of EVs as part of its net zero strategy. However, at the same time, the Autumn Statement confirmed that arguably the biggest EV incentive in the form of low company car tax rates will remain in place until at April 2028, meaning these cars can still offer a cost-effective option.

Fuel & electricity

Employees undertaking business mileage in their company cars will result in fuel and electricity costs that need to be managed. Employers need to take care to ensure they understand the financial and administrative implications of different approaches to reimbursing business mileage costs.

Is the cost of business fuel and electricity important?

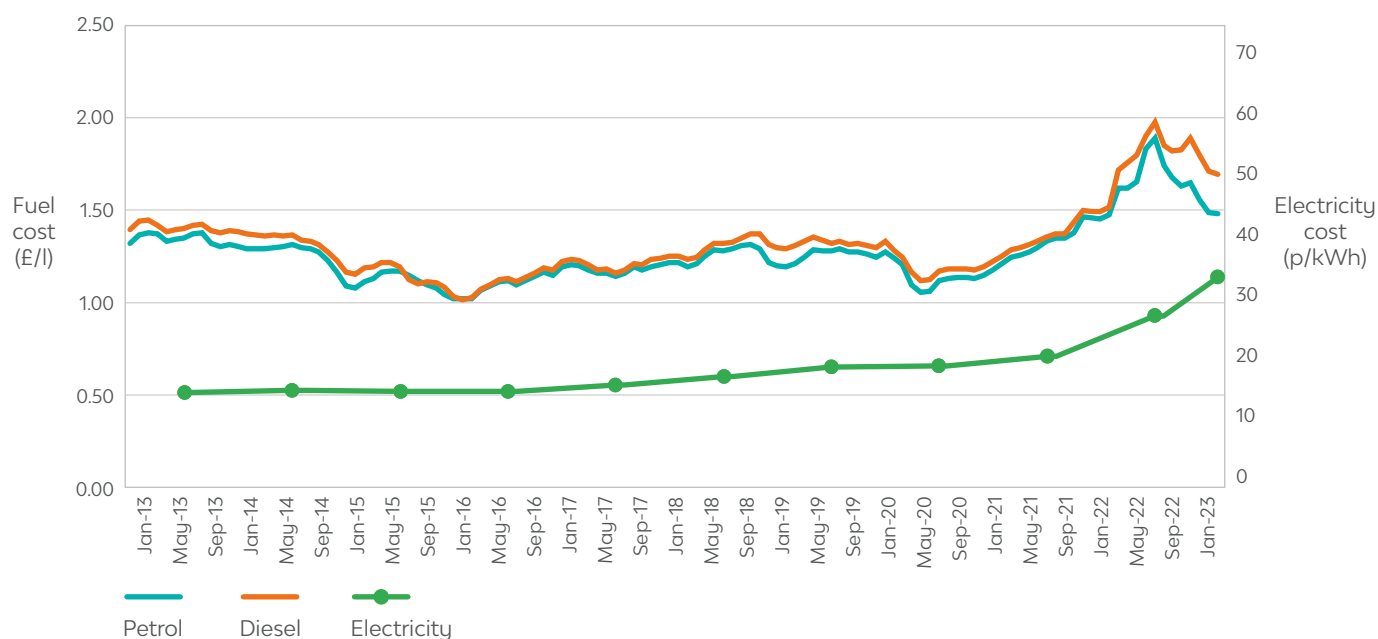
When employees undertake business mileage in a company or private car (for example, necessary attendance at a meeting or visiting customers) they will typically be reimbursed by their employer for the cost of the fuel or electricity used. The issue of business mileage reimbursement has become increasingly important in recent years due to the increased volatility of fuel and electricity prices and the resulting impact on companies and their employees.

Over the last 10 years, the price of both petrol and diesel has changed significantly as shown by the chart below. Between 2013 and 2020 the price at the pump fluctuated up and down by c.35% and 43% for petrol and diesel respectively. However, since 2020 there have been unprecedented rises in fuel costs with the price of petrol and diesel hitting record highs in 2022. The dramatic and rapid increases in the cost of fuel had a significant impact for businesses and their employees.

At the same time, the growth in the number of employees driving EVs has introduced a new layer of complexity to the issue of business mileage reimbursement. Initially, there were only a handful of employees with EVs, and relatively stable electricity prices meant reimbursement did not present too many material challenges. In recent years there has been significant growth in the number of employees driving an EV, with government figures showing that registrations of new BEVs and PHEVs increased by 1,726% and 329% respectively over a five-year period. The chart below shows that in the last five years energy prices have been rising. A steady increase started in 2017 but this became a much more significant rise in 2021 due to a global energy shortage. The problem of rising electricity prices became so acute the government felt the need to step in with the introduction of the Energy Price Guarantee in 2022 which put a limit on the price people pay for their energy.

Despite the price of petrol and diesel falling back somewhat, and the intervention in electricity prices from the government, managing the costs of business mileage reimbursement remains an important issue to consider.

UK fuel and electricity prices¹ (2013 - 2023)



¹ Fuel Source: www.gov.uk published by Department for Business, Energy & Industrial Strategy

Electricity Source: NimbleFins Average Cost of Electricity per kWh in the UK 2023 (2022 and 2023 data estimated based on energy price caps)

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

Broadly speaking, if an employee uses their own funds to pay for fuel used on business journeys in a company car there are two principal methods for calculating the amount of reimbursement the employee receives. These are:

- Adopting HMRC's advisory rates; or
- Reimbursing actual costs incurred.

The method chosen can have an impact on costs, cash flow and the level of administration required for both the company and its employees.

Adopting HMRC advisory rates

HMRC publish Advisory Fuel Rates (AFRs) and an Advisory Electric Rate (AER) to help employers calculate the amount of business mileage reimbursement for employees undertaking business journeys in a company. Many companies use advisory rates because this approach can be relatively simple to implement and administer. With the advisory rates, the employee reclaims the cost of business fuel or electricity based on an allowed rate per mile as published by HMRC. The rates are updated every quarter and they are intended to reflect fuel and electricity 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 or electricity used for private travel. If the reimbursement rate paid per mile of business travel is no higher than the advisory rates HMRC 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 current advisory rates published by HMRC can be found here: <https://www.gov.uk/guidance/advisory-fuel-rates>

Advisory Fuel Rate

The table below show the current AFRs published by HMRC:

Rates applicable from 1 March 2023

Engine size (cc)	Petrol – rate per mile	LPG – rate per mile
1,400cc or less	13p	10p
1,401cc or 2,000cc	15p	11p
Over 2,000cc	23p	17p
Engine size	Diesel – rate per mile	
1,600cc or less	13p	
1,601cc or 2,000cc	15p	
Over 2,000cc	20p	

The guidance published by HMRC confirms that hybrid cars should be treated as either petrol or diesel cars for the purposes of using the AFRs.

Advisory Electric Rates

The AER published by HMRC is for use where employees use a fully electric company car for business mileage. In March 2023 HMRC increased the AER from 8p to 9p per mile and now update this quarterly in line with the approach taken for AFRs (previously there was no commitment to update the AER on a regular basis).

The introduction of the AER 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 costs incurred

An alternative method of reimbursing employees who undertake business journeys in a company car is to reimburse for the actual costs incurred. To adopt an actual cost approach, a company will need to calculate the cost of fuel and electricity used based on the miles driven and the fuel or electricity consumption of the car driven. If a company can demonstrate that the reimbursement reflects the cost of fuel or electricity used and it does not provide any profit to employees, then the reimbursement may be higher than the advisory rates without triggering an income tax or NI 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.

When it comes to calculating and demonstrating the cost of fuel used for business mileage there are only a limited number of variables to consider and so this should not present too many challenges for employers to administer. In most cases, the price of fuel at the pump, the MPG of the car, and the amount of business and private mileage driven will be enough to identify and reimburse the cost of fuel used for business purposes so it can be reimbursed in line with HMRC guidance.

However, when it comes to the actual cost of electricity used this can be a much more complex issue to administer for a number of reasons. Firstly, employees can charge their car at home, in public, or at workplace charging facilities if they are available. The three options for charging will often have very different pricing with a much greater potential for variability than petrol station fuel prices. Secondly, if employees charge at home, it can be difficult for them to identify the electricity used for the car and the electricity used for their normal domestic supply. Finally, if employers make workplace charging available without cost for employees this means employees will not incur a cost for some of their charging. The tax rules allow for employers to reimburse employees where they have incurred a cost, but with if employees receive free charging it makes it harder to demonstrate where a cost has truly been incurred.

Let's look at some examples

To help illustrate the implications of adopting different approaches to business mileage reimbursement we have some examples showing the different financial and administrative considerations.

Example 1: Adopting HMRC AFRs

The following information will be used to calculate the amount of reimbursement to be paid.

- The fuel type for the car - petrol.
- The engine size - 1,498cc.
- The number of business miles travelled in the period - 300 miles.

Based on the HMRC AFRs published to apply from 1 March 2023, an employee driving a petrol engine car with an engine size of 1,498cc would be entitled to receive business mileage reimbursement at a rate of 15p per mile. The total business mileage reimbursement due is calculated by multiplying the total number of business miles claimed (300) by the applicable AFR (15p) which gives a reimbursement of £45.00.

Example 2: Adopting actual cost of fuel

The following information will be used to calculate the amount of reimbursement to be paid.

- The fuel type for the car - petrol.
- The fuel efficiency of the car - 44mpg.
- The cost of fuel - £1.55 p/l.
- The number of business miles travelled in the period - 300 miles.

If a car has a fuel efficiency of 44MPG it will use 0.0227 gallons of fuel for each mile driven (1 mile / 44 MPG). When converted to litres, this would equate to a fuel efficiency of 0.103 litres of fuel for each mile driven (0.0227 gallons x 4.546). If the cost of fuel is £1.47 per litre, then the cost of the fuel will be £0.15 per mile (0.103 litres x £1.55 per litre). The reimbursement due is therefore £45.56 (300 miles x £0.15 per mile).

Please note, the example above shows one option for calculating the actual cost of fuel used for business journeys. A business may decide to adopt an alternative calculation approach to suit its own requirements. Where a business decides to reimburse based on actual costs it should be comfortable that the chosen approach will offer a robust measure of costs incurred and it will be possible to evidence this to HMRC if required.

