# 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 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 £250,000 per year (previously £25,000). However it should be noted that for expenditure incurred after the 1 April 2013 (6 April for an unincorporated business), the maximum allowance that can be attributed to that expenditure is a fraction of £250,000. The fraction will be the amount of the £250,000 that is included in the calculation of the overall AIA for the accounting period.

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.

Where purchases exceed the AIA, a writing down allowance (WDA) is due on any excess in the same period. This WDA is at a rate of 18% (previously 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 (6 April for an unincorporated business).

## Writing Down Allowances (WDA)

WDA rates reduce from April 2012. The main rate of 20% will be reduced to 18% and the lower rate of 10% which applies to some higher emission cars reduces to 8%. It will be necessary to calculate hybrid rates where the accounting period straddles April 2012 which will give a rate between 20% and 18% (or between 10% and 8%) for that period.

## Complex cars!

### The green car

Cars generally only attract the WDA but there is one exception to this 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 $CO_2$ emissions of the car do not exceed 110 grams per kilometre (gm/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 $CO_2$ emissions of the car rather than the cost.

- Cars between 111-160 gm/km are placed in the main pool and will qualify for an annual allowance of 18% (previously 20%).
- Cars in excess of 160 gm/km are placed in the special rate pool and will qualify for an annual allowance of 8% (previously 10%).

If a used car is purchased with $CO_2$ emissions of 110 gm/km or less, this will be placed in the main pool and will receive an annual allowance of 18% (previously 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 18% or 8% (previously 20% and 10%) depending on the $CO_2$ 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 18% (previously 20%) reducing allowance only.

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 18% (previously 20%) but with a maximum annual allowance on each car of £3,000. 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 two cars for £20,000 in its 12 month accounting period to 31 March 2012. The dates of purchase and $CO_2$ emissions are as follows:

| White car | Blue car |
|---|---|
| 1 May 2011 | 1 May 2011 |
| 145 gm/km | 165 gm/km |

Allowances in the year to 31 March 2012 relating to these purchases will be:

| White car (main pool as emissions less than 160 gm/km) | Blue car (special rate pool as emissions more than 160 gm/km) |
|---|---|
| £20,000 @ 20% = £4,000<br>No Capping | £20,000 @ 10% = £2,000 |

In the following year to 31 March 2013 the allowances will be:

| White car | Blue car |
|---|---|
| £16,000 @ 18% = £2,880 | £18,000 @ 8% = £1,440 |

## Future changes

Cars with emissions between 111-160gm/km inclusive currently qualify for main rate WDA. The threshold is to be revised down to 130gm/km for additions from 1 April 2013 for businesses within the charge to corporation tax and 6 April 2013 for businesses in the charge to income tax.

The 100% first year allowance (FYA) available on new low emission cars purchased (not leased) by a business is revised and extended with effect from 1 April 2013. The current rule is that a 100% FYA is generally available where a car's emissions do not exceed 110 gm/km until 31 March 2013. The availability of a 100% FYA is to continue for a further two years for purchases from 1 April 2013 but only where emissions do not exceed 95gm/km.

## 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 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 $CO_2$ emissions which exceed 160 gm/km.

For 2008/09 and earlier years this applies where the car has $CO_2$ emissions in excess of 110 gm/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 $CO_2$ emissions of 166 gm/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 $CO_2$ emissions of 175 gm/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 abacus can help

If you would like further details on any matter contained in this factsheet please do get in touch with **abacus**.

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