THE BMW GROUP GUIDE TO FLEET FUNDING.

The way in which fleet vehicles are funded varies widely, but there are two main acquisition methods:

- **Outright purchase**
- **Leasing over a fixed period**

With outright purchase, the fleet funds the acquisition and operation of the vehicle and assumes all responsibility, including the residual value risk.

Leasing involves outsourcing the acquisition and, more often than not, the operational costs to a specialist provider such as a leasing company in return for a pre-agreed fixed monthly payment. In most cases, the leasing company retains ownership of the vehicle and assumes the residual value risk.

There are several variations of leasing that offer flexible solutions depending on a customer's circumstances and requirements, and these, together with the advantages and disadvantages of outright purchase are covered in this BMW Guide to Fleet Funding.

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1: OUTRIGHT PURCHASE.

Outright purchase, where a company funds the fleet from its own resources, historically has been the predominant funding method.

For an organisation with the cash to do this, and a fleet manager with the expertise to negotiate, purchase, maintain and insure the fleet, as well as oversee effective disposal, this can still work well. The benefits for larger fleets include substantial buying power, complete flexibility on acquisition and disposal and, in some cases, enhanced asset value.

But it can be a costly exercise – you have numerous depreciating assets on the balance sheet, and you are exposed to residual value fluctuations at resale. Added to that, of course, is that outright purchase demands that you must be secure financially, with the liquidity to tie large amounts of capital up in the purchase of cars.

Whole-life costs: the cornerstone of any fleet acquisition calculation

Whole-life costs – the total projected operating costs of a particular make and model over a set period, usually expressed in pence-per-mile terms – should form the basis of any company car equation, particularly when considering outright purchase. Comprising many facets of vehicle operation including depreciation, fuel costs and servicing, as well as funding charges, insurance and employers' National Insurance Contributions (NIC), whole-life costs enable you to build a picture of a vehicle's operating costs that can be used to compare with other models. In turn, these comparisons will help set the criteria to establish the most cost-effective options for your choice list.

Capital allowances

Significant tax advantages are available for fleets purchasing their cars outright. The allowances are particularly attractive if the purchased cars are low emitters of CO_2.

A capital allowance is the amount a company is allowed to offset against corporation tax due to the depreciation of assets it has bought, working on the theory that the value of that asset, such as a car, decreases every year. The figure – the so-called write-down allowance, or WDA – is calculated relative to the CO_2 emissions of the car as well as by deducting the value of the car when it is sold from the cost when it was new.

A 100% first-year write-down allowance (FYA) applies to cars bought with CO_2 emissions of 75g/km or less, applicable until 31 March 2018 for limited companies and 5 April 2018 for sole traders and partnerships. New cars purchased outright with CO_2 emissions of between 76-130g/km are eligible for a WDA of 18% a year, while those with higher emissions attract a WDA of 8% a year.

From 1 April 2018, the 100% first-year threshold reduces from 75g/km to 50g/km, and the main rate threshold falls from 130g/km to 110g/km, applicable until 31 March 2021.

Electric cars have qualified for a 100% first year capital allowance since 2002.

2: LEASING.

Often, businesses find it easier to create a company car choice list using set cost parameters – the basis of contract hire. A monthly 'car allowance' banding is set by the employer in conjunction with an outsourced leasing company, with drivers selecting a car from a choice list of vehicles within their bandings, which conveniently can be 'tiered' according to a driver's entitlement.

For the employer, the advantages are clear because the vehicle residual value and disposal risks are eliminated as both are taken on by the leasing company and packaged as part of the monthly rental.

The fixed monthly cost structure also allows for predictable and reliable forecasting, and because vehicles do not appear on the balance sheet, financial ratios can be improved and working capital freed up for other purposes.

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Furthermore, the administration burden of the fleet, which may also include servicing and repairs, tyre replacement and glass repair/replacement, is also handed to the leasing company, leaving the employer to concentrate on its core business.

Most companies can claim back a proportion of the VAT charged on the finance element of the monthly rentals as well as all the VAT on servicing and maintenance costs.

For leased vehicles, cars with CO_2 emissions of 130g/km or less are eligible for 100% of their lease payments to be offset against tax, while for cars with CO_2 emissions of 131g/km or more only 85% of their lease payments can be offset.

Leasing companies are, however, exempt from the 100% first-year allowance (FYA).

The resulting convenience of contract hire means it has overtaken outright purchase as the most popular funding method in the UK, accounting for funding in some 60% of the total company car market.

WHY YOUR VAT POSITION IS IMPORTANT.

Changes to VAT were introduced in 1995 enabling VAT-registered companies that could show vehicles were used exclusively for business use to recover VAT in full when buying cars.