Observation:

In this example, the price of petrol fell steadily in the three months before HMRC updated the AFRs, meaning that the employee in example 1 was reimbursed an amount equal to the cost of fuel incurred. In periods of rapid price changes, employees reimbursed via AFRs can end up with a financial advantage or disadvantage. However, the reverse can also be true, and if fuel prices rose after HMRC published the AFRs then employees could be left out of pocket. In 2022, the dramatic and sustained rises in fuel prices meant that employees were financially disadvantaged where they were reimbursed based on HMRC AFRs and employers switched to reimburse based on actual costs to deal with the risk of an employee shortfall.

Example 3: Adopting the HMRC AER (assuming no free workplace charging provided)

The following information will be used to calculate the amount of reimbursement to be paid.

- The number of business miles travelled in the period – 300 miles.

Based on the HMRC AER published to apply from 1 March 2023, an employee driving a fully electric car would be entitled to receive business mileage reimbursement at a rate of 9p per mile. The total business mileage reimbursement due is calculated by multiplying the total number of business miles claimed (300) by the applicable AER (9p per mile) which gives a total reimbursement of £27.00.

Example 4: Adopting actual cost of electricity (assuming no free workplace charging provided)

To calculate the reimbursement the following information is needed:

- The cost of electricity used to charge the car for the period – £86.00. This is made up of:
 - 150 kWhs charged at home at a rate of 34p p/kWh costing £51.00.
 - 50 kWhs charged in public at a rate of 70p p/kWh costing £35.00.
- The total number of business and private miles driven in the period – 800 miles.
- The number of business miles travelled in the period – 300 miles.

If the total mileage driven is 800 miles and 300 of these are for business, then 38% of the overall mileage relates to business journeys (300 miles / 800 miles). If the cost of charging the car to cover 800 miles is £86.00 and 38% of the use is for business purposes, the cost actual cost of electricity used for the business journeys is £32.25 (£86.00 x 38%).

Please note, the example above shows one option for calculating the actual cost of electricity used for business journeys. A business may decide to adopt an alternative calculation approach to suit its own requirements. Where a business decides to reimburse based on actual costs it should be comfortable that the chosen approach will offer a robust measure of costs incurred and it will be possible to evidence this to HMRC if required.

Observation:

The examples above show that the different approaches to business mileage reimbursement can result in different payments despite covering the same distance, although with electricity the potential difference is significantly higher. In this example, if the employee was reimbursed for business mileage based on the AFRs they would receive £5.25 (19%) less than the actual cost of electricity incurred.

The examples highlight a key challenge for HMRC and employers when it comes to reimbursing electricity costs, and one that did not apply in the case of fuel. There can be significant variations in the efficiency for different electric cars, with the miles per kWh rating varying between 1 and 5 miles per kWh. In addition, the price of electricity can more than double depending on where the car is charged. The combination of these factors means that cost of electricity used could vary by more than 100% on each journey and this makes it extremely difficult to establish an appropriate pence per mile rate (or rates) for reimbursing electricity used for business mileage. Adopting a policy to reimburse based on actual costs can help to alleviate this issue, although it can result in increased levels of administration for employers to be able to demonstrate that have only reimbursed the costs incurred and no element of the payment would be deemed as earnings and subject to income tax and NI.

Can employees in a company car claim tax relief in relation to business mileage in a company car?

The illustrative examples in this section demonstrate that in some circumstances employees may be left out of pocket when it comes to claiming reimbursement for the costs, they incur on business journeys. This is especially relevant for employees driving a BEV because the difference between the AER and the actual cost can vary by up to 17p per mile depending on where the car is charged. While some companies manage this issue with changes to their policy, processes and systems so that employees are reimbursed for the full cost incurred, not all companies are able to do this leaving some employees out of pocket where they undertake business journeys in their company car.

The tax system does have a mechanism that can alleviate the issue and negative financial impact for employees, although it only replaces a portion of the financial shortfall. Where employees incur expenses from their employment that are not fully reimbursed by their employer, they may be entitled to claim tax relief from HMRC. A claim can include employees who incur costs undertaking business mileage in their company car that are not fully reimbursed by their employer. The section below provides an overview of the process for claiming tax relief in this situation, which is the same process as claiming relief on general expenses of employment. Please note, this should not be confused with Mileage Allowance Relief (MAR), which is only available where employees are reimbursed less than the AMAP rates for business travel in their privately owned car. MAR is detailed in the Cash Allowances chapter.

In essence, claiming tax relief allows employees to either pay less income tax or receive an income tax refund. Some forms

of tax relief are automatic, but others require an employee make a claim for from HMRC. Employees can claim tax relief at any point during the tax year (unless they file a tax return in which case relief should be claimed through the return filing process), although this is typically a process carried out at the end of the tax year when all the information required is available. Once a claim is made HMRC will usually make any adjustments needed through the employee's tax code or issue a refund of income tax paid.

HMRC guidance states that records need to be retained for evidencing valid business journeys and the costs incurred. Typically, this would involve recording the start and end location and the number of miles driven for each journey. The records kept may be requested by HMRC to support any claims for tax relief, so at a minimum these records should be kept for 22 months from the end of the tax year. With some expenses, a historic claim can be made if within 4 years of the end of the tax year in which the expenses were incurred.

Tax relief only compensates employees for the income tax due on their expenses rather than the full cost of the expense incurred and it only applies to the element of the expense not reimbursed by the company. This means that if a company reimburses for business mileage, but the rate is below the actual cost incurred, employees can only claim tax relief for the difference. The tax relief applies at the employee's marginal tax rate, and so a higher rate taxpayer paying 40% income tax will only receive 40% of their expense costs in tax relief in a successful claim. Employees may wish to consider the level of administration involved with making a claim against the value of any tax relief to decide whether it is worth the time and effort.

Let's look at an example

To help illustrate the financial implications of claiming tax relief we have an example showing value to an employee of making a claim.

Example 1: Employee travelling 10,000 business miles a year

An employee driving a BEV who is reimbursed for business mileage at the HMRC AER of 9p per mile. The employee has a 50%/50% split between home and public charging and the car has an efficiency rating of 3.5 mi/kWh.

- The employee claims business mileage reimbursement from the company at 8p per mile giving an overall reimbursement of £900 (10,000 miles x 9p per mile).
- The actual cost of electricity incurred is £1,485.71. This is calculated as follows:
 - £485.71 for charging at home (5,000 miles / 3.5 mi/kWh = 1,428.5 kWhs multiplied by 34p/kWh)
 - £1,000 for charging in public (5,000 miles / 3.5 mi/kWh = 1,428.5 kWhs multiplied by 70p/kWh)
- Therefore, the employee would have spent £585.71 more on the electricity used for business journeys than they received in reimbursement (£1,485.71 - £900).
- The employee could submit a claim for tax relief for the shortfall.
- If the employee is:
 - A higher rate taxpayer with a marginal tax rate of 40%, the value of the claim would be £234.29 (£585.71 x 40%).
 - A basic rate taxpayer with a marginal tax rate of 20%, the value of the claim would be £117.14 (£585.71 x 20%).

Observation:

The example above shows that if an employee is not fully reimbursed by their employer for the costs incurred for undertaking business mileage, they can reduce the financial impact by making a claim for tax relief. The tax relief claim does not completely resolve the issue, and so employee will still be out of pocket. The value of the is heavily influenced by the employee's marginal tax rate, with a higher rate taxpayer seeing a more beneficial outcome. An employee will want to weigh up the administration involved with the claim against the expected value it can deliver.

What happens if employees use a fuel or electricity card to pay for fuel and electricity they use?

Some companies use a fuel or electricity card as a mechanism to pay for and reimburse business mileage. In this situation, the fuel or electricity is paid for by means of a company card where the employee charges the cost to the card and the bill is then paid by the company. The employee will then have to submit records to allow the company to distinguish between the costs relating to business journeys and those for private mileage, with the employee meeting the cost of private mileage.

There are a number of reasons for using fuel or electricity cards, such as the bulk buying power providing discounts, cash flow benefits for the employee, or simply ease of use. Using a company card can also make it easier to adopt an actual cost basis for reimbursement, because all the costs are usually tracked in one place. However, there is a certain level of administration that is necessary to establish the business and private costs and ensure employees only receive reimbursement for business mileage. If this cannot be demonstrated, then a car fuel benefit charge is likely to apply for any employees provided with fuel for private motoring and this can have significant cost implications for both the company and the employee.

What happens if a company funds private fuel or electricity?

In some cases, a company may choose to meet the costs of fuel or electricity used by its employees for private journeys. Typically, this is done using a company fuel or electricity card as a payment mechanism, although it is possible for an employer to reimburse its employees for the costs they incur. One of the key benefits of funding private journeys is that it removes the need for the business to keep mileage records to identify the split of business and private journeys because the company simply pays for everything. This can reduce administration and remove the need for systems to record and retain business mileage data. 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 electricity, and they do not have to keep any mileage records. While there are benefits, it is important to note that there can be significant financial implications for a company and its employees in relation to fuel or electricity provided for private journeys.

If a company decides to meet the cost of fuel used for private journeys it will incur the cost for the fuel purchased and there will also be VAT implications to consider. In addition, the provision of fuel for private journeys will trigger a car fuel benefit charge resulting in an employer NICs liability and statutory reporting requirements. If an employee is provided with fuel for private journeys, they will have to pay income tax on the value of the car fuel benefit charge. The charge is calculated based on the fuel type and CO₂ emissions of the car, as well as car fuel benefit multiplier set by the government. When the company and employee costs are all considered, the provision of private fuel can be an expensive benefit, and in some cases could leave employees financially disadvantaged.

If a company decides to meet the cost of electricity used for private journeys this can offer similar benefits to fuel, with reduced requirements for tracking employee journeys and managing business mileage reimbursement. The company will incur the cost of electricity provided and there will also be VAT implications to consider. However, there is no equivalent to the car fuel benefit charge for electricity in current tax legislation, and so the treatment and financial implications of a company providing electricity for private journeys are very different. Based on current HMRC guidance, a benefit charge will not be triggered where the company provides electricity from workplace or public charging facilities regardless of whether it is for business or private journeys. However, if an employee is reimbursed for electricity at home and this is used for private journeys the reimbursement should be treated as earnings and subject to income tax and NI.

