

Business Motoring – Tax Aspects

This factsheet focuses on the current tax position of business motoring, a core consideration of many businesses. The aim is to provide a clear explanation of the tax deductions available on different types of vehicle expenditure in a variety of business scenarios.

Methods of acquisition

Motoring costs, like other costs incurred which are wholly and exclusively for the purposes of the trade are tax deductible but the timing of any relief varies considerably according to the type of expenditure. In particular, there is a fundamental distinction between capital costs and ongoing running costs.

Purchase of vehicles

Where vehicles are purchased outright, the accounting treatment is to capitalise the asset and to write off the cost over the useful business life as a deduction against profits. This is known as depreciation.

The same treatment applies to vehicles financed through hire purchase with the equivalent of the cash price being treated as a capital purchase at the start with the addition of a deduction from profit for the finance charge as it arises. However, the tax relief position depends primarily on the type of vehicle, and the date of expenditure.

A tax distinction is made for all businesses between a normal car and other forms of commercial vehicles including vans, lorries and some specialist forms of car such as a driving school car or taxi.

Tax relief on purchases

Vehicles which are not classed as cars are eligible for the Annual Investment Allowance (AIA) for expenditure incurred. This allowance allows a 100% write off against profits on plant and machinery purchases of £100,000 per year (the allowance was £50,000 before 1 April 2010 for a business within the charge to corporation tax and before 6 April 2010 for a business within the charge to income tax). It is proposed that this will reduce to £25,000 in 2012.

As the chargeable accounting periods of many businesses will span the operative date of change, a pro rata calculation of their maximum entitlement will be required.

A restriction has been set so that only £50,000 of that available amount can be used for expenditure incurred before 1 April 2010 (for corporation tax) or 6 April 2010 (for income tax).

Where purchases exceed the AIA, a writing down allowance (WDA) is due on any excess in the same period. This WDA is currently at a rate of 20%. Cars are not eligible for the AIA, so will only benefit from the WDA.

Capital allowance boost for low-carbon transport

A 100% first year allowance is available for capital expenditure on new electric vans from 1 April 2010 for companies and 6 April 2010 for an unincorporated business.

Complex cars!

The green car

Cars generally only attract the WDA but there is one exception to this and that is where a business purchases a new car with low emissions – a so called 'green' car. Such purchases attract a 100% allowance to encourage businesses to purchase cars which are more environmentally friendly. The 100% write off is only available where the CO₂ emissions of the car do not exceed 110 grams per kilometre (g/km). The cost of the car is irrelevant and the allowance is available to all types of business.

When did you buy?

There have been significant changes to the basis of capital allowances for car purchases and the tax relief thereon from 1 April 2009 for companies and 6 April 2009 for individuals in business.

For purchases from April 2009:

The annual allowance is dependent on the CO2 emissions of the car rather than the cost.

- Cars between 110 -160 g/km are placed in the main pool and will qualify for an annual allowance of 20%. It is proposed that this will reduce to 18% in 2012.
- Cars in excess of 160 g/km are placed in the special rate pool and will qualify for an annual allowance of 10%. It is proposed that this will reduce to 8% in 2012.

If a used car is purchased with CO2 emissions of 110 g/km or less, this will be placed in the main pool and will receive an annual allowance of 20%.

Any cars used by the self employed where there is part non-business use will still be separately allocated to a single asset pool. The annual allowance will initially be either the current 20% or 10% depending on the CO2 emissions and then the available allowance will be restricted for the private use element.

For purchases before April 2009 the following rules apply:

Cars costing up to £12,000 were included in the main plant pool and get the annual 20% reducing allowance only. There are proposals to reduce this to 18% in 2012.

Cars costing more than £12,000 (so called expensive cars) usually had to be allocated to a separate single asset pool. Each qualifies for the annual allowance of 20% but with a maximum annual allowance on each car of £3,000. There are proposals to reduce this to 18% in 2012. On disposal of each separate asset an extra allowance is available on any overall net cost.

Any cars used by the self employed with part non business use were also separately allocated to a single asset pool so that any private use element can be restricted. This does not apply to employee provided cars.

Example

A company purchases three cars for £20,000 in its 12 month accounting period to 31 December 2009. The dates of purchase and CO2 emissions are as follows:

Red car	White car	Blue car
1 March 2009	1 May 2009	1 May 2009
145	145	165

Allowances in the year to 31 December 2009 relating to these purchases will be:

Red car (old rules apply - single pool as more than £12,000 cost)	White car (new rules apply - main pool as emissions less than 160)	Blue car (new rules apply - special rate pool as emissions more than 160)
£20,000 @ 20% = £4,000 but restricted to £3,000	£20,000 @ 20% = £4,000 No capping	£20,000 @ 10% = £2,000

In the following year to 31 December 2010 the allowances will be:

Red	White	Blue
£17,000 @ 20% = £3,400 but restricted to £3,000	£16,000 @ 20% = £3,200 No capping	£18,000 @10% = £1,800

Disposals

Where there is a disposal of plant and machinery from the main or special rate pools any balance of expenditure, after taking into account sale proceeds, continues to attract the annual allowance.

