

## **CARS AND TAXATION**

Cars – and their tax treatment – always raise a lot of questions.

### VAT

VAT isn't usually deductible on the acquisition of car. It is on the acquisition of a van or motorcycle. The only exception to the vat rules on buying a car is if the car is to be used solely for business, eg a taxi or driving school, and there is a ban on any private use of the car (and this is scrutinised quite closely by HMRC).

VAT is normally deductible on running costs and fuel for a car.

Where vat is claimed back on fuel and there is any private use of the vehicle then a fixed scale charge for the private fuel is imposed and vat has to be paid on that scale charge. The scale charge is treated as additional sales of the business (think of it as a imposed charge for hiring the car from the business for private use).

### Income Tax – Sole Traders and Partnerships

Where a car is bought by a sole trader or partner for use in their business then the expenditure normally qualifies for Capital Allowances at 20% PA and a Balancing Allowance / Charge on sale. However any car over £12,000 is deemed "expensive" and the allowances are restricted to £3,000 pa until the pool value of unrelieved expenditure is less than £12,000. NB see further notes below about capital allowances.

Running costs for the car (fuel, servicing, insurance, road fund licence) are normally deductible for tax and Class IV NI.

Capital allowances and running costs are subject to a private use restriction.

If a car is bought on hire purchase or finance lease (where you will own the vehicle), then this is treated as two separate transactions – acquisition of the vehicle, qualifying for Capital Allowances, and a loan on which the business use of the finance charges can be claimed.

Where a car is acquired on an operating lease – broadly speaking a lease where you do not own the asset at the end – then the lease payments are deductible, again subject to a private use restriction and also subject to a restriction if the car costs more than £12,000.

If a car is bought by a sole trader for use by a staff member, then see the rules below.

For businesses turning over less than the VAT registration threshold, currently £67,000, then instead of claiming running costs and capital allowances, a simple mileage rate can be applied. The rate is 40p per mile for the first 10,000 miles per annum and thereafter 25p per mile. This is sometimes a simpler alternative for a small business.

The rules on vans and motorcycles are very similar, although Capital Allowance rates differ.

## Income Tax / Corporation Tax - Cars for employees (including directors)

Where a business buys a car for use by an employee, including company directors (who are treated as employees) there are two considerations – tax deduction for the business and the tax charge for the employee.

### TAX DEDUCTION FOR THE BUSINESS

The expenditure normally qualifies for Capital Allowances at 20% PA and a Balancing Allowance / Charge on sale. However any car over £12,000 is deemed “expensive” and the allowances are restricted to £3,000 pa until the pool value of unrelieved expenditure is less than £12,000. NB see further notes below about capital allowances.

Running costs for the car (fuel, servicing, insurance, road fund licence) are normally deductible for tax and Class IV NI.

If a car is bought on hire purchase or finance lease (where you will own the vehicle), then this is treated as two separate transactions – acquisition of the vehicle, qualifying for Capital Allowances, and a loan on which the business use of the finance charges can be claimed.

Where a car is acquired on an operating lease – broadly speaking a lease where you do not own the asset at the end – then the lease payments are deductible, again subject to a private use restriction and also subject to a restriction if the car costs more than £12,000.

There are no private use restrictions on the above.

### TAX CHARGE ON THE EMPLOYEE / DIRECTOR

The employee (including in all cases company directors) is subject to a benefit in kind for tax on having the benefit of a car for private use (a so called “company car”). The benefit in kind is added to their income for tax purposes and the employer pays Class 1A National Insurance on the benefit.

For a car the benefit is generally a percentage of the cars list price, linked to its emissions level, and with an additional charge if fuel is provided for private use. A table of emissions and percentages is appended at appendix one.

Where fuel is provided for private use, a further benefit is payable, and again subject to tax on the employee and NI on the employer. The benefit is calculated according to the emissions percentage on a figure of £14,400. If the employee is required to repay fuel costs for private motoring, or no fuel is provided at all then this charge does not apply. Where no fuel is provided then fuel costs can be claimed, tax free, from the employer at as called “advisory fuel rates” (see appendix one).

A “pool” car isn’t a taxable benefit for a staff member, but there are strict rules for a car to be a pool car, in particular (a) it must not be normally allocated to one member of staff exclusively and (b) it must not be normally be taken home by a staff member at night,

Example benefit in kind:

Car with CO<sub>2</sub> emissions of 25g/km, 2005/06 tax year. List price £18,000. Petrol.

Benefit in kind is 32% of list price (from table in appendix), i.e. £5,760. The employee pays tax on this amount, and the employer Class 1A NI.

If fuel is provided for private use then a further benefit in kind is due at 32% x £14,400 = £4,608. The employee pays tax on this amount, and the employer Class 1A NI.

Different rules apply to the private use of company vans. Where the only private use is travelling to and from work, and other incidental use (eg an occasional shopping trip) then there is no benefit in kind. Otherwise there is a benefit in kind of £3,000 for private use of the van (applicable to both Income Tax for the employee and class 1A NI for the employer) and a further £500 fuel benefit if fuel is provided for private use

Employee / Director using their own car for business

Because company cars are taxed quite heavily – both for employee and employer – in many cases its sensible for the employee / director to use their own car and claim mileage.

The mileage rates that can be claimed, tax free, are:

Cars and vans

First 10,000 miles PA	40p per mile
Over 10,000 miles pa	25 p per mile
Passenger miles (other than driver)	5p per passenger per mile
Motorcycle rate per mile	24 p
Pedal cycle rate per mile	20 p

Allowances paid at these rates are tax free for the employee, and tax deductible for the employer.

For a small company it nearly always makes sense for the directors to own their own cars and claim mileage, as they bear the cost of both the Income Tax and NI benefit charges.

## Further notes on Capital Allowances

Capital allowances on cars are changing.

For 2007/08 and previous years the writing down allowance rate was 25%. 100% first year allowances applied to new cars with emissions of less than 120g/km.

For 2008/09 the writing down allowance becomes 20%. 100% first year allowances applies to new cars with emissions of less than 110g/km. NB the £50,000 Annual Investment Limit for plant and equipment from 008/09 onwards does not extend to cars. It does extend to vans / motor cycles.

From 1 April 2009, the writing down allowance will depend on emissions. The present proposals are:

- cars emitting less than 110g/km – 100% first year allowance
- cars emitting over 110g/km and less than 160g/km, 20% annual writing down allowance
- cars emitting over 160g/km 10% writing down allowance

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## Appendix 1 – Emissions percentages and advisory fuel rates

### Emissions Table 2008/09

CO <sub>2</sub> in g/km*	Taxable %		CO <sub>2</sub> in g/km*	Taxable %	
	Petrol	Diesel		Petrol	Diesel
Less than 121	10%	13%	185 to 189	25%	28%
121 to 139	15%	18%	190 to 194	26%	29%
140 to 144	16%	19%	195 to 199	27%	30%
145 to 149	17%	20%	200 to 204	28%	31%
150 to 154	18%	21%	205 to 209	29%	32%
155 to 159	19%	22%	210 to 214	30%	33%
160 to 164	20%	23%	215 to 219	31%	34%
165 to 169	21%	24%	220 to 224	32%	35%
170 to 174	22%	25%	225 to 229	33%	35%
175 to 179	23%	26%	230 to 234	34%	35%
180 to 184	24%	27%	235 and over	35%	35%

\* The exact CO<sub>2</sub> figure is rounded down to the nearest 5g/km

### Advisory fuel rates from 1 June 2008

	Petrol	Diesel	LPG
1400 cc or less	12 p pm	13 p pm	7 p pm
1401 to 2000 cc	15 p pm	13 p pm	8 p pm
2000cc or more	21 p pm	17 p pm	13 p pm

These rates are updated every six months – for the latest rates see [http://www.hmrc.gov.uk/cars/advisory\\_fuel\\_current.htm](http://www.hmrc.gov.uk/cars/advisory_fuel_current.htm) .