The costs and tax treatment involved with fuel or electricity provided for private journeys can be very different, leading to very different outcomes for a company and its employees. Therefore, it is important companies understand the potential implications of providing private fuel or electricity before providing these benefits.

Let’s look at some examples

To help illustrate the implications of providing fuel or electricity for private motoring with a company car we have produced illustrative examples showing the cost implications for the company and employees. Please note, for simplicity, the examples exclude the impact of any fuel or electricity purchased for business use.

Example 1: Private fuel provided for an employee travelling 5,000 private miles each year

A higher rate taxpayer receives private fuel and drives a typical 4 door petrol engine company car with CO₂ emissions of 125g/km and a fuel consumption of 35MPG. The assumed cost of petrol for this example is £1.55 p/l.

The results are as follows:

Company perspective

The cost to the company of funding fuel for private journeys is:

Cost of private fuel purchased	£1,007
VAT recovery on fuel	(£168)
VAT fuel scale charge ¹	£192
Employer's NI on car fuel benefit	£1,151
Total cost (2023/24 tax year)	£2,182

Employee perspective

The employee cost associated with receiving a car fuel benefit is:

Car fuel benefit multiplier	£27,800
Appropriate percentage	30%
Taxable benefit	£8,340
Income tax paid at 40% (2023/24 tax year)	£3,336

¹ The VAT fuel scale charge for 2023/24 was not published at the time of writing this guide. The figure shown is based on the 2022/23 values with an inflationary increase applied for 2023/24.

Observation:

The employee would have paid £3,336 in income tax to receive a car fuel benefit where the value of the fuel provided by the employer would have been £1,007. Therefore, the employee would have saved £2,329 if they had personally purchased the private fuel themselves. The cost to the company of providing the car fuel benefit, which would have left the employee £2,329 out of pocket, would have been £2,182.

Example 2: Private fuel provided for an employee travelling 20,000 private miles each year

A basic rate taxpayer receives private fuel and drives a typical 4 door diesel engine company car with CO₂ emissions of 110g/km and a fuel consumption of 45 MPG. The assumed cost of diesel for this example is £1.75 p/l.

The results are as follows:

Company perspective		Employee perspective	
The cost to the company of funding fuel for private journeys is:		The employee cost associated with receiving a car fuel benefit is:	
Cost of private fuel purchased	£3,536	Car fuel benefit multiplier	£27,800
VAT recovery on fuel	(£589)	Appropriate percentage	27%
VAT fuel scale charge ¹	£127	Taxable benefit	£7,506
Employer's NI on car fuel benefit	£1,036	Income tax paid at 20% (2023/24 tax year)	£1,501
Total cost (2023/24 tax year)	£4,111		

¹ The VAT fuel scale charge for 2023/24 was not published at the time of writing this guide. The figure shown is based on the 2022/23 values with an inflationary increase applied for 2023/24.

Observation:

The employee would have paid £1,501 in income tax to receive a car fuel benefit where the value of the fuel provided by the employer would have been £3,536. It is evident that where an employee undertakes substantial levels private mileage, they can receive a financial advantage if the income tax paid on the car fuel benefit is less than the cost they would have incurred if they purchased the private fuel themselves. In this example the employee would have received a financial benefit of £2,035. However, it is important to note that the company would incur a significant cost associated with the provision of private fuel and the associated employer NICs liability (£4,111). In some circumstances, it may be more cost effective for an employer to look at alternative options for structuring the provision of private fuel to deliver cost efficiencies, but this would need to be carefully considered so that it is aligned with HMRC rules and guidance.

Example 3: Private electricity provided for an employee travelling 5,000 private miles each year

A higher rate taxpayer is reimbursed for the cost of electricity for private journeys for a BEV with an efficiency of 4 mi/kWh. The charging takes place at the employee's home with a rate of 35p/kWh.

The results are as follows:

Company perspective

The cost to the company of funding electricity for private journeys is:

Cost of private electricity reimbursed	£438
Employer NICs on electricity reimbursement ¹	£63
Total cost (2023/24 tax year)	£500

Employee perspective

The employee cost associated with being reimbursed for electricity for private journeys is:

Reimbursement for private electricity	£438
Income tax paid at 40%	£175
Employee NI paid at 2%	£9
Total employee cost (2023/24 tax year)	£184

Example 4: Private electricity provided for an employee travelling 20,000 private miles each year

A basic rate taxpayer is reimbursed for the cost of electricity for private journeys for a BEV with an efficiency of 4 m/kWh. The charging takes place at the employee's home with a rate of 35p/kWh.

The results are as follows:

Company perspective

The cost to the company of funding electricity for private journeys is:

Cost of private electricity reimbursed	£1,750
Employer NICs on electricity reimbursement ¹	£250
Total cost (2023/24 tax year)	£2,000

Employee perspective

The employee cost associated with being reimbursed for electricity for private journeys is:

Reimbursement for private electricity	£1,750
Income tax paid at 20%	£350
Employee NI paid at 12%	£210
Total employee cost (2023/24 tax year)	£560

¹If an employee charges their car at home and is reimbursed for electricity for private journeys the reimbursement is taxable as earnings. This will be subject to Class 1 NICs and attract the apprenticeship levy.

What other considerations are there for fuel reimbursement?

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

Q. Can a business recover VAT on the cost of business fuel or electricity 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 typically 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.

Based on HMRC's view at the time of writing (see guidance in section 8 [here](#) and [Revenue and Customs Brief 1 \(2022\)](#)), if employees charge an electric vehicle (which is used for business journeys) at home, the company cannot recover the VAT on the cost of the electricity. This is because HMRC's view is that the supply is made to the employee and not to the business. If the electric vehicle is charged at a public charge point, HMRC's view is that the supply is made to the company or employer, and it should be possible to recover VAT on the business element only subject to keeping detailed mileage records (to calculate business vs private use) and normal input tax recovery rules. In an earlier brief (see [here](#)), HMRC set out its view that a company can recover the VAT on electricity in full in respect of workplace charging (subject to normal input tax recovery rules and keeping business vs private mileage records), but this might be subject to an output tax adjustment if there is any private use. Alternatively, the company can recover the VAT on the business element only in this scenario (subject to normal input tax recovery rules). However, HMRC's guidance specifically refers to "employer's electric vehicle". It's not immediately clear why there is a reference to employer's electric vehicles and if HMRC view this as different to the VAT recovery position for an employee's electric vehicle being charged at the workplace.

Q. Can a business recover VAT on the cost of private fuel or electricity 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 CO₂ emissions of the car. The higher the CO₂ output of the car, the greater the VAT fuel scale charge.

Based on HMRC guidance at the time of writing, a company should not be entitled to VAT recovery in respect of electricity used by its employees for private journeys when the electric vehicle is charged at home or in a public place. If the electric vehicle is charged at a workplace, it might be possible for the employer to recover the VAT in full (see HMRC's view [here](#)), but this would be subject to an output tax adjustment if there is any private use.

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, the start and end 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.

In January 2022, HMRC announced they are considering the situation where an employee is reimbursed by the employer for the actual cost of electricity used in charging an electric vehicle for business purposes. This is to determine what evidence can be provided, to allow the employer to claim the related VAT (subject to normal input tax recovery rules). At the point of publication for this guide, no further information has been provided by HMRC in relation to this. The HMRC announcement can be found [here](#): [Revenue and Customs Brief 1 \(2022\): reviewing how to claim VAT when charging electric vehicles for business purposes - GOV.UK \(www.gov.uk\)](#)

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?

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.

For the first tax year in which a car is registered, a first year VED rate applies and is based on the CO₂ emissions of the car and whether the RDE standard is met (for diesel vehicles). For subsequent years a flat standard rate applies which is not related to CO₂ emissions or RDE2. There is also an additional rate supplement that applies to the standard rate for five years starting from the first year that the standard rate applies. The additional rate (£355 from 1 April 2022) is due on cars with a list price exceeding £40,000 at the point of first registration. There is also a £10 discount applies to all first year and standard VED rates for 'alternative fuel vehicles', which includes hybrids, bioethanol and liquid petroleum gas vehicles.

The table below shows the current VED rates that apply from 1 April 2022.

2022/23 Vehicle Excise Duty rates for cars registered from 1 April 2017

CO ₂ emissions (g/km)	First year rates			Standard rates (applies after first year)	
	Petrol/diesel car ¹ (tax class 48 and 49)	Diesel car ² (tax class 49)	Alternative fuel car (tax class 59)	Standard rate ³ (exc. additional rate ⁴)	Standard rate ³ (inc. additional rate ⁴)
0	£0	£0	£0	£0	£0
Jan-50	£10	£25	£0	£165	£520
51-75	£25	£120	£15		
76-90	£120	£150	£110		
91-100	£150	£170	£140		
101-110	£170	£190	£160		
111-130	£190	£230	£180		
131-150	£230	£585	£220		
151-170	£585	£945	£575		
171-190	£945	£1,420	£935		
191-225	£1,420	£2,015	£1,410		
226-255	£2,015	£2,365	£2,005		
Over 255	£2,365	£2,365	£2,355		

¹ Diesel cars tested to RDE2 standards.

² Diesel cars tested to RDE only standards.

³ A £10 discount applies to all VED rates for 'alternative fuel vehicles', which includes hybrids, bioethanol and liquid petroleum gas vehicles.

⁴ Cars with a list price over £40,000 at first registration will pay the additional rate of £355 for 5 years starting after the first year.

Future VED rules

In the Autumn Statement (November 2022) the government announced the introduction of VED for zero emission cars, vans, and motorcycles to take effect from 2025. The objective of the changes announced will be to ensure all drivers begin to pay a fairer tax contribution into the motoring tax system. Currently, electric vehicles, which do not currently pay VED, and AFVs and hybrids, which pay a discounted rate, pay less than petrol and diesel vehicles. The measures will equalise the VED treatment of all zero emission and ICE vehicles from April 2025 and will apply to both new and existing vehicles.