Where there is a disposal of a car held in a single asset pool, there is an additional allowance if there is an unrelieved cost. This is often referred to as a balancing allowance.

This applies to:

- cars which cost greater than £12,000 prior to April 2009
- any cars used by the self employed with part non business use whenever purchased.

In the less usual situation of a car disposal where all costs have been recovered and there is an excess of sale proceeds then this is clawed back as a 'negative' capital allowance.

What difference will it make?

The key change here is that certain employee or director provided cars would have been placed in a single asset pool when the cost of the purchase exceeded £12,000. Therefore on disposal any shortfall in allowances would have been available at the time of disposal. For cars purchased from April 2009 this will not apply as the cars will be included in one of the two plant pools (main or special rate). Instead the annual allowance will continue to be claimed in that and subsequent periods.

Example

The company above sells all three cars in its accounting period to 31 December 2012 for £7,000. The tax balances immediately prior to sale and the effects of the sales are as follows:

At the start of the period	Red (single asset)	White (main pool)	Blue (special rate pool)
Tax balance	£11,200	£10,240	£14,580
Proceeds	(£7,000)	(£7,000)	(£7,000)
Balance after disposal	£4,200	£3,240	£7,580
Allowance permitted in period of disposal	£4,200	£648 (£3,240 @ 18.5%*)	£758 (£7,580 @ 8.5%*)
In subsequent periods	Nil as all covered	*Transitional WDA rate reducing to 18% in 2013	*Transitional WDA rate reducing to 8% in 2013

What if vehicles are leased?

The first fact to establish with a leased vehicle is whether the lease is really a rental agreement or whether it is a type of purchase agreement, usually referred to as a finance lease. This is because there is a distinction between the accounting and tax treatment of different types of leases.

Tax treatment of rental type operating leases (contract hire)

The lease payments on operating leases are treated like rent and are deductible against profits. However where the lease relates to a car there may be a portion disallowed for tax.

For 2009/10 onwards for new lease agreements a disallowance of 15% will apply for cars with CO2 emissions which exceed 160 g/km.

For 2008/09 and earlier years this applies where the car has CO2 emissions in excess of 110 g/km and a retail price when new which exceeds £12,000. An adjustment is made to disallow part of that excess. These rules continue to apply for lease agreements entered into before 1 April 2009 for companies and 6 April 2009 for businesses within the charge to income tax.

Example

Contract signed 1 April 2009 by a company:

The car has CO2 emissions of 166 g/km and a £6,000 annual lease charge. The disallowed portion would be £900 (15%) so £5,100 would be tax deductible.

Contract signed pre 1 April 2009 by a company:

The car has CO2 emissions of 175 g/km, a retail list price of £20,000 and an annual lease charge of £6,000. There would be a disallowance of £1,200 (calculated by applying a formula) so only £4,800 would be tax deductible.

Tax treatment of finance leased assets

These will generally be included in your accounts as fixed assets and depreciated over the useful business life but as these vehicles do not qualify as a purchase at the outset, the expenditure does not qualify for capital allowances unless classified as a long funded lease. Tax relief is generally obtained instead by allowing the accounting depreciation and any interest/finance charges in the profit and loss account - a little unusual but a simple solution! A disallowance still applies if the vehicle is an expensive car.

Private use of business vehicles

The private use of a business vehicle has tax implications for either the business or the individual depending on the type of business and vehicle.

Sole traders and partners

Where you are in business on your own account and use a vehicle owned by the business - irrespective of whether it is a car or van - the business will only be able to claim the business portion of any allowances. This applies to capital allowances, rental and lease costs, and other running costs such as servicing, fuel etc.

Providing vehicles to employees

Where vehicles are provided to employees irrespective of the form of business structure - sole trader/partnership/company - a taxable benefit generally arises for private use. A tax charge will also apply where private fuel is provided for use in an employer provided vehicle. For the employer such taxable benefits attract 13.8% (12.8% before 6 April 2011) Class 1A National Insurance.

Vans

No charge applies where employees have the use of a van and a restricted private use condition is met. For details on what this means please contact us. Where the condition is not met there is a flat rate charge per annum of £3,000 for the unrestricted private use plus an additional £550 for private fuel.

How we can help

If you would like further details on any matter contained in this factsheet please do contact us.

For information of users: This material is published for the information of clients. It provides only an overview of the regulations in force at the date of publication, and no action should be taken without consulting the detailed legislation or seeking professional advice. Therefore no responsibility for loss occasioned by any person acting or refraining from action as a result of the material can be accepted by the authors or the firm.