# THE BMW GROUP GUIDE
## TO FLEET FUNDING.


**BMW Group** Fleet & Business Sales


# INTRODUCTION.

The way in which fleet vehicles are funded varies widely, but acquisition may be split into two main 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.

# 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. This figure – the write-down allowance, or WDA – is calculated relative to the car's $CO_2$ emissions as well as by deducting its value 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 50g/km or less, applicable until 31 March 2021 for limited companies and 5 April 2021 for sole traders and partnerships. New cars purchased outright with $CO_2$ emissions of between 51-110g/km are eligible for a WDA of 18% a year, while those with higher emissions attract a WDA of 6% a year.

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

# 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.

### Predictable forecasting

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.

Leasing's fixed monthly cost structure 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.

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

However, early termination charges may apply to contracts ended before the full term has been reached – if, for example, an employee leaves his/her position and the leased company car cannot be re-deployed to another employee.

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

### Tax efficient

For leased vehicles in 2019/20, cars with $CO_2$ emissions of 110g/km or less are eligible for 100% of their lease payments to be offset against corporation tax, while for cars with $CO_2$ emissions of 111g/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.


# PRACTICAL CONSIDERATIONS.

**Leasing: why your VAT position is important**
Changes to VAT were introduced in 1995 enabling VAT-registered companies to recover VAT in full when purchasing cars as long as they can demonstrate their company cars are used exclusively for business mileage.

For leasing companies this means that, as it owns the car but does not use it for private mileage – the lessee does – it can claim back the VAT at acquisition. Together with its already strong volume-based buying power, the resulting savings should be reflected in favourable lease rates to customers.

For the lessee, the VAT on lease rentals for cars is 100% recoverable – subject to normal VAT rules – if the car is used entirely for business mileage. If there is any element of private mileage, however, only 50% of the VAT on the rentals is recoverable.

There are further VAT advantages: 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 allows 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 cars 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 car 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 image when travelling on business?

Drivers may see personal choice as more important than a rigid company car policy, but 'grey fleet' vehicles present significant problems for employers that can be easily 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 COMPARISONS.

| SCHEME | OUTRIGHT PURCHASE | CONTRACT HIRE | FINANCE LEASE |
|---|---|---|---|
| **VEHICLE OWNER** | Fleet | Leasing company | Leasing company |
| **IS CAR ON OR OFF FLEET'S BALANCE SHEET?** | On | Off | On |
| **DOES THE FLEET TAKE THE RV RISK?** | Yes | No | Yes |
| **ARE THERE MILEAGE/ WEAR LIMITATIONS?** | No | Yes | No |
| **ADVANTAGES** | • Flexibility: the fleet retains full control of the fleet and is not locked into contracts<br>• Any profit at disposal is retained by the fleet<br>• A write-down allowance (WDA) of 18% a year is available to the fleet on cars with $CO_2$ emissions of between 51-110g/km. Those with $CO_2$ emissions of 111g/km or more attract a WDA of 6% a year. A 100% first-year allowance (FYA) applies until 31 March 2021 to cars with $CO_2$ emissions of 50g/km or less.<br>• Zero-emission electric vans are eligible for a 100% FYA, joining all low-emission vehicles with $CO_2$ emissions of 75g/km or less, applicable until April 2021. All other vans are eligible for an 18% annual capital allowance.<br>• For VAT-registered companies, 100% of the VAT on service and maintenance costs can be reclaimed | • Little to no risk for the fleet as the residual value and maintenance risk is passed to the leasing company<br>• Low initial outlay – typically three rentals in advance<br>• Fixed outgoings make for easy, reliable budgeting<br>• The fleet should benefit from the supplier's ability to recover VAT on the vehicle purchase price<br>• For cars with $CO_2$ emissions of up to 110g/km fleets can offset 100% of the lease payments against tax, while cars with emissions of over 111g/km are eligible for 85% of their lease payments to be offset<br>• 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<br>• For VAT-registered companies, 100% of the VAT on service and maintenance costs can be reclaimed<br>• Administration burden is handed to a third party | • Any profit at disposal is retained by the fleet<br>• Payment patterns can be structured to suit the fleet's needs<br>• Includes final balloon payment which reduces monthly costs<br>• Provides additional credit line<br>• For cars with $CO_2$ emissions of up to 110g/km fleets can offset 100% of the lease payments against tax, while cars with emissions of 111g/km or over are eligible for 85% of their lease payments to be offset<br>• 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<br>• For VAT-registered companies, 100% of the VAT on service and maintenance costs can be reclaimed |
| **DISADVANTAGES** | • Limited buying power compared with a leasing company<br>• Fleet is unable to reclaim full VAT on purchase price unless cars are used solely for business mileage<br>• The fleet takes full exposure to residual value risk<br>• Administration burden lies with the fleet<br>• The fleet takes risk for unexpected repair costs<br>• Ties up capital that could be used elsewhere within the business | • Early termination and excess mileage costs give inflexibility, with fixed term contract<br>• Unsuitable for unpredictable mileage fleets as excess mileage penalties can be expensive<br>• The fleet does not own the vehicle so cannot benefit from potential residual value rewards<br>• Additional VAT costs for non-VAT-registered or partially VAT-exempt companies | • The fleet assumes the administration burden and is exposed to usual risks of ownership<br>• The fleet is liable for unexpected maintenance, repair and potential residual value losses<br>• Sale proceeds may not match final balloon payment<br>• Additional VAT costs for non-VAT-registered or partially VAT-exempt companies<br>• Vehicles are on-balance sheet which may inhibit further borrowing |