The changes announced were:

- New zero emission cars registered on or after 1 April 2025 will be subject to the lowest first year rate of VED (currently £10 per year). From the second year of registration onwards, they will move to the standard rate (currently £165 per year).
- Zero emission cars registered between 1 April 2017 and 31 March 2025 will also become subject to the standard rate.
- The expensive car supplement exemption for electric vehicles is due to end in 2025. New zero emission cars registered on or after 1 April 2025 will therefore be liable for the expensive car supplement (currently £355). The expensive car supplement currently applies to cars with a list price exceeding £40,000 for five years.
- Rates for Alternative Fuel Vehicles and hybrids will also be equalised.
- Zero emission vans will move to the rate for petrol and diesel light goods vehicles, currently £290 a year for most vans.

Further information:

- Government guidance on Vehicle Excise Duty can be found here - <https://www.gov.uk/vehicle-tax-rate-tables>
- The current VED rates published by the DVLA can be found here - https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1062988/v149-rates-of-vehicle-tax-from-1-april-2022-for-cars-motorcycles-light-goods-vehicles-and-private-light-goods-vehicles.pdf
- The policy paper for the introduction of VED for electric vehicles can be found here - [Introduction of Vehicle Excise Duty for zero emission cars, vans and motorcycles from 2025 - GOV.UK \(www.gov.uk\)](#)

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 filed 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 simpler;
- A small initial cost;
- No exposure to residual value risk;
- 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”, and 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 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 that 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 simpler;
- 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 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 license 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	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? ¹	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 optional maintenance?	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 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.

Electric Vehicles

Low Company Car Tax bands for electric and some plug-in hybrid electric vehicles (PHEVs), has signalled clear support for the government's 'Road to Zero' objective and stimulated fleet demand. 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

With almost 200 plug-in hybrid (PHEVs) and electric cars (EVs) available to buy or lease in the UK, they have become an increasingly viable and popular alternative to petrol and diesel vehicles (often referred to together as ICE – internal combustion engine). According to the SMMT, passenger cars registered in 2022 were more than twice as likely to be a plug-in (22.8% share) than a diesel (9.6% share) and, although the choice of electric vans is more restricted, 5.9% of LCV registrations last year. As of September 2022, there were 919,505 plug-in cars and 41,881 plug-in vans on the road (source: DfT), and that share is expected to continue growing in the coming years.

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, and means new cars and vans must be zero-CO₂ at the tailpipe to be sold from 2035. Manufacturers will also face mandatory EV targets from 2024, as a percentage of their UK sales, supported by a £1 billion investment in rapid chargers, so that no driver will be more than 30 miles from one.

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 furthering 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 for drivers choosing EVs, such as the 2% benefit in kind tax which is frozen until April 2025 and will remain low for a further three years. 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 22,355 charging locations, and 37,851 charging devices connectors in January 2023 – that's a 31% year-on-year increase. So, it's no longer a matter of range anxiety – but that of 'change anxiety'.

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.

Therefore, a whole life cost (WLC) perspective is absolutely essential. This goes beyond the 'ticket' or list price of the vehicle (which is typically higher for an EV) and takes other factors into account, such as taxes, subsidies, fuel and electricity use, repair, maintenance and tyres and length of usership or ownership. LeasePlan's Car Cost Index revealed that the low in-life costs for EVs compensate for their higher initial investment versus an ICE model, and means they are competitive on a WLC basis in most segments – if not cheaper. This means purchasing decisions can take the wider benefits into account.

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. Electric vehicles can also offer reduced Class 1A NICs if they are available through a salary sacrifice scheme.

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 Podcast podbean.com

Explore: EV Tools and Insights leaseplan.com

Good to know: GreenFleet 2022 'Leasing Company of the year'

Access to vehicle charging

A key element of the transition to electric vehicles will be ensuring convenient and cost-effective access to vehicle charging facilities.

Since the introduction of low CCT rates for EVs there has been a significant increase in the number of employees opting for these vehicles. The Autumn Statement confirmed that the low rates of CCT will remain in place until 2028 and this is likely to provide a longer-term incentive for more employees to make the switch. While there can be a strong financial business case for making the move to an EV, there may be some challenges still to overcome in terms of day-to-day practicality. One aspect of EV use that is likely to influence take up is the ease of access to vehicle charging infrastructure, with work still to do to make EV charging as quick and easy and a visit to the petrol station. This section explores the considerations for companies and their employees when it comes to access to charging for EVs.

What are the options for vehicle charging?

Broadly speaking, access to charging for EVs can be broken down into the following three types of location:

1. Residential charging.
2. Public charging (including on the go and destination charging).
3. Workplace charging.

The speed of charging an EV at these locations depends on the power of the charge point and the battery capacity of the car. The power of a charge point is measured in kilowatts (kW) and typically fall into the following categories:

Category	Power output
Slow	Up to 5kW
Fast	7-22kW
Rapid	25-99kW
Ultra-Rapid	100kW+

To calculate roughly how long it will take to charge an EV, you can use the following calculation:

Battery capacity (kWh) ÷ Charger power (kW) = Charging time (hours)

While the calculation above will give a broad view, there may be other factors affecting charging times. For example, charging speed can be affected by the car's onboard charger, and the car's management system may vary the speed of charging to extend the life of the battery. Another point to consider when it comes to public charging is that the speed of charging will often have a direct impact on costs, with the price of electricity usually increasing as the charger power and speed increases.

It is important for companies and their employees to understand the different charging options and the implications they have for cost and convenience. This will help employers in building a cohesive car scheme policy designed to enable access to charging and support the move to EVs.

What are the key attributes of the charging options?

Residential charging

The most basic approach to charging is for employees to plug the car into the residential mains electricity supply using a charge lead with a 3-pin plug connection. This will usually have a power output of 2-3kW (Slow) and add c.6-8 miles of range every hour. However, employees may need to check their car comes with an appropriate 3-pin mains charge lead for this option, because not all cars come with this type of lead as standard, and it can be an expensive accessory to buy.

Alternatively, employees can install a home charge point and these usually have a power output of 7kw (Fast) that can add c.30 miles of range every hour. At this charging speed, employees should be able to fully charge most EVs in 8-10 hours, which means drivers can access the maximum electric range for the car on a daily basis.

Where employees on high business mileage fleets make the switch to an EV there may be a greater need for them to install a home charge point. This may be necessary to make it practical for them to charge and use their car's full electric range daily to do their job and minimise the need for more expensive public charging. In this situation employers may wish to consider their car scheme policy to decide whether the cost of installing a home charge point should rest with the employee, or be part of the car scheme offering. In addition to increasing the ease of use for an EV, another valuable benefit of installing a home charge point is that they will typically provide employees with robust and accurate information on electricity usage and costs to support business mileage reimbursement claims.

The cost of charging an EV at home will vary depend on the residential energy tariff in question and the efficiency of the car. Assuming a price of 34p/kWh, which is the rate in the government's energy price guarantee, and an EV that travels 3 miles/kWh, the cost of charging at home would be in the region of 11p/mile. Except for free charging at the workplace or in some public areas, residential charging is likely to offer the lowest cost option for EV charging and so encouraging the use of home charging where possible can reduce company and employee costs.

Public Charging

The speed of public charge points can vary significantly depending on the infrastructure available. The power output can start at 3-6kW (Slow); with most charge points offering 7kW-22kW (Fast); some able to output 25-99kW (Rapid); and a small number of charge points offering charging at 100kW+ (Ultra-rapid).

The cost of using public charge points can vary significantly, but in most cases, it is likely to be a more expensive option compared to home charging. It may be possible for employees to find some free public charge points, but these tend to be Slow chargers and may not be the most convenient to use. Employees should expect to pay for electricity from Fast, Rapid and Ultra-rapid chargers with the price of electricity usually linked to the speed of charging, with the fastest chargers having the highest electricity prices. Depending on location type of charge, the average price for public charging is likely to be c.45p p/kWh for Slow and Fast chargers, with a higher price of c.70p/kWh for the rapid and ultra-rapid chargers. Using an average efficiency EV, this would equate to 13p/mile and 20p/mile respectively.

Workplace charging

Employers considering the installation of workplace charging will need to take account the capacity of the power grid at work and the expected demand for charging before installing facilities. If it is practical and cost effective, opting for 7kW (Fast) chargers instead of slower 3kW chargers can significantly increase the capacity for charging EVs at a work.

Where an employer provides workplace charging it is common practice that the facilities and electricity are provided free of charge. Workplace charging is usually made available to employees, but sometimes extends to customers and visitors as well. Some employers do charge for the cost of electricity provided from workplace charging, but this requires charge points that can record and assign usage to a particular driver. Regardless of the approach taken to charging, it may be sensible for employers to include a fair use policy to clearly set out appropriate employee behaviours, and to avoid employees incurring significant electricity costs.

HMRC guidance

HMRC published guidance setting out the expected tax treatment to apply for the provision of access to charging facilities and electricity (Please see EIM23900 for the full HMRC guidance). The following table provides a summary of the key scenarios covered.

Location	Scenario	Type of mileage	Company car	Private car
Residential	Employer pays for a vehicle charging point to be installed at the employee's home	n/a	No taxable benefit	Taxable benefit ¹
	Employee charges car at home: their employer reimburses the electricity costs incurred	Business use only	No taxable benefit (up to AER or actual cost)	No taxable benefit (up to AMAP rates)
		Mixed business and private use	Reimbursement is taxed as earnings ¹ Employee entitled to a deduction for the cost of business miles travelled	Reimbursement is taxed as earnings ¹ Employee entitled to AMAPs/MAR for business mileage travelled
		Private use only	Reimbursement is taxed as earnings ¹	Reimbursement is taxed as earnings ¹
Public	Employee charges car in public: their employer reimburses the electricity costs incurred	Currently, there is no published HMRC guidance covering this scenario		
Workplace	Employer allows cars to be recharged from a vehicle charging point at work	Any	No taxable benefit	No taxable benefit ²

¹ Taxable value based on the cost to the employer

² Applies since 6 April 2018 and is subject to the conditions set out in the HMRC guidance EIM01035

The HMRC guidance was first published several years ago and since then there have been new technology and product developments changing the way companies and employees use and charge their EVs. As a result, the guidance does not cover all the scenarios that are likely to be seen in practice at this point in time. This can be challenging for companies wanting to design and operate robust EVs charging policies that are aligned to HMRC rules and guidance.

