



## Company Cars – Changes to the tax system

Far ranging changes to tax allowances for Company Cars will be introduced from April 2009 and we are putting this memo together to outline their impact so that you can consider your approach to how you deal with motor car purchases going forward.

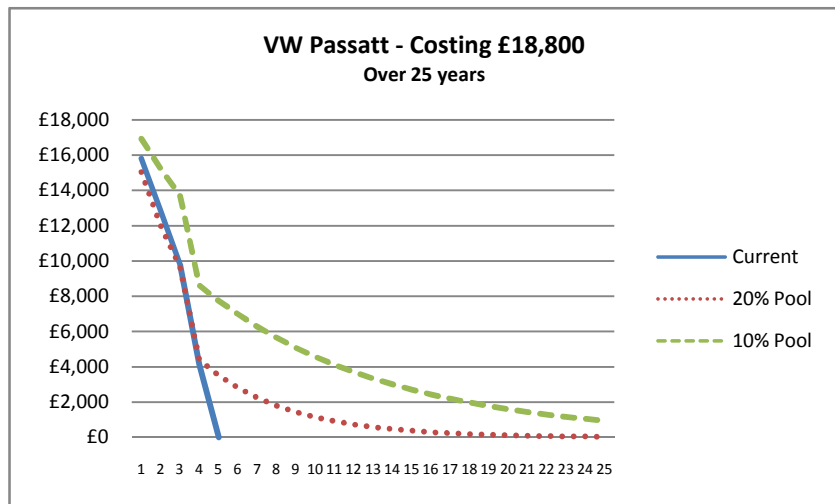
Currently, the actual capital cost of owning cars (i.e. purchase price less sales proceeds) with an original cost over £12,000 (referred to as “expensive cars”) is offset against profits earned essentially during the life of the car using the capital allowances regime (So if you buy a car for £18,000 and sell it for £8,000 you will claim an overall deduction against tax of £10,000).

The main changes which only apply to new cars purchased after 6 April 2009, dictate that the cost of the car is spread over a period longer than the vehicle’s life. Does this matter? Well, except for the most CO<sub>2</sub> efficient cars, you will have to wait many years to get the full tax benefit. Unbelievably you could still be claiming tax allowances on some of these vehicles 60 years later!

For example, you buy a modest fleet car (for example a VW Passatt) car costing £18,800 and sell it for £4,200 during the fourth year (after plenty of mileage).

Currently you can claim all of the £14,600 against profits of the period of ownership. From April 2009 the allowances claimed in the four years will total £6,000 leaving a “residue” of £8,600 for which no allowances have been given -

and that’s equivalent to between £1,720 and £2,600 (depending upon the profits in your company) of extra tax paid that will take years to recover – all you can do is to carry on claiming capital allowances at 10% assuming, of course, that nothing else changes.



If the car has CO<sub>2</sub> emissions of less than 160g/km (which is achievable for this type of car), the effect is lessened with only £4,400 (between £880 and £1,232 in tax) remaining unclaimed after the life of the car.

If you can operate cars emitting less than 110g/km of CO<sub>2</sub> (such as Volkswagen Polo BlueMotion, Seat Ibiza and Ford Fiesta Econetic – all of which emit below 100 g/km) you can claim 100% first year allowance to offset against profits. Also, because the new scheme doesn't limit the amount of capital allowance claim per car (currently limited to £3,000 per annum) there will be a short term cash benefit, depending on the cost and CO<sub>2</sub> emissions of the cars being operated. The administrative work will also reduce.

### **Existing cars**

If your business already owns cars, and those cars cost less than £12,000, they will stay hidden in the general pool when the rules change, with a WDA of 20% per annum (even if they have high CO<sub>2</sub> emissions). If you are planning to buy a cheaper car with high emissions, you may accelerate tax relief by acquiring the car before April 2009 and keeping it out of the lower 10% pool.

If an existing car cost more than £12,000 and it is currently in its own expensive car pool, it will also stay there after the rules change. It will continue to benefit from a WDA of 20% capped at £3,000 pa, and will benefit from a balancing allowance on disposal, for a transitional period of five years. Businesses planning to acquire expensive high emission cars can avoid the delayed relief brought in by the new rules if they acquire the car before April 2009 and dispose of it before the five year transitional period expires.

