LeasePlan

What's next?

Employee Rewards:
The benefits landscape

Introduction

A key component of the relationship between any employer and their workers is a good rewards package. Foremost amongst this is obviously pay, but in recent decades' supplementary reward systems have become increasingly important, in the form of employee benefits that reward performance and motivate employees.

These benefits range from pension contributions and private health insurance to subsidised gyms and workplace nurseries. Many employee rewards take the form of 'benefits-in-kind', and the most significant of these in the UK is the provision of a company car. In 2015-16, the nation's company cars had a combined taxable value of £4.3 billion (excluding fuel and ancillary benefits), easily the highest of any type of benefit-in-kind.

It's clear that such rewards provide considerable advantages for employers and employees, something illustrated by the growth in their popularity over recent decades.

That's why LeasePlan UK has compiled this white paper, which describes the history and features of company car schemes, the ways they operate, the legislative changes affecting them, and the likely ways in which they will continue to evolve and adapt. We hope that it will provide a useful summary of the options available and the advantages that they offer to employers and employees.

In general, employee rewards are more prevalent in the private sector than in public sector organisations. They are particularly popular in industries such as information and communications technology, finance and insurance, and consultancy. Larger companies are also more likely to offer rewards than small and medium-sized enterprises.[1]

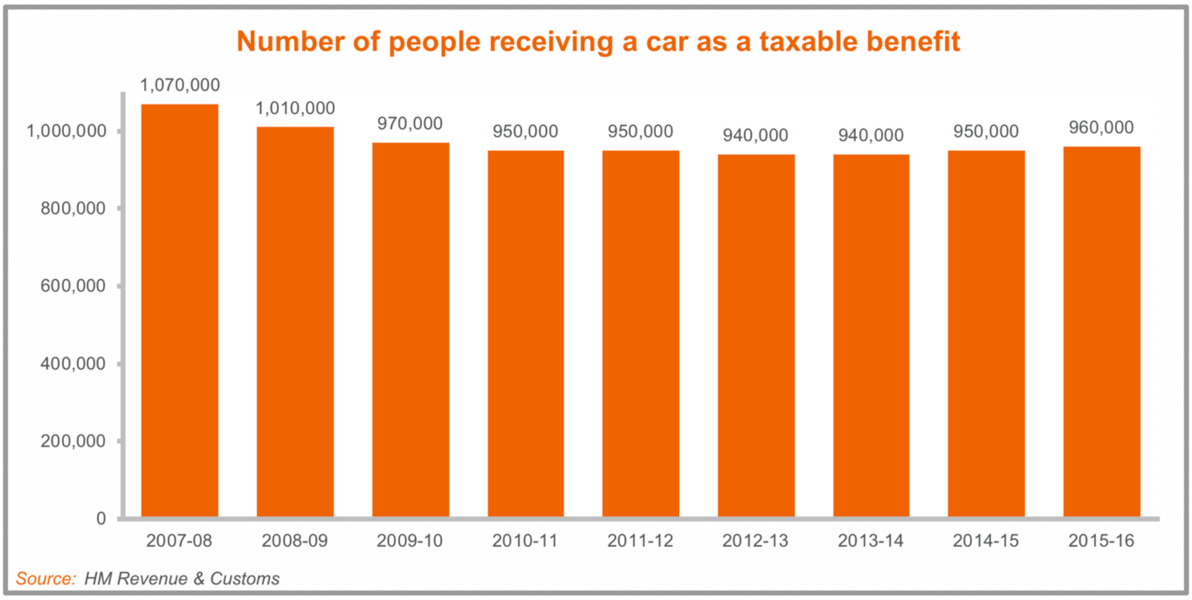
Company cars

The company car really came to prominence following the decision of Edward Heath's Government to freeze pay in November 1972. Employers responded by offering their employees benefits-in-kind, including company cars, instead of pay rises.

In April 1994, a new system of Company Car Tax (CCT) was introduced, with cars taxed on the basis of price, rather than engine size. The taxable value of a car was set at 35% of its list price, with deductions available depending on the age of the car and its annual business mileage. Eight years later, the CCT system was reformed again, and rates have been tied to a car's carbon dioxide (CO_2) emissions since April 2002.