Case study: The importance of adopting Whole Life Cost (WLC)

Introduction

When it comes to managing a company car fleet it is important to make decisions based on detailed and accurate information. Understanding the true cost of providing company cars to set appropriate entitlement levels and vehicle choice lists can be a tricky process. Getting this wrong can result in undesirable cost implications for a company and its employees.

The cost of funding car scheme arrangements will include a range of costs that can be relatively easy to identify and measure. For example, lease payments, maintenance and motor insurance are some of the more obvious costs a company will incur. Information about these costs is usually available on invoices or supplier reporting, and so they are usually relatively easy to identify and assess.

However, there will also be a range of costs involved with car schemes that are less visible or obvious, making them much harder to manage. For example, employer NICs, mileage reimbursement, VAT recovery, corporation tax and future rule changes can all have a material impact on the overall cost of funding car scheme arrangements. These costs will flow through a range of different payroll and expenses systems or through company accounts, and so it can be much harder to robustly identify and measure their impact.

To address this, employers may wish to consider adopting a Whole Life Cost (WLC) approach to managing car scheme arrangements. A WLC approach captures all direct and indirect costs associated with funding and using a car over its expected lifetime. It includes the more visible and obvious costs, but it also takes account of the less visible costs too and can give companies a much more robust picture on the costs involved with funding car scheme arrangements.

This case study is designed to explore the moving parts involved with WLC calculations and to demonstrate the additional financial insight that this approach can deliver.

Analysis & assumptions

In this case study the WLC was calculated for a selection of example cars from a job-need and perk population of drivers. The cars modelled included a range of power trains and price points.

All calculations were based on the following:

- The business pays the main rate of corporation tax and has no restriction on its VAT recovery.
- All cars are acquired in April 2023 and kept for a replacement cycle of 48 months.
- Fuel and electricity costs based on current prices at the time of writing the guide.
- Electricity costs were based on a 75%/25% split of home and public charging.

In addition, the calculations for job-need drivers were based on the following:

- The employee is a basic rate taxpayer driving 15,000 business and 5,000 private miles p/a.
- The cars modelled were:
 - ICE - a petrol engine car with CO₂ emissions of 122g/km.
 - PHEV - a petrol plug-in hybrid car with CO₂ emissions of 23g/km, and an electric range of 37 miles.
 - BEV - a fully electric car.

In addition, the calculations for perk drivers were based on the following:

- The employee is a higher rate taxpayer driving 2,500 business and 7,500 private miles p/a.
- The cars modelled used were:
 - ICE - a diesel engine car with CO₂ emissions of 129g/km.
 - PHEV - a petrol plug-in hybrid car with CO₂ emissions of 31g/km, and an electric range of 41 miles.
 - BEV - a fully electric car.

Results

The following table shows the result for the job-need cars modelled.

	ICE	PHEV	BEV
List price	£28,175	£33,535	£31,745
Obvious Costs			
Lease Rentals	£26,772	£27,481	£28,635
Maintenance	£4,953	£6,249	£4,924
Motor Insurance	£3,000	£3,000	£3,000
Sub-total	£34,725	£36,730	£36,559
Less Obvious Costs			
VAT Recovery	(£4,457)	(£5,032)	(£3,207)
Corporation Tax Relief	(£10,814)	(£11,065)	(£10,258)
Leasing disallowance	£920	£0	£0
Employer NICs on car benefit	£4,588	£2,360	£482
Business mileage reimbursement	£8,400	£10,200	£7,200
Sub-total	(£1,363)	(£3,537)	(£5,783)
WLC (48 months)	£33,362	£33,193	£30,776

The results show:

- If you only consider the obvious costs the ICE car modelled is the most cost-effective option. On this basis, opting for the ICE is forecast to save £1,834 (or 5%) when compared to the BEV which is next best option.
- However, taking account of the less obvious costs changes the picture, with the overall costs for all the cars falling when factoring in the VAT recovery and corporation tax relief.
- Bringing the less obvious costs into consideration has the biggest impact for the BEV, with noticeable differences in the cost of employer NICs, business mileage reimbursement and leasing disallowance between the cars modelled.
- The overall cost of funding the BEV falls by £5,783, or 16%, when the less obvious costs are included in the calculation. In contrast, the overall cost for the ICE only falls by 4%.
- When comparing the employer costs of funding the cars modelled on a WLC basis the BEV is the most cost-effective option. On this basis, opting for the BEV is forecast to save £2,586 (or 8%) when compared to the ICE alternative.

53. Case study: The importance of adopting Whole Life Cost (WLC)

The following table shows the result for the perk cars modelled.

	ICE	PHEV	BEV
List price	£41,615	£44,710	£49,750
Obvious Costs			
Lease Rentals	£37,584	£39,347	£40,667
Maintenance	£4,392	£4,267	£3,634
Motor Insurance	£3,000	£3,000	£3,000
Sub-total	£44,976	£46,614	£47,301
Less Obvious Costs			
VAT Recovery	(£4,147)	(£4,273)	(£3,995)
Corporation Tax Relief	(£12,613)	(£11,550)	(£11,440)
Leasing disallowance	£1,292	£0	£0
Employer NICs on car benefit	£7,925	£2,159	£755
Business mileage reimbursement	£1,700	£1,700	£1,700
Sub-total	(£5,843)	(£11,964)	(£12,980)
WLC (48 months)	£39,133	£34,650	£34,321

The results show:

- If you only consider the obvious costs the ICE car modelled is the most cost-effective option. On this basis, opting for the ICE is forecast to save £1,638 (or 4%) when compared to the PHEV which is next best option.
- As before, taking account of the less obvious costs changes the picture, with the overall costs for all the cars falling when factoring in the VAT recovery and corporation tax relief.
- Bringing the less obvious costs into consideration has the biggest impact for the BEV, with a significant difference in the cost of employer NICs and no leasing disallowance cost.
- The overall cost of funding the BEV falls by £12,980, or 27%, when the less obvious costs are included in the calculation. In contrast, the overall cost for the ICE only falls by 13%.
- When comparing the employer costs of funding the cars modelled on a WLC basis the BEV is the most cost-effective option. On this basis, opting for the BEV is forecast to save £4,812 (or 12%) when compared to the ICE alternative.

Observation:

The results of the case study highlight the challenges involved for companies trying to understand the financial implications of potential decisions for their company car arrangements. On the face of it, allowing employees to choose ICE vehicles can appear to be a cost-effective approach. The list price and cost of rentals for these cars are typically cheaper than comparable PHEV or BEV alternatives, and so they would seem to be the better option from a cost perspective.

However, calculating the true cost of funding company cars is a complex process with many moving parts, and costs changing based on the choice of car. The cost that had the most noticeable difference between the cars modelled was the cost of employer NICs on the company car benefit, with the impact of this increasing significantly as the cars involved get more expensive. Business mileage reimbursement and leasing disallowance also affected the overall result.

Switching to a WLC approach completely changed the outcome of the analysis, with the BEV offering the lowest cost option when compared to the alternatives modelled. This highlights the challenge for employers, with the potential for less obvious and harder to track costs having a material impact on funding. Adopting a WLC approach can help companies to base their decisions and future strategy on robust and informed analysis, and this can help with better management of car scheme costs.

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.

A key feature of an ECOS is that it will involve the transfer of title for the vehicle to the employee at the outset of the arrangement. The transfer of title to the employee means that the car provided fails one of the requirements for it to be deemed a company car, and so it will be treated as a private car for tax purposes. Therefore, the related mechanisms involved, such as a loan to purchase the vehicle, business mileage reimbursement, motor insurance etc., will need to be considered for their own income tax and NIC treatment, rather than through the car benefit charge.

It is important to be aware that the term "Employee Car Ownership Scheme" is only one of many terms 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.

Is an ECOS appropriate for electric vehicles?

Historically, many employers used an ECOS for job need fleets to offer an arrangement that would deliver a cost profile that more accurately reflected the level of business use for the cars involved. Central to this was the fact that a private car provided via an ECOS would not attract CCT and this would offer significant savings that were leveraged in the way the car was funded.

For example, an employee provided with a £30,000 company car with a CCT rate of 29% would have paid £145 or £290 per month in tax, for a basic rate or higher rate taxpayer respectively. In an ECOS, employees usually contributed towards the costs of funding their car based on the value of the CCT they saved, with any remaining funding provided through business mileage claims and AMAPs, and in some cases an additional employer cash top up. This means employees were broadly kept in the same financial position as a company car. However, if the employees were provided with a BEV, the amount of income tax saved would drop to £10 or £20 a month for a basic or higher rate taxpayer respectively (assuming a list price of £30,000 and CCT rate of 2%). As a result, it is likely an employer would have to pay significantly more cash top ups to keep employees neutral, and this would reduce or remove any financial benefit of operating an ECOS.

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 greater resources are needed for communication and 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 can increase 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 offering cash allowances increased following their inception, with a significant majority of companies now offering a cash allowance in some form or another. To accommodate the increasing demand, a number of new leasing products were developed and are available for employees opting to receive a cash allowance. For instance, a range of affinity schemes are 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 a company links its employees to a fleet provider who 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).

In the years leading up to the pandemic, there was a broad trend with many employers and employees moving away from company cars towards cash allowances. This was especially true for perk populations, where employees typically paid higher rates of company car tax which made the cash alternative a financially attractive option. The trend towards cash allowances grew during the pandemic, where business and private mileage levels dropped dramatically leaving employees paying tax on vehicles that were not being used as much and offering less value for money. However, the general trend at the start 2023 is much less clear, with the volatility in vehicle prices, supply issues, rising inflation and the impact of low tax rates for EVs all impacting the choice of a company car or cash allowance.

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. Depending on the car in question and the employee tax position, 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 tax home pay. 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 considering the new rules around emission testing and the change in CO₂ 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 that employees use for business purposes. Also, with the 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 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 the extent of volume support and manufacturer discounts received on remaining company cars, pushing those costs higher, potentially negating any cost savings from introducing cash allowances. Therefore, it is important that a company fully considers all 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 others 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:

- What is the overall objective of providing cash allowances?
- Does the business prefer employees choosing a company car or cash allowance?
- 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 costliest 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 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 or electricity they have used. However, unlike company cars, where the reimbursement is only intended to cover the cost of fuel or electricity, 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 NIC liability. 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

It is worth noting that employers do not have to reimburse at the maximum rates published by HMRC and can choose to reimburse below these rates if desired. In general, where employees are not entitled to a cash allowance, companies will reimburse for business mileage at the full AMAP rates to provide funding to cover employees' costs. However, where employees receive a cash allowance that can be used to meet some of the costs of funding a private car, companies will usually reimburse for business mileage below AMAP rates. This is to avoid the risk employees could profit from business journeys which could encourage unnecessary business mileage.