### **Leased cars**

Cars under existing leases will remain under the current regime until the lease comes to an end. Cars under leases taken out from April 2009 will be subject to the new 15% disallowance rule where CO<sub>2</sub> emissions exceed 160 gm/km. Short term hire cars will be subject to the same rules.

### *Example*

Under the current rules, the lease payments for a £25,000 car would have 26% of the payments disallowed. For a £50,000 car, the element disallowed would be 38%.

Under the new rules, there will be no disallowance if emissions are below 160gm/km, and only a 15% disallowance if emissions are above this. Leasing will therefore be more attractive than it used to be.

### **Possible Solutions to consider**

The figures mentioned above are arguably relatively minor for one off vehicle purchases, however for larger fleets or more expensive cars it could be that the ownership route will have significant taxation disadvantages after April 2009. Other options that avoid the residue of unrelieved capital expenditure are:

- Operate cars which have very low CO<sub>2</sub> emissions
- Consider using contract hire or lease cars from April 2009
- Introduce cash-for-car type arrangements and avoid operating any new company cars going forward.
- For larger fleets of cars, it would be worth considering setting up a leasing company to hire the vehicles back to the company.

**Conclusion:**

The purpose of this document is to set out the broad changes and principles that are unfolding with regard to how tax relief for motor vehicles is changing. It is not intended to make any recommendations as each case will depend upon its own merits.

If you feel that a more in depth discussion or consideration on this matter is required, then please feel free to get in touch.

Kind Regards

Mark Andrews

**A bit more information (if you need it...)****Very low CO<sub>2</sub> emissions**

By far the best option is to use cars emitting less than 110 g/km. These will be eligible for 100% first year tax allowances giving maximum tax benefit. However, the choice is somewhat restricted, with cars tending to be smaller and possibly viewed as less suitable for business travel.

**Contract hire**

All issues associated with WDAs become the problem of the hire company. They may need to reflect the large deferred tax residuals in their own pricing however they will be in a better position to access the tax value of the cars over the short / medium term.

Rentals for contract hire are written to the profit and loss account immediately and the cars are not shown on the company liability. There are some restrictions for cars with emissions exceeding 160g/km (namely 15% of the rental). Additionally VAT is restricted to 50% of the rentals (this is the equivalent to the 100% VAT block on new cars anyway).

**Cash for Car Schemes**

Under these arrangements employers negotiate a buy out of the employees' rights to company cars - in exchange for an increased salary and paying a mileage claim (usually 40p for the first 10,000 miles and 25p thereafter) - the employees then take on responsibility for acquiring and running their own vehicles.

The calculations behind this option are complex and employees can become emotive. However, if constructed correctly, Cash for Car schemes can be efficient and afford benefits to both parties.

## Capital allowances

Capital allowances are the tax equivalent of depreciation and they will be calculated on the cost of the car and its Carbon Dioxide (CO<sub>2</sub>) emissions and offset against taxable profits.

Writing Down Allowances (“WDAs”)

<u>CO<sub>2</sub> Range</u>	<u>Current</u>	<u>From April 2009</u>
110 to 160 g/km	20% pa	20% pa <i>(most manufacturers have ‘green’ fleet cars in this range)</i>
More than 160 g/km	20% pa	10% pa
Maximum WDA per annum	£3,000	No limit

*Note: An allowance of 100% will be available for cars emitting less than 110 g/km (120 g/km until April 2009).*

Once an expensive car has been sold, companies are allowed to claim the difference between cost, less any WDAs already taken and sale proceeds as a Balancing Allowance. As from April 2009 this allowance will be withdrawn and WDAs will continue at the rates shown above long after the car has been sold.

### Example of a more expensive car

If you buy a luxury car costing £57,500 and sell it for £18,975 during the fourth year. Currently you can claim the difference, £38,525 against profits of the period of ownership. From April 2009 the allowances claimed in the four years will total £17,877 leaving a “residue” of £20,648 for which no allowances have been given - and that’s equivalent to around £6,200 of extra tax paid that will take years to recover – all you can do is to carry on claiming WDAs at 10% - after 20 years there will still be over £3,800 outstanding (£1,140 of tax) assuming, of course, that nothing else changes.

