

Contractor guide to company cars – Part 1: how to calculate if it's worthwhile

Contractors trading through their own **limited company** have the option of running a company car. But the calculation to work out whether it's more tax efficient to personally own a car versus running it through the company is not only complex, but also different for every contractor.

Although contractors using their personal car for business trips can only claim 45p per business mile up to 10,000 miles, and 25p per mile thereafter, this rarely covers the costs of running a car. Conversely, if a contractor's limited company provides a car for both business and private use, they pay income tax at their highest rate on the benefit provided.

"So every contractor's case has to be judged on its own merits," says **James Abbott**, head of tax at contractor accountant **Abbott Moore**. "There is no simple curve over which it becomes cost effective to choose one option over the other."

Calculating benefit in kind (BIK) – the killer variable

Abbott says that the benefit in kind income tax charge is based on the chosen vehicle's list price and rated CO2 emissions in g/km. "For vehicles with emissions at or less than 125 g/km, the benefit in kind is calculated by multiplying the list price of the car by 15%. And the list price should also include any extra features or options."

Then, for every 5 g/km increase in emissions, the charge is increased by 1% and capped at 35%. Diesel vehicles attract a surcharge of 3%, also capped at 35%. Abbott provides an example (all figures, rates and allowances correct at time of publication/based on 2011-2012 rates and allowances):

Step 1 – vehicle details

Volvo V50 SE Edition Diesel D4: on-the-road list price is £24,110, plus metallic paint [an example of an extra feature/option which must also be included] at £565 = £24,675. According to the manufacturer's website, the car's CO2 emissions are 134 g/km.

Step 2 – BIK calculation

The benefit in kind calculation is as follows:

134 g/km [vehicle emissions] minus 125 g/km = 9 g/km

For each 5 g/km increase, the charge increases by 1%, but this is rounded down to the nearest 5 g/km. Because the Volvo V50 model's emissions are 9 g/km above the basic rate of 125 g/km, that means the contractor would only be charged an additional 1% of the list price, plus the diesel loaded supplement of 3%, to make 19%.

[basic charge of 15%] + [additional charge of 1% because emissions are above 125 g/km] + [diesel loading of 3%] = 19%

List price plus optional extras = £24,675 x 19% = £4,688.25 benefit in kind charge.

Step 3 – income tax and employer's National Insurance calculation

Abbott points out this is not what the contractor will actually pay, but the amount on which they must pay income tax at their highest rate:

Standard rate taxpayer: 20% x £4,688.25 = £937.65 to pay

Higher rate taxpayer: 40% x £4,688.25 = £1,875.30 to pay

The contractor's limited company will also pay employer's National Insurance Contributions (NICs) of 13.8% on the benefit in kind, which works out as:

13.8% x £4,688.25 = £646.98

"A contractor must let HMRC know when they have a company car for the first time within 28 days of the end of the quarter end," says Abbott. "The quarters run to 5 April, 5 July, 5 October and 5 January and the notification is made online via HMRC's website. The notification will enable HMRC to amend the contractor's tax code for the car benefit and start to collect the tax due. If there has been any underpayment it will be payable as part of the contractor's annual **Self Assessment Tax Return**."

This means contractors should set aside money for this charge, particularly if HMRC didn't amend the contractor's code promptly or their salary is too low to collect all the tax due.

Step 4 – It doesn't end there – additional benefit in kind for private fuel

Contractors with company cars can claim business mileage at HMRC's standard 'advisory fuel rates', which are typically reviewed each quarter to account for changes in fuel pump prices and vary according to engine size and type. For example, the current advisory fuel rate for the Volvo V50 2 litre diesel used in the example would be 15p per litre.

Business mileage can be expensed with no benefit in kind charge, as it is like any other legitimate business expense. The catch, according to Abbott, is when the company pays for private mileage and fuel: "The benefit in kind charge if a contractor's company pays for their private fuel is a standard £18,800, which is multiplied by the contractor's original benefit in kind percentage calculation."

That means with the Volvo V50, the benefit in kind charge was calculated to be 19%.

The fuel benefit standard benefit in kind of £18,800 x 19% = £3,572

The additional income tax the contractor would pay is calculated by:

Standard rate taxpayer: 20% x £3,572 = £714.40

Higher rate taxpayer: 40% x £3,572 = £1,428.80

Plus employers NICs of 13.8%:

13.8% x £3,572 = £492.94

Before any other calculations are taken into consideration, a 40% taxpayer must therefore pay £1,875.30 [BIK income tax for the car] + £1,428.80 [BIK income tax for fuel] + £646.98 [employers' NIC for car] + £492.94 [employer's NIC for fuel] = £4,444.02.

The final sum – it is worth it?

When deciding whether to have a company car or use their own car for business journeys, contractors should consider:

The costs of the company buying and running the car, plus the personal tax and NICs paid on the benefit in kind, minus the corporation tax savings of buying and running the car and

The corporation tax saving on paying 45p a mile (or 25p when mileage exceeds 10,000 miles) added to the cost of personally buying and running the car.



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Abbott explains: "If 1 is greater than 2, then buying and running the car privately will generally be more tax efficient and financially advantageous for most contractors." In his experience, most contractors are better off buying and running a car personally, but Abbott suggests contractors should ask their accountants to 'run the numbers'.

In the second part of our contractor guide to company cars, Abbott runs through other considerations limited company contractors should take into account when choosing whether to buy and run a company car.

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