As the leasing company owns the car, but does not use it for any private mileage – the lessee does – it can claim back the VAT at acquisition. Together with its already strong volume-based buyer power, the savings should be reflected in favourable lease rates to customers.

Added to that is that VAT on lease rentals for cars is 100% recoverable, subject to normal VAT rules, if the vehicle is used entirely for business. Only 50% of the VAT on the rentals is recoverable if there is any private use of the car.

There are further VAT advantages too: the VAT charged on expenses such as maintenance and repairs incurred by a business on a leased car is 100% recoverable. If contract hire charges include maintenance and other services, the 50% restriction to VAT recovery applies only to the 'basic rental' element of the charge.

A basic rental charge usually includes elements such as depreciation, funding costs, VED, overheads, profit and the cost of options or accessories.

'CASH FOR CAR': SHOULD I CONSIDER THE 'GREY FLEET'?

Paying employees a cash allowance in lieu of a company car has become popular in recent years as it can be seen as a significant benefit to staff, allowing them to choose their own car using employers' money, on which they pay income tax and National Insurance.

Legislative changes concerning duty of care, however, increasingly have made the practice less attractive as it is now the fleet, rather than the individual, that bears full responsibility for vehicles being driven on company business.

If the fleet does not own, or have control over, an employee's car can you be certain, for example, that drivers will choose a vehicle that is suitable for purpose, ensure that it is properly insured for business use, adhere to maintenance schedules for safety and roadworthiness and fit with the company's desired business image when travelling on business?

Drivers often see flexibility and personal choice as more important than a rigid company car policy, but so-called 'grey fleet' vehicles present significant problems for employers that can, and should, easily be avoided.

FURTHER INFORMATION: WHOLE-LIFE COSTS.

Many independent specialists provide vehicle whole-life cost illustrations using a variety of criteria. These include:

Kee Resources
www.keeresources.com

CAP HPI Ltd
www.cap-hpi.com

International Decision Systems
www.idsdata.co.uk

Glass's
www.glassbusiness.co.uk

FLEET FUNDING METHOD COMPARISON.

SCHEME	VEHICLE OWNER	IS CAR ON OR OFF FLEET'S BALANCE SHEET?	DOES THE FLEET TAKE THE RV RISK?	ARE THERE MILEAGE/WEAR LIMITATIONS?	ADVANTAGES	DISADVANTAGES
OUTRIGHT PURCHASE	Fleet	On	Yes	No	• Flexibility: the fleet retains full control of the fleet and is not locked into contracts • Any profit at disposal is retained by the fleet • A write-down allowance (WDA) of 18% a year is available to the fleet on cars with CO_2 emissions of between 76-130g/km. Those with CO_2 emissions of 131g/km or more attract a WDA of 8% a year. A 100% first-year allowance (FYA) applies until 31 March 2018 to cars with CO_2 emissions of 75g/km or less. • From 1 April 2018, the main rate capital allowance threshold falls from 130g/km to 110g/km. On the same date, the 100% first-year threshold reduces from 75g/km to 50g/km, with the allowance applicable until 31 March 2021 • For VAT-registered companies, 100% of the VAT on service and maintenance costs can be reclaimed	• Limited buying power compared with a leasing company • Fleet is unable to reclaim full VAT on purchase price unless cars are used solely for business mileage • The fleet takes full exposure to residual value risk • Administration burden lies with the fleet • The fleet takes risk for unexpected repair costs • Ties up capital that could be used elsewhere within the business
CONTRACT HIRE	Leasing company	Off	No	Yes	• Little to no risk for the fleet as the residual value and maintenance risk is passed to leasing company • Low initial outlay – typically three rentals in advance • Fixed outgoings make for easy, reliable budgeting • The fleet should benefit from the supplier's ability to recover VAT on the vehicle purchase price • For cars with CO_2 emissions of up to 130g/km fleets can offset 100% of the lease payments against tax, while cars with emissions of over 131g/km are eligible for 85% of their lease payments to be offset • For VAT-registered companies, VAT can be reclaimed by the fleet on the finance element of the lease, subject to a 50% restriction where private use occurs • For VAT-registered companies, 100% of the VAT on service and maintenance costs can be reclaimed • Administration burden handed to third party	• Early termination and excess mileage costs give inflexibility, with fixed term contract • Unsuitable for unpredictable mileage fleets as excess mileage penalties can be expensive • The fleet does not own the vehicle so cannot benefit from potential residual value rewards • Additional VAT costs for non-VAT-registered or partially VAT-exempt companies
FINANCE LEASE	Leasing company	On	Yes	No	• Any profit at disposal is retained by the fleet • Payment patterns can be structured to suit the fleet's needs • Includes final balloon payment which reduces monthly costs • Provides additional credit line • For cars with CO_2 emissions of up to 130g/km fleets can offset 100% of the lease payments against tax, while cars with emissions of over 131g/km are eligible for 85% of their lease payments to be offset" • For VAT-registered companies, VAT can be reclaimed by the fleet on the finance element of the lease, subject to a 50% restriction where private use occurs • For VAT-registered companies, 100% of the VAT on service and maintenance costs can be reclaimed • Any profit at disposal is retained by the fleet	• The fleet assumes administration burden and is exposed to risks of ownership • The fleet is liable for unexpected maintenance, repair and potential residual value losses • Sale proceeds may not match final balloon payment • Additional VAT costs for non-VAT-registered or partially VAT-exempt companies • Vehicles are on-balance sheet which may inhibit further borrowing