In recent years, the number of company car drivers in the UK has held steady at around 1 million.[2] There was a slight dip in the years immediately after the financial crisis of 2007-08, but the number has begun to tick up again in the last few years. In 2015-16, the last year for which official figures are available, 960,000 drivers were in receipt of a company car as a taxable benefit.

[1] *Changes in remuneration and reward systems*, Eurofound
[2] *Benefits in Kind Statistics: February 2018*, HM Revenue & Customs, T4.5



Why offer rewards?

From the employee's point of view…

For employees, there are several advantages of reward schemes. The most important are:

- **Choice.** A good rewards scheme gives employees the opportunity to set their own priorities about which rewards they value most. The crucial aspect is that the employee is in charge.

- **Flexibility.** Benefit packages offer employees the opportunity to personalise rewards to fit their needs as closely as possible. For company cars, this includes the model of car, how long they keep it, how green it is, and whether to include costs such as insurance and maintenance.

- **Value.** Companies generally have greater buying power than individuals, as well as access to manufacturer discounts that are not available to private buyers. Company car schemes therefore typically enable employees to afford much better cars than they would otherwise be able to obtain.

- **Control.** What's more, every aspect, from specifications to ancillary costs, is consolidated and directly within the employee's control.

From the employer's point of view…

There are also many good reasons for employers to offer rewards, including:

- **Loyalty.** Employees' loyalty and happiness within their firms are significantly improved when they feel valued and have a say in the benefits they accrue at work.

- **Motivation.** Reward schemes offer firms the chance to directly link staff performance to incentives. A well-designed scheme can help to make employees more invested in their work.

- **Recruitment and retention.** An attractive range of benefits is a key component in attracting a retaining the best staff.

- **Image.** From reducing their carbon footprint to engaging in community projects, rewards allow companies to make a public statement about their values and priorities.

The different types of company car

Traditional company car schemes

In traditional company car schemes, the company buys or leases cars itself for employees to use. The most common way that employers provide company cars for their employees is through Contract Hire. The company simply hires the car from a leasing provider for a predetermined period and mileage at a fixed monthly cost. The leasing provider retains ownership of the car, along with all the associated risks, rewards and responsibilities. At the end of the agreed term, the company simply hands back the car and pays any end-of-contract charges.

The benefits of this type of arrangement include low initial costs and fixed monthly payments that make budgeting easy. In addition, neither the employer nor the employee is exposed to the financial risks of car ownership, such as depreciation.

Employee Car Ownership

An alternative way of providing a company car is through an Employee Car Ownership (ECO) scheme. Here, the employee pays a monthly fee to acquire their car, usually from a fleet provider and within a framework specified by their employer.

Usually, an ECO car is supplied via a Credit Sale Agreement, which transfers the title to the employee at the outset. Because ownership of the car passes to the employee, it is not deemed to be a 'company car' for tax purposes and is therefore not subject to CCT. However, it is important that the ECO scheme is structured correctly so as not to fall foul of company car legislation.

Salary sacrifice

A salary sacrifice scheme is an arrangement whereby an employee gives up a portion of their salary in return for some form of employer-provided benefit, such as a car. It has become increasingly popular in recent years and is an integral part of many flexible benefits packages offered by employers.

Typically, the salary sacrificed covers not only the financing of the car, but also maintenance and insurance. Employees can also benefit from their company's corporate buying power to drive a new car at a much lower cost than if they were funding it privately.

The tax treatment of salary sacrifice schemes has changed recently (see below), but employees are still exempt from having to pay National Insurance Contributions on the amount they sacrifice.

Cash allowance

As the tax treatment of company cars evolved, many companies began to give their employees the choice of a company car or a cash allowance in lieu. This gives employees greater flexibility: for example, they can spend less than their full allowance on a company car and take the remainder in extra income, or they can take the full amount in cash and use it to fund a car that is not available from their employer.

However, care needs to be taken when structuring a cash allowance policy, to make sure it does not create too much uncertainty for the company and that it takes into account both current and future legislation. In addition, recent changes to the rules governing Optional Remuneration Schemes (OpRA, see below) have increased the complexity of cash allowance schemes and the administrative burden on companies that offer them.

And, while employees may prefer the greater flexibility of cash allowance policies, employers will find it more difficult to ensure that their drivers have cars that are well-maintained and appropriately insured.

A flexible approach

Different employers and different employees will benefit more from some of these schemes than others. Many companies, recognising that there is no single 'one-size-fits-all' programme, will want to tