



# Company car tax reform in the UK

**A Summary**

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# Company car tax in the UK



- **Employer:** car provision, fuel, insurance, O&M, taxes
- **Employee:** private use of the car is a benefit in kind – taxed via income tax
- **What is the subsidy? Employee does not pay taxes on the net full annual cost of a car**, excl. business use) – e.g. optimal rate of income tax 51% in NL (G&O, 2009)



# Pre- reform: Private use of company cars



## Pre – reform

1. **Benefit in kind tax graduated on business mileage.** ↑ **km the** ↓ **the tax rate (35%-15%).** →

**35%** of the list price of the car < **2,500** business miles  
**25%** if **2,500 to 17,999** business miles  
**15%** if **18,000** or more business miles

2. **Fixed tax charge for free fuel benefit** – independently of actual use



# Post reform - Private use of company cars



## Post – reform (2002)

1. **Benefit in kind tax rate graduated on CO2 emissions.** →

10% at or <120gCO<sub>2</sub>/km  
15% under <135gCO<sub>2</sub>/km  
+5% for each 5gCO<sub>2</sub>/km  
35% for > 235gCO<sub>2</sub>/km

2. **Business mileage thresholds were removed.**

3. **Fuel benefit charge is graduated on CO2 emissions of the company car**

- The subsidy was not removed but reformed - used to greening the car market
- Perverse incentives to buy heavier cars and drive more have been removed



# Impacts of cc tax reform



## Purchasing behaviour

- 60% employee influenced by reform
- ↓ 20 gCO<sub>2</sub>/km average company car emissions

## Emissions reduction

- ↓ 0,2 – 0,3 MtCO<sub>2</sub>/year and up to 0,64 MtCO<sub>2</sub>/year in 2010
- ↓ 300 – 400 million business miles year

## Impacts of free fuel tax

- ↓ 660,000 employees receiving free fuel (from 1m to 400,000)
- ↓ 100 million private miles in 2005 compared to 1997

## Opting out

- CC no longer considered essential for business
- Cash (65% of opt out)
- Other non cash benefits



# Unintended impacts of reform



- ↓ **Number of company cars** from 1.6 million to 1.4 million
- **Leakage to other more tax favourable systems** (mileage allowance payments, private vans) – on average + 5 gCO<sub>2</sub>/km
- **Switch from petrol to diesel** (from 33% in 2002 to 60% in 2005) – trade off CO<sub>2</sub> with local air quality
- ↓ **Revenue loss**: £120 million net revenue loss (↓ tax rate for environmentally friendly cars, ↓ company cars, ↓ fuel use, ↑ revenues from income tax from cash option)



## Flat rate mileage allowances (in 2002)

£0.40 (€0.58) per mile up to 10,000 and

£0.25 (€0.36) per mile above 10,000 miles

→ **needs to mirror cc scheme**

Data source: HMRC (2006) and (2007)

# Main drivers of reform



- Reform was **strongly resisted until a clear evidence base** was established by new research (characterising company cars and travel data).
- **Progressive elements in government and industry** were prepared to help and champion change.
- **NGOs, businesses and government cooperation**
- Introduction of the **car labelling Directive** facilitated the introduction of CO2 grades, as a lever to affect car choice

# Obstacles to reform



- Vested interests in status quo.
- Inertia
- Trade offs with social concerns - rural areas, commutes.



# Factors to enhance/ hinder success



- **CC taxes do not operate in isolation – policy should be integrated and aligned**
  - benefit in kind CO2 based + Free fuel benefit taxes CO2 based + VED ownership taxes CO2 based
  - .... use of private cars for business schemes + mileage allowance schemes + Tax treatment of parking expenditure + Tax treatment of relocation benefits + Road pricing / Congestion charge reimbursement
- **Need to periodically re-examine goals (e.g. 4 years)**
- **Announce reform in good advance**

# Is reform transferable to Germany?



- **Yes (depending on the exact design of company car taxation system)**
- The benefit in kind flat rate could be CO2 graduated, higher level bands could be set up
- The benefits on CO2 from this reform will not bring much impact if commuter subsidies are kept in place



# Further references



- Gutierrez-i-Puigarnau E. and van Ommeren J. (2009), *Welfare effects of distortionary fringe benefits taxation: the case of employer provided cars*, Tinbergen Institute Discussion Paper, 20 March 2009 – ref. G&O (2009) [here](#)
- HMRC (2006), *Report on the evaluation of the company car tax reform: stage 2*
- HMRC (2007), *report on interaction between company cars, employee car ownership scheme cars and mileage allowance payments*
- IEEP et al. (2006), *Improving the knowledge basis of car purchase decision mechanisms and environmental impact of company car taxation*



**Thank you!**

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# Integrated assessment results



## Policy reform:

- **Subsidy removal:** US model - additional wage that can be used to lease a car if needed; employee pays taxes on full cost; de-taxed reimbursement for use for business purposes.

## Negative impacts

- Need to carefully avoid leakage to other systems

In the UK a system of statutory mileage allowances still exists, with the level currently set at £0.40 (€0.58) per mile up to 10,000 and £0.25 (€0.36) per mile above 10,000 miles (ABRL, 2006).

# Provision of company car as a benefit in kind to employees



## Is the objective still valid?

- Promote productivity / de-tax business.
- 90% company cars are not or hardly used for business purposes (research in the NL, G&O, 2009).
- **Professionals prefer cash or relocation benefits.**

## Cost-effectiveness:

- Targeted policies for increased productivity are more effective.
- Removal would increase cost-effectiveness of other instruments e.g. road pricing.

## Incidental impacts:

- The most inequitable fringe benefit (COWI, 2004) – high income, men.
- Increase commuting distances, larger cars, more cars per household.
- Substantial taxes foregone (in EU 18 billion EUR / year in deadweight loss, G&O, 2009).