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FLEET FUNDING METHOD COMPARISON. (continued)

SCHEME	VEHICLE OWNER	IS CAR ON OR OFF FLEET'S BALANCE SHEET?	DOES THE FLEET TAKE THE RV RISK?	ARE THERE MILEAGE/WEAR LIMITATIONS?	ADVANTAGES	DISADVANTAGES
HIRE PURCHASE (OR LEASE PURCHASE)	Fleet, for tax and accounting purposes	On	Yes	No	• Interest element of the repayments is offset against tax in line with accounting treatment • Provides additional credit line • Vehicle depreciation can be written off against taxable profit • A write-down allowance (WDA) of 18% a year is available to the fleet on cars with CO_2 emissions of between 76-130g/km. Those with CO_2 emissions of 131g/km or more attract a WDA of 8% a year. A 100% first-year allowance (FYA) applies until 31 March 2018 to cars with CO_2 emissions of 75g/km or less • From 1 April 2018, the main rate capital allowance threshold falls from 130g/km to 110g/km. On the same date, the 100% first-year threshold reduces from 75g/km to 50g/km, with the allowance applicable until 31 March 2021 • For VAT-registered companies, 100% of the VAT on service and maintenance costs can be reclaimed	• Potentially, a large deposit is required • Administration burden lies with the fleet • The fleet is liable for the RV risk as disposal is transferred to the company • Vehicles are on-balance sheet which may inhibit further borrowing
CONTRACT PURCHASE	Fleet	On	No	No, if fleet pays balloon at end, otherwise yes	• Combines tax advantages of outright purchase with operational benefits of contract hire • No residual value risk as this is guaranteed by the finance company • A write-down allowance (WDA) of 18% a year is available to the fleet on cars with CO_2 emissions of between 76-130g/km. Those with CO_2 emissions of 131g/km or more attract a WDA of 8% a year. A 100% first-year allowance (FYA) applies until 31 March 2018 to cars with CO_2 emissions of 75g/km or less. • Efficient for non-VAT registered companies as VAT is not payable on rental payments	• Fleets can reclaim VAT on the capital cost if cars are used only for business mileage • Vehicles currently appear on-balance sheet and count as assets which may or may not be advantageous • Contracts include use/wear limitations • Vehicles are on-balance sheet which may inhibit further borrowing
SALARY SACRIFICE	Leasing company	Off	No	Yes	• Potential tax and National Insurance savings for drivers and company if operated efficiently • Driver pays BIK tax but receives maintained, taxed and insured car at rates that can be lower than private funding methods and in return for a single monthly charge taken from pre-tax salary • Tax and NI-efficient for the employer • Worthwhile staff benefit with little or no input from employer as administration is handled by outsourced leasing company • Reduces 'grey fleet' risks and potentially enhances fleet's 'green' credentials • The employee benefits from the supplier's buying power	• Driver 'sacrifices' part of pensionable salary • Not suitable for employers with high staff turnover as early redemption charges can be costly • Contracts include use/wear limitations • Rule changes in April 2017 potentially reduce effectiveness
SALE AND LEASEBACK	Leasing company	Off	No	Yes	• Releases capital tied up in outright purchased fleet • Removes vehicles from the balance sheet, improving financial ratios (currently) • Eliminates RV/maintenance risk and cuts administration • Potentially, the fleet benefits from the supplier's buying power	• Careful negotiation needed with the leasing company to agree a resale value for the fleet • Contracts include use/wear limitations
EMPLOYEE CAR OWNERSHIP SCHEME (ECOS)	Leasing company	Off	No	Yes	• Removal of employee BIK tax • Tax and NI savings for employer and (potentially) employee • All the benefits of contract hire but with overall tax savings if properly set up	• Complex to set up and administer, though leasing company does most of the admin • Requires thorough investigation, analysis and external advice to be set up properly • Potential HMRC problems if set up incorrectly • Contracts include use/wear limitations

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