For example, if an employee is driving a private car with fuel consumption of 44MPG and a fuel price of £1.55/litre, each mile travelled would cost approximately only 16p per mile in fuel costs. If the driver were being reimbursed 45p per mile, this would leave 29p 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 29p 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 only.

Where employers reimburse business mileage above the AMAP rates, income tax and NICs will be due on the reimbursement, regardless of whether the employee can demonstrate higher costs were incurred. There was some confusion on this point as the government's responses to a number of Parliamentary Questions on AMAPs in March and August 2022. The responses stated that actual expenditure in relation to business mileage could be reimbursed free of Income Tax and National Insurance contributions. The statement made was incorrect, and this option is in fact only possible for volunteer drivers.

What is Mileage Allowance Relief?

If a company reimburses an employee for business mileage in their privately owned vehicle below the AMAP rates, the employee is entitled to claim tax relief, but not National Insurance relief, on the difference between what they received and what the AMAP 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 16p per mile they would only receive £960, a shortfall of £1,740 compared to what they could have been paid using the HMRC rates. As a result, the employee can claim tax relief at the end of the tax year for the shortfall, and assuming a 40% taxpayer, the relief would be worth an additional £696 (£1,740 X 40%).

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: An employee offered a perk company car or cash allowance

In this example the employee is a higher rate taxpayer travelling 2,500 business miles and 7,500 private miles each year. The vehicle provided is a petrol engine car with CO₂ emissions of 146g/km and a list price of £40,670. 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).

		Company			Employee		
		Annual cost ¹	Diff' £s	Diff' %	Annual cost ⁽¹⁾	Diff' £s	Diff' %
Company car		£9,822	-	-	£7,042	-	-
Cash allowance	Employer neutral	£9,822	£0	0%	£6,313	(£729)	(10%)
	Employee neutral	£8,741	(£1,081)	(11%)	£7,042	£0	0%

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

The results show that the cost to the business of providing the company car, or a company neutral cash allowance, would be £9,822 p/a. 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 £729 net p/a, or 10%, 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 £8,741 per annum. This would equate to reduction in costs of £1,081 p/a, or 11%, 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 £280 p/a. If the employee fails to make a MAR claim, which many do, this will leave them financially disadvantaged compared to the level of funding they are entitled to when undertaking business mileage in a private car.

Example 2: An employee offered a job need company car or cash allowance

In this example the employee is a basic rate taxpayer travelling 15,000 business miles and 5,000 private miles each year. The vehicle provided is a diesel engine car with CO₂ emissions of 128g/km and a list price of £27,945. 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		£7,830	-	-	£2,497	-	-
Cash allowance	Employer neutral	£7,830	£0	0%	£2,942	£445	18%
	Employee neutral	£8,393	£563	7%	£2,497	£0	0%

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

The results show that the cost to the business of providing the company car, or a company neutral cash allowance, would be £7,830 per annum. As in example 1, 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.

However, the outcome has changed compared to example 1 when looking at the employee perspective, with the employee actually worse off by £445 net p/a, or 18%, 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 £8,393 p/a. This would equate to a cost increase of £563 p/a, or 7%, 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 £640 p/a. As before, if the employee fails to make a MAR claim, this will 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 relatively low 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.

For simplicity, the examples shown were based on an employee provided with a petrol engine car. The growing trend for employees to switch to EVs adds another layer of complexity to the choice of company car or cash allowance and this is explored further in the following case study.

What about providing 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 optimised cash allowances?

Due to the way in which optimised cash allowance arrangements worked historically, they were 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 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 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 main objective of implementing an optimised cash allowance arrangement is typically to deliver a cost reduction for the company. With a large 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, 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) that 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:

- 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 increased take home pay. However, there will be additional work required to implement the arrangement and the ongoing operation. 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. 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. Do the HMRC AMAP rates apply to private EVs?

- A. Yes. The AMAP rates apply for business mileage undertaken in a private car regardless of whether the car in question uses fuel or electricity.

Q. Is it possible to reclaim VAT on a 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 (or pays the cost upfront such as on a credit card billed to the company)?

- 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 via payroll (or on the employee’s Form P11D if the company pays for the fuel at the outset). 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. If the employee is reimbursed by the company, then they should also have income tax and employee’s NI deducted from the reimbursement via payroll.

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.

Case study: The impact of EVs on the choice of a company car or cash allowance

Introduction

According to the latest figures available from HMRC, the number of company car drivers has been steadily declining since a peak of almost 1 million in 2015/16. The latest figures (published September 2022) show numbers falling four years in row, with HMRC forecasting a further 10% drop for the 2020/21 tax year (at the time of writing, HMRC had only published actual figures up to 2019/20). One of the possible reasons for the decline seen in the figures available to date 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, several issues have affected the provision of company cars making cash allowances a relatively more attractive option in comparison. Since 2015, the company car tax costs have increased with HMRC figures showing that the taxable value of the cars provided increased in the period up to 2019/20, despite the number of company cars actually falling. In the same period new legislation was introduced that increased the cost and complexity of administering of some company car scheme arrangements. Cash allowances have also been growing in popularity with employees who want flexibility and may not see the value of a long-term commitment to a company car, especially after the COVID-19 pandemic.

However, the announcement of low rates of company car tax for EVs (which took effect from April 2020) have had a major impact, with new trends emerging in company and employee behaviours. In 2015/16, HMRC figures show that cars with emissions of 0g/km - 50g/km only accounted for 1% of company cars on the road (at these emission levels these cars would be an EV). In contrast, HMRC expect that when the figures are confirmed for 2020/21, EVs will have accounted for 18% of the company cars on the road, with fully electric vehicles showing the fastest rate of growth (the timing of the figures being released means it is not possible to see the true impact of the low tax rates for EVs just yet, with confirmed figures only available for period before the new rates took effect). However, it is known that companies and employees considering the choice of company cars and a cash allowance will have had more to think about, and it will be interesting to see what impact it has when HMRC releases its next set of benefit statistics.

This case study is designed to explore the financial implications of companies and employees choosing between company cars and cash allowances and how this is affected by the switch to EVs.

Analysis & assumptions

In this case study the WLC was calculated for a selection of example cars from a job-need and perk population of drivers. The cars modelled included a range of power trains and price points. The analysis compared the WLC of:

- 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. To highlight the impact of the low tax rates for EVs the cars modelled include a comparable petrol, diesel, PHEV and BEV alternative.

All calculations were based on the following:

- The business pays the main rate of corporation tax and has no restriction on its VAT recovery.
- All cars are acquired in April 2023 and kept for a replacement cycle of 48 months.
- Fuel and electricity costs based on current prices at the time of writing the guide.
- The cost of business mileage was reimbursed using HMRC's AFRs for fuel and actual cost of electricity for the BEV (this is to avoid employees being out of pocket using the AER).
- Electricity costs were based on a 75%/25% split of home and public charging.
- Employees claiming mileage allowance relief where applicable.

In addition, the calculations for job-need drivers were based on the following:

- Employees are basic rate taxpayers driving 15,000 business and 5,000 private miles p/a.

In addition, the calculations for perk drivers were based on the following:

- Employees are higher rate taxpayers driving 2,500 business and 7,500 private miles p/a.

Results

The following table shows the result for the job-need cars modelled.

Car description					Company	Employee			
	List price	Power-train	CO ₂	Elec. Range	WLC	Company car	Private car	Diff' (£s)	Diff' (as %)
Small hatchback	£19,730	Petrol	107	n/a	£25,336	£5,237	£7,664	£2,427	46%
	£21,605	Diesel	101	n/a	£26,085	£6,872	£8,725	£1,853	27%
Hatchback	£26,275	Petrol	121	n/a	£31,864	£10,524	£13,977	£3,453	33%
	£26,990	Diesel	110	n/a	£31,308	£7,727	£9,484	£1,757	23%
	£33,535	PHEV	23	41	£32,755	£5,517	£17,505	£11,988	217%
	£31,290	BEV	0		£28,092	£5,488	£17,907	£12,419	226%
SUV	£31,370	Petrol	149	n/a	£37,661	£13,953	£16,473	£2,520	18%
	£31,365	Diesel	122	n/a	£34,148	£10,665	£11,611	£946	9%
	£33,785	PHEV	30	30	£32,769	£10,541	£20,462	£9,921	94%
	£35,695	BEV	0		£31,569	£5,585	£20,176	£14,591	261%

The results show that:

- Where a BEV model was available, opting for this as a company car offered the employee the most cost-effective option, both for the company and employee perspective.
- 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 9% and 261% higher funding the same cars privately with a cash allowance.
- This is due to the combined impact of relatively low costs of company car tax, along with higher costs of funding the same car privately.
- With less expensive cars that have lower CO₂ emissions, the BIK value will be 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 a total of 20,000 miles p/a, 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. Also, the cost of personally leasing a PHEV or BEV is likely to be higher than comparable petrol and diesel equivalents.

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

The following table shows the result for the perk cars modelled.

Car description					Company	Employee			
	List price	Power-train	CO ₂	Elec. Range	WLC	Company car	Private car	Diff' (£s)	Diff' (as %)
Saloon	£38,040	Petrol	153	n/a	£33,902	£27,764	£22,022	(£5,742)	(21%)
	£40,310	Diesel	138	n/a	£34,100	£28,865	£20,743	(£8,122)	(28%)
	£43,460	PHEV	30	41	£35,096	£17,204	£29,515	£12,311	72%
	£42,450	BEV	0		£29,032	£7,868	£27,104	£19,236	244%
Exec. Saloon	£50,000	Petrol	165	n/a	£50,118	£36,468	£31,789	(£4,679)	(13%)
	£53,340	Diesel	135	n/a	£51,233	£36,345	£30,346	(£5,999)	(17%)
	£55,020	PHEV	32	40	£43,692	£15,314	£37,937	£22,623	148%
	£61,350	BEV	0		£40,495	£8,699	£36,140	£27,441	315%
Exec. SUV	£85,920	Petrol	216	n/a	£67,041	£59,467	£39,123	(£20,344)	(34%)
	£74,980	Diesel	219	n/a	£69,153	£52,794	£42,048	(£10,746)	(20%)
	£83,160	PHEV	53	28	£60,069	£33,658	£48,435	£14,777	44%
	£81,350	BEV	0		£55,510	£9,579	£47,639	£38,060	397%

The results show that:

- Where a BEV model was available, opting for this as a company car offered the employee the most cost-effective option, both for the company and employee perspective
- 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 13% to 34% compared to costs of opting for a 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 higher list prices, company car tax rates, and employee income tax rate.
 - Also, with a relatively low annual mileage of 10,000 miles, the cost of funding a personal lease and maintenance should 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 44% to 397% 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, 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 higher than a petrol or diesel equivalent due to the higher cost of the technology involved with these vehicles, making them more expensive to fund privately.

