

development impact on vehicle costs

HBJ Gateley Wareing

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Under plans set out following the Government's recent emergency budget, councils across the country are having to look to save costs wherever possible. Two areas that are of particular note are the system of grey fleet mileage reimbursement and the effect that the forthcoming VAT increase will have on leasing costs.

Grey fleet mileage costs

Local authorities have historically relied on employees to use their own cars for use when on council business (the so-called "grey fleet"). Business mileage covered has tended to be reimbursed at generous allowance rates (at least when compared with comparable private sector rates) and authorities are now under pressure to bring reimbursement rates into line with the official government-approved rates (known as Approved Mileage Allowance Payments, or AMAP rates). Understandably, the authorities which have already proposed changes to achieve this have experienced some difficulties as the AMAP rates are generally significantly lower than those currently offered.

In Derby, council workers went on strike following the announcement of the cash saving measures. In order to resolve the issue Derby Council workers accepted a compensatory lump sum payment for agreeing to the reduced rates.

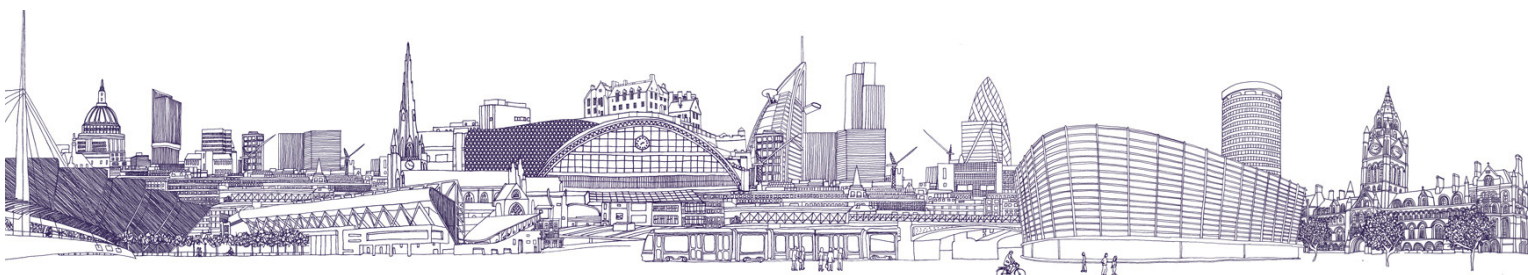
In contrast Hampshire County Council avoided industrial action through direct consultation with employees affected by the rate cuts before announcing their implementation. In this instance, Hampshire County Council was looking to achieve savings on its grey fleet of £1.8 million. By using the consultation process, the council was able to reach agreement on reduced mileage rates and, whilst these didn't achieve the full amount of the savings the council was aiming for, the rates did go a significant way towards meeting the target.

VAT and leasing costs

Also set out in the emergency budget was a proposed hike in VAT from 17.5% to 20%, to take effect on 4 January 2011. This increase is likely to have a significant financial impact on council-run vehicle fleets.

Vehicle leasing companies continue to enjoy advantages under current HMRC practices, which allow them to reclaim VAT on vehicle and equipment purchases. Leasing companies are entitled to do this on the understanding that they will pay the VAT back to HMRC when they sell the vehicle on.

The rise in VAT will mean that, when companies come to sell the vehicles, HMRC will expect to receive VAT reimbursement at a rate of 20% despite the companies purchasing the cars when rates were at 17.5% or even 15%.



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For the leasing companies, the tax increase has the potential to cause a black hole in their accounts which may run into millions of pounds.

In anticipation of tax changes of this type, most lease agreements contain clauses which allow the leasing company to charge the customer for any costs which they incur following a rise in VAT. Some of the leasing companies' biggest customers are council-run vehicle fleets.

The cost implications of the rate-change will bite when vehicle hire contracts come to an end or when vehicles need upgrading. Councils should be aware of this issue now and take the necessary advice to ensure that, where they can, they mitigate any cost implications which will be caused by the rise in VAT.

The continuing drive to make cost savings will be a fact of life for the next few years. It is possible to reduce grey fleet costs by cutting mileage rates. However, this will need to be handled sensitively and in a way which is consistent with the employees' terms of employment. Some care will be needed in handling the legal aspects of changing employment terms and appropriate advice should be sought.

There are potential ways of minimising the financial effect of the VAT increase. It would be advisable to consider the impact that the VAT change will have on lease costs before the new rate takes effect and, if necessary, talking to the authority's advisers on possible avenues for minimising the charge.

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