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# FLEET FUNDING METHOD COMPARISONS (continued).

| SCHEME | HIRE PURCHASE (OR LEASE PURCHASE) | CONTRACT PURCHASE | SALARY SACRIFICE |
|---|---|---|---|
| **VEHICLE OWNER** | Fleet, for tax and accounting purposes | Fleet | Leasing company |
| **IS CAR ON OR OFF FLEET'S BALANCE SHEET?** | On | On | Off |
| **DOES THE FLEET TAKE THE RV RISK?** | Yes | No | No |
| **ARE THERE MILEAGE/ WEAR LIMITATIONS?** | No | No if fleet pays balloon at end, otherwise yes | Yes |
| **ADVANTAGES** | • Any profit at disposal is retained by the fleet<br>• Interest element of the repayments is offset against tax in line with accounting treatment<br>• Provides additional credit line<br>• Vehicle depreciation can be written off against taxable profit<br>• A write-down allowance (WDA) of 18% a year is available to the fleet on cars with $CO_2$ emissions of between 51-110g/km. Those with $CO_2$ emissions of 111g/km or more attract a WDA of 6% a year. A 100% first-year allowance (FYA) applies until 31 March 2021 to cars with $CO_2$ emissions of 50g/km or less.<br>• Zero-emission electric vans are eligible for a 100% FYA, joining all low-emission vehicles with $CO_2$ emissions of 75g/km or less, applicable until April 2021. All other vans are eligible for an 18% annual capital allowance.<br>• For VAT-registered companies, 100% of the VAT on service and maintenance costs can be reclaimed | • Combines tax advantages of outright purchase with operational benefits of contract hire<br>• No residual value risk as this is guaranteed by the finance company<br>• A write-down allowance (WDA) of 18% a year is available to the fleet on cars with $CO_2$ emissions of between 51-110g/km. Those with $CO_2$ emissions of 111g/km or more attract a WDA of 6% a year. A 100% first-year allowance (FYA) applies until 31 March 2021 to cars with $CO_2$ emissions of 50g/km or less.<br>• Zero-emission electric vans are eligible for a 100% FYA, joining all low-emission vehicles with $CO_2$ emissions of 75g/km or less, applicable until April 2021. All other vans are eligible for an 18% annual capital allowance.<br>• Efficient for non-VAT registered companies as VAT is not payable on rental payments | • Potential tax and national insurance savings for drivers and company if operated efficiently<br>• 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<br>• Tax and national insurance-efficient for the employer<br>• Worthwhile staff benefit with little or no input from employer as administration is handled by outsourced leasing company<br>• Reduces 'grey fleet' risks and potentially enhances fleet's 'green' credentials<br>• The employee benefits from the supplier's buying power |
| **DISADVANTAGES** | • Potentially, a large deposit is required<br>• Administration burden lies with the fleet<br>• The fleet is liable for the RV risk as disposal is transferred to the company<br>• Vehicles are on-balance sheet which may inhibit further borrowing | • Fleets can reclaim VAT on the capital cost if cars are used only for business mileage<br>• Vehicles currently appear on-balance sheet and count as assets which may or may not be advantageous<br>• Contracts include use/wear limitations<br>• Vehicles are on-balance sheet which may inhibit further borrowing | • Driver 'sacrifices' part of pensionable salary<br>• Not suitable for employers with high staff turnover as early redemption charges can be costly<br>• Contracts include use/wear limitations |

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# FLEET FUNDING METHOD COMPARISONS (continued).

| SCHEME | SALE AND LEASEBACK | EMPLOYEE CAR OWNERSHIP SCHEME (ECOS) |
|---|---|---|
| **VEHICLE OWNER** | Leasing company | Leasing company |
| **IS CAR ON OR OFF FLEET'S BALANCE SHEET?** | Off | Off |
| **DOES THE FLEET TAKE THE RV RISK?** | No | No |
| **ARE THERE MILEAGE/ WEAR LIMITATIONS?** | Yes | Yes |
| **ADVANTAGES** | • Releases capital tied up in outright purchased fleet<br>• Removes vehicles from the balance sheet, improving financial ratios<br>• Eliminates RV/maintenance risk and cuts administration<br>• Potentially, the fleet benefits from the supplier's buying power | • Removal of employee BIK tax<br>• Tax and NI savings for employer and (potentially) employee<br>• All the benefits of contract hire but with overall tax savings if properly set up |
| **DISADVANTAGES** | • Careful negotiation needed with the leasing company to agree a resale value for the fleet<br>• Contracts include use/wear limitations | • Complex to set up and run, though leasing company takes on most of the administration<br>• Requires thorough investigation, analysis and external advice to be set up properly<br>• Potential HMRC problems if set up incorrectly<br>• Contracts include use/wear limitations |

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