Observation:

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

With perk car fleets, where employees are typically higher rate taxpayers and cars tend to have a higher list price, switching to use a cash allowance can be a more cost-effective approach for petrol and diesel engine cars. This is mainly due to the fact that these cars typically have a high BIK value and significant income tax costs for employees and NICs costs for the company. This dynamic is likely to be one of the reasons that there has been a trend to move away from company cars in recent years. However, when it comes to EVs, the results show a very different picture. The low rates of company car tax for EVs offer a very low BIK value, even for cars with a high list price, so they are most cost-effective when provided as a company car.

With job need fleets the picture is quite different, with company cars shown as being the most cost-effective option for employees for all the examples shown. This is mainly due to the relatively low cost of company car tax and increased costs of personal leasing for higher mileage contracts. The outcome is most extreme for the EVs modelled, with the additional price premium of these vehicles leading to a much higher cost of funding these vehicles with a cash allowance.

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, vehicle list price, CO₂ emissions, contract mileage etc. if they are to make an informed choice and deliver a policy that works for the business and its employees.

Salary sacrifice

Salary sacrifice is a contractual agreement between an employee and their 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, with employees able to sacrifice salary in return for being provided with a range of benefits, that can include for example health insurance, bikes for work and pension contributions. The attractiveness of salary sacrifice for employees usually stems 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 offset 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 years leading up to 2017. The main reason for this was that the financial impact of giving up an element of salary plus paying CCT on the car provided, was often lower than the cost for an employee of leasing the a comparable new car privately. As a result, there was a financial incentive for employees to fund a car via salary sacrifice.

The introduction of the OpRA legislation (explained in the 'Understanding company car tax' chapter) 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 NICs advantages of salary sacrifice arrangements for most benefits, and this included cars. The introduction of the OpRA legislation meant that salary sacrifice arrangements lost much of their financial efficiency and the numbers of cars taken via salary sacrifice arrangements began to fall.

However, when the OpRA legislation was implemented the government included an exemption for Ultra Low Emission Vehicles (ULEVs), which are vehicles that emit 75g/km or less of CO₂. The exemption was included so that the CCT rules kept a financial incentive for employees to pick company cars with lower emissions. Critically, the exemption for ULEVs meant that salary sacrifice continued to offer a financial advantage for these vehicles. For the purposes of this chapter, any reference to salary sacrifice relates to ULEVs. In recent years, the rapid growth in the choice of EVs available, and the introduction of reduced CCT rates for EVs, has resulted in a surge in demand for salary sacrifice in the last few years. The trend has helped to boost the uptake of EVs, which falls squarely in line with the government's road to zero agenda.

What are the advantages of salary sacrifice?

There are several reasons why a salary sacrifice arrangement can be an attractive benefit offering for companies and employees. These can include, but are not limited to:

Income tax and NI efficiencies

The salary sacrifice mechanism can deliver income tax and NI efficiencies because the sacrifice is made from gross pay. This means that participating employees will no longer have to pay income tax or employee NICs on the value of the salary they have given up. With combined income tax and employee NIC rates that range from 32% to 47%, sacrificing salary can offer a significant financial advantage for employees. Also, companies will no longer have to pay employer NICs on the salary given up, which offers further financial advantages for this type of arrangement.

Low rates of CCT

The introduction of low rates of CCT for BEVs and some PHEVs means that these cars will have a low BIK value. This means that the income tax and employer NICs implications involved with company cars is quite low. In the Autumn Statement 2022 it was confirmed that the low rates of CCT for EVs will remain at least until 6 April 2028.

Provision of connected benefits

The tax system includes a mechanism that limits the BIK value for a company car and additional benefits that are provided in connection with the car. This means an employer can provide additional benefits within the salary sacrifice arrangement where they are connected to the company car without incurring an additional tax or NICs liability. In most salary sacrifice car schemes this includes the provision of vehicle maintenance and motor insurance, but it could also include other benefits like the installation of a home charge point.

Recruitment and retention

With a growing desire from employees to make changes that can mitigate the impact of climate change, and an expanding range of new and exciting EV technologies, a salary sacrifice arrangement can present the opportunity for companies to offer a new and an engaging employee benefit. As an optional benefit, it can give employees greater personal choice and flexibility on how they are rewarded which can have a positive impact on recruitment and retention conversations.

Reduction in 'grey fleet'

Grey fleet is a term used to describe the situation where employees use their private cars for business travel. Operating grey fleets can be challenging because companies will typically have a lack of management and control over the vehicles in the grey fleet. This means grey fleet vehicles may not be ideally suited for business journeys and they could be at odds with the company's corporate image or sustainability policy. With a grey fleet, there can also be a lack of clarity as to who has responsibility in such matters as motor insurance and maintenance, and from a corporate governance perspective, a company has certain health and safety responsibilities that can prove problematic for large grey fleets. Salary sacrifice involves the provision of a company car where the business has a much greater degree of oversight and control over the cars, and it can reduce the size of and potential risk associated with grey fleet vehicles.

Convenience

Employees may perceive salary sacrifice as an attractive benefit where they can access a car 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 leasing company and often come with servicing, roadside assistance, and other related support services. For employees who have never experienced a company car before, it is likely they would value the convenience aspect and the reduced hassle of car 'usership'.

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 who are not typically entitled to a company car to access the bulk buying discounts of their employer.

As noted above, a salary sacrifice arrangement can offer a wide range of benefits for an employer and its employees. However, introducing this type of arrangement can also present some challenges. For instance, a business may wish to consider the following before introducing a new scheme:

- The potential investment of time and/or money required to design and implement the arrangement.
- The practical challenges associated with everyday use of EVs and likely level of demand from employees.
- The level of ongoing support and administration required.
- Any financial risks for the business and its employees.
- The statutory reporting requirements associated with providing company cars.

It may be advisable for an employer to consider the full range of benefits alongside the potential challenges before introducing a salary sacrifice for EVs arrangement. A carefully considered and well-designed scheme can help to mitigate or even remove the potential challenges, while offering a robust arrangement that unlocks a range of benefits for an employer and their employees.

Let's look at some examples

To help illustrate the potential benefits of salary sacrifice we have included some examples below. To give a like-for-like comparison, the examples show the employee cost of taking a car via salary sacrifice compared to the cost of the same vehicle funded privately using a personal lease, and a comparable ICE car also funded using a personal lease.

The employee costs shown are as follows:

- The salary sacrifice cost is the net value of the salary sacrificed after taking account of the income tax and employee NICs that would have been due on the salary, plus the amount of CCT due on the company car BIK and electricity private mileage.
- The personal lease cost includes the cost to the employee of funding the car via a personal lease paid from net salary after taking account of the income tax and employee NI due, plus the cost of electricity or fuel for private mileage.

In all the examples, the cars were provided over a 3 year term assuming 10,000 private miles p/a include maintenance and motor insurance. The fuel and electricity calculations used current prices at the time of writing this guide, and electricity was based on a 75%/25% split of home and public charging. The salary sacrifice calculation was set up to generate a saving for the company by retaining 50% of the NICs saved.

Example 1: Hatchback

The employee is a basic rate taxpayer and the cars used in this example are:

- A BEV with a list price of £25,790; and
- A petrol engine car with a list price of £25,085 and CO₂ emissions of 122g/km.

	BEV		ICE equivalent
	Salary sacrifice	Personal lease	Personal lease
Net employee cost (36 months)	£17,176	£26,380	£26,943
Saving of salary sacrifice (36 months)	-	£9,204	£9,767
Saving of salary sacrifice (per month)	-	£256	£271

The example shows that opting to fund the BEV via salary sacrifice is the most cost effective option for the employee. When compared to the personal lease option, salary sacrifice would save £256 p/month taking the same car, or £271 p/month for a comparable petrol alternative.

In this example, the company would generate a saving of £346 p/a for each car.

Example 2: SUV

The employee is a basic rate taxpayer and the cars used in this example are:

- A BEV with a list price of £31,745; and
- A petrol engine car with a list price of £27,700 and CO₂ emissions of 121g/km.

	BEV		ICE equivalent
	Salary sacrifice	Personal lease	Personal lease
Net employee cost (36 months)	£20,601	£32,101	£24,871
Saving of salary sacrifice (36 months)	-	£11,500	£4,270
Saving of salary sacrifice (per month)	-	£319	£119

The example shows that opting to fund the BEV via salary sacrifice is the most cost effective option for the employee. When compared to the personal lease option, salary sacrifice would save £319 p/month taking the same car, or £119 p/month for a comparable petrol alternative.

In this example, the company would generate a saving of £437 p/a for each car.

Example 3: Executive saloon

The employee is a higher rate taxpayer and the cars used in this example are:

- A BEV with a list price of £51,000; and
- A petrol engine car with a list price of £44,470 and CO₂ emissions of 146g/km.

	BEV		ICE equivalent
	Salary sacrifice	Personal lease	Personal lease
Net employee cost (36 months)	£25,844	£44,457	£47,550
Saving of salary sacrifice (36 months)	-	£18,613	£21,706
Saving of salary sacrifice (per month)	-	£517	£603

The example shows that opting to fund the BEV via salary sacrifice is the most cost effective option for the employee. When compared to the personal lease option, salary sacrifice would save £319 p/month taking the same car, or £119 p/month for a comparable petrol alternative.

In this example, the company would generate a saving of £604 p/a for each car.

