Business Car Taxation – Guide for Sole Traders & Partnerships

Her Majesty's Customs & Excise carry the slogan *'Tax doesn't have to be taxing'*, however, when it comes to the subject of 'Capital Allowances' and business car taxation, many business owners find it difficult to understand what the rules are.

On 6th April 2009 (1st April for Incorporated Entities), new rules came into force, to encourage businesses to procure vehicles which have a lower 'CO2' emissions rating. In most cases, there are greater tax advantages when you procure a 'cleaner' vehicle, to those vehicles which have a bigger environmental impact.

There are different rules which apply, depending on whether you choose to lease or purchase your vehicle.

Buying a Car

If you are a Sole Trader or Partnership and you choose to purchase a vehicle, adding the vehicle to your business assets, then you will be able to deduct a proportion of the cost of the vehicle from your 'taxable profit' and reduce your tax bill. This type of deduction is known as a 'Capital Allowance'.

When you purchase assets for your business, the value of these assets is placed in a 'pool'. The pool they are placed in is dependent on the amount the asset may be 'written down' against your taxable profit – for example, you may have purchased furniture or a computer for your business, and these assets would be placed in a 'Plant and Machinery Pool'.

If you are a Sole Trader or a Partner in a Partnership, and there is some 'private use' of the vehicle, then the vehicle will be placed in a 'pool' of its own. Under current legislation, this type of business may write down the value of the asset at a rate of 20% per annum, regardless of the vehicles CO2 rating. Then, when it comes to the sale or disposal of the vehicle, the business can claim the difference between the sale proceeds and the current tax written down value – known as a 'balancing allowance'

However, if there is no private use of the vehicle, then the same rules which apply to incorporated entities such as Limited Companies will then be applicable:

Under the recent changes to tax legislation, cars which emit less than 160g/km in CO2 can go into a pool with other plant and machinery. In this 'pool', the cost of the vehicle may be 'written down' at **20% per annum**.

Vehicles which have a CO2 rating of over 160g/km are placed in a **10% 'pool'** with items such as "long-life" assets and "integral" fixtures in building, and it will therefore take much longer to benefit from tax relief on these vehicles.

In both cases, the percentage claimed back will be on a reducing balance basis, so the business will be able to claim less each year as time passes. Then, on the sale or disposal of the vehicle, the proceeds are applied to the respective pool, and no 'balancing allowance' is applicable. This means that some of the tax relief available is pushed into future years, which means that a business could still be claiming relief on a vehicle long after its been sold.

Its also worth noting that vehicles which have a CO2 rating of under 110g/km, businesses can claim 100% of the Capital Cost in the year of acquisition against their taxable profits. This is continuing until at least 2013. ***Note –*** *In order to qualify for 100% tax relief, the vehicle must be unused and not second hand.*

Tip – The general rule for capital allowances have always been that the expenditure is incurred when there is an 'unconditional obligation to pay', providing that it is paid for within 4 months.

Leasing a Car

The magic number to remember is **160**. Vehicles which have a certified CO2 rating of under 160g/km will represent greater taxation benefits than those over this limit.

Vehicle Manufacturers have been working on ways to reduce the environmental impact of the vehicles they produce for many years now, and there are now well over 3,000 different models available which fall under this crucial CO2 limit – including some very popular prestige models including *BMW 3-Series* and new *Mercedes E-Class*.

Tip – It's worth noting that when considering a vehicle which has CO2 emissions close to the 160 mark, some manufacture cost options can actually tip the vehicle over the rating, which could prove a costly error. So it's worth checking with your dealer or leasing company before placing your order.

If the vehicle is under 160g/km CO2 (including those which emit 110g/km or less), then the business may offset 100% of the lease rental payments against their taxable profits.

If the vehicle emits over 161g/km CO2, then there is a 15% restriction on the amount the business can claim against their taxable profits, so just 85% may be recovered.