Example 4: Executive SUV

The employee is a higher rate taxpayer and the cars used in this example are:

- A BEV with a list price of £69,850; and
- A diesel engine car with a list price of £70,120 and CO₂ emissions of 181g/km.

	BEV		ICE equivalent
	Salary sacrifice	Personal lease	Personal lease
Net employee cost (36 months)	£31,227	£58,578	£67,505
Saving of salary sacrifice (36 months)	-	£27,351	£36,278
Saving of salary sacrifice (per month)	-	£760	£1,008

The example shows that opting to fund the BEV via salary sacrifice is the most cost effective option for the employee. When compared to the personal lease option, salary sacrifice would save £760 p/month taking the same car, or £1,008 p/month for a comparable petrol alternative.

In this example, the company would generate a saving of £891 p/a for each car.

Observation:

The examples show that opting for a BEV via salary sacrifice can offer a significant financial advantage for employees when compared to funding the same car using a personal lease. In addition, the analysis shows that salary sacrifice for a ULEV can also offer large cost savings when compared to personally leasing a comparable ICE car, although the level of savings will depend on the cars in question. The results highlight the fact that a salary sacrifice arrangement can offer an engaging car scheme arrangement for employees that can deliver significant financial benefits as well as an opportunity to reduce carbon emissions.

However, it is 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.

What is HMRC's approach to salary sacrifice arrangements?

Salary sacrifice is a longstanding concept with a range of guidance published by HMRC and so there should be relatively limited complexity and potential compliance risk involved with a properly designed and implemented scheme. In general, there are usually two main areas of potential HMRC interest in respect of a salary sacrifice arrangement for company cars. These are:

- The effectiveness of the salary sacrifice arrangement.
- Ensuring the correct income tax and NICs treatment and reporting for the company cars provided.

Historically, employers were able to seek clearance from HMRC to confirm that their salary sacrifice arrangement was effective, and that it operated correctly for income tax and NICs. However, at the end of 2020, HMRC updated its guidance to confirm that it would only provide clearance for salary sacrifice arrangements if there was a point of legal uncertainty about the proposed arrangements. Before this, HMRC would have provided post implementation clearance on salary sacrifice arrangements if requested. This change of approach has helped to remove some of the administration involved with implementing a salary sacrifice arrangement. However, without the option of seeking HMRC clearance, it places more onus on employers to make sure that any arrangement put in place will involve an effective salary sacrifice and will operate in line with legislation and HMRC guidance.

If an arrangement is not effective and it is challenged by HMRC, this can result in complex and costly implications for a business. Principally, HMRC may seek to subject the amounts “sacrificed” to income tax and NICs if they believe the salary was not effectively sacrificed. Therefore, it is important that employers considering a salary sacrifice arrangement take appropriate advice and care when designing, implementing and operating this type of arrangement. It is important to note that HMRC would examine arrangements on a case-by-case basis, and that there is no mechanism for a blanket approval for an “off the shelf” arrangement that may be marketed by car lessors.

HMRC have published a range of guidance for employers to help them understand salary sacrifice and how to operate it correctly. Some useful sources of guidance include:

- Guidance for employers on how to set up salary sacrifice arrangements and calculate tax and NICs contributions on them - Salary sacrifice for employers - GOV.UK (www.gov.uk)
- Technical guidance on salary sacrifice - EIM42750 - Salary sacrifice: what is a salary sacrifice: arrangement of guidance - HMRC internal manual - GOV.UK (www.gov.uk)

What is required for an ‘effective’ salary sacrifice?

While a salary sacrifice arrangement should not be too complex to implement and administer, care needs to be taken to ensure that any arrangements put in place meet HMRC requirements for an ‘effective sacrifice’. In some cases, the question of whether an arrangement is effective can be affected by details such as the terminology used in employee communications, or whether employees could be reasonably considered to have understood what they are agreeing to. The key conditions required for an effective salary sacrifice include:

A contractual variation of terms

A salary sacrifice will only be effective where the terms and conditions of the employee’s employment contract are changed. Changing the contract can be done by rewriting it in part or whole, setting out the changes in a separate agreement attached to the main contract, or the company informing employees of proposals to make changes. In practice, the contractual change is usually enacted by the employee entering into a separate salary sacrifice agreement that varies specific terms of their employment contract.

A binding change

Where an employee receives a non-cash benefit via salary sacrifice, they must not have the right to change their mind and revert to the original salary at any time. Otherwise, the arrangement could be seen as an optional and temporary change rather than a permanent one and may not be considered an effective sacrifice.

Prior agreement

HMRC guidance stipulates that the entitlement to future remuneration must be given up before it is treated as received for employment income purposes. This means an employee who is entering into a salary sacrifice arrangement must agree to vary the employment contract in advance of the date when the first payment under the new arrangement is due. In practice, employees are usually required to sign the salary sacrifice agreement before ordering their vehicle and well before the date the first sacrifice payment is due.

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

- A. No, 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 sees fit.

Q. Are there any employee population where salary sacrifice may not work as well others?

- 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 can lead to early termination 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. Also, salary sacrifice may not be ideal for some employees where NMW implications can increase the complexity involved with administration.

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: implementing a salary sacrifice arrangement that does not offer an effective sacrifice or correctly the constituent elements of remuneration to tax and NIC.
 - Financial risk: operating arrangements without an effective policy or financial insurance to manage and mitigate operational costs that are not built into the sacrifice e.g., early termination and excess mileage charges, insurance excess costs, repairs for unfair wear and tear.
 - Low take-up: under invested in employee communications can result in poor and uncoordinated materials that do not maximise employee take up and the potential benefits on offer.
 - Internal resource costs: failing to consider the internal resource requirements needed to design, implement and then provide ongoing administration for the scheme.

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 NICs cost associated with the vans provided. From an employee perspective, there will also be the issue of income tax due on the BIK value. 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.

What is the definition of a van for tax purposes?

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, in particular whether the vehicle provided should be deemed a van or a company car under for tax purposes.

One example of the potential issues can be seen in a well-known tax case that centered on whether certain vehicles should be treated as a company car or company van. The case involved three different 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 the result being that two vehicle were vans, while the other was a car. The case went through three levels of the justice system to the Court of Appeal, where it was ultimately found that all three vehicles were cars for income tax purposes.

If an employee is found to be provided with a company car instead of a company van, the most likely outcome is that the company will have to disclose this issue to HMRC and make good any income tax and NICs liabilities that were not paid. In addition, employees using company vans are usually provided with fuel for these vans, and often there's no requirement to recorded business and private mileage. If the vehicle provided is actually a car, the fuel can trigger a car fuel benefit charge, which can significantly increase the amount of income tax and NICs liabilities to make good. If the employer makes good any employee liabilities as part of the disclosure, this may need to be done on a grossed up basis, further increasing the costs involved. When these issues are combined, making a mistake on whether a vehicle is a car, or a van can result in significant financial implications.

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 ton (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, fiberglass 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).

How do you determine 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 to decide whether it should be reported as a BIK. If the use of the van meets certain conditions, then there is no BIK or 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 (here) 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 that 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.

Van fuel benefit

If an employee is provided with fuel as well as a company van, then a fuel benefit charge arises if the associated 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. For the 2023/24 tax year, the van fuel benefit charge is £757.

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 the optional remuneration arrangements 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 vans are treated.

Appendix 1 – Company car tax rates

In the 2022 Autumn Statement the government announced rates affecting the amount of income tax paid on company car benefits for an additional three tax years to provide long term certainty for taxpayers and industry with rates now published for 6 April 2025 through to 5 April 2028.

The announcements set the appropriate percentage used to calculate the income tax due on company car benefit as follows:

- For electric vehicles with CO₂ emissions of 0g/km - the applicable rate (2% in 2024/25) will rise by 1 percentage point each year for three subsequent tax years up to a maximum of 5% in 2027/28.
- For ULEVs with CO₂ emissions of 1-75g/km - the applicable rates will rise by 1 percentage point in each of the three subsequent tax years, up to a maximum of 21% in 2027/28.
- For all other vehicles with CO₂ emissions exceeding 75g/km - the applicable rates will be increased by 1 percentage point in the 2025/26 tax year up to a maximum of 37%. The rate will then remain frozen for a further two tax years until 6 April 2028.

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

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

CO ₂ emissions (g/km)	Electric range ²	% of vehicle list price ¹				
		2021/22	2022/23 2023/24 2024/25	2025/26	2026/27	2027/28
0	N/A	1	2	3	4	5
1-50	>130	1	2	3	4	5
1-50	70-129	4	5	6	7	8
1-50	40-69	7	8	9	10	11
1-50	30-39	11	12	13	14	15
1-50	<30	13	14	15	16	17
51-54		14	15	16	17	18
55-59		15	16	17	18	19
60-64		16	17	18	19	20
65-69		17	18	19	20	21
70-74		18	19	20	21	21
75-79		19	20	21	21	21
80-84		20	21	22	22	22
85-89		21	22	23	23	23
90-94		22	23	24	24	24
95-99		23	24	25	25	25
100-104		24	25	26	26	26
105-109		25	26	27	27	27
110-114		26	27	28	28	28
115-119		27	28	29	29	29
120-124		28	29	30	30	30
125-129		29	30	31	31	31
130-134		30	31	32	32	32
135-139		31	32	33	33	33
140-144		32	33	34	34	34
145-149		33	34	35	35	35
150-154		34	35	36	36	36
155-159		35	36			
160-164		36	37	37	37	37
165+		37				

¹ 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.

² Electric range is the number of miles which is the equivalent of the number of kilometers 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.

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.

B

Balloon payment

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 CO₂ emissions, with a supplement for diesel 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 CO₂ 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*

An 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 OpRA legislation.

N*National Insurance contributions (NICs)*

A social security charge that is 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 Benefit-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 WLTP 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 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 introduced 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 30 to 50 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 record a car's emissions more accurately, especially of harmful air pollutants such as NOx. Unlike WLTP and the old NEDC regime, the RDE tests take place on real roads. All new car types need to be compliant with RDE Step 2 ('RDE2') – 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 2023/24 tax year runs from 6 April 2023 to 5 April 2024.

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 CO₂ 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 CO₂ 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 (WLTP)*

The regime for measuring a new car's CO₂ 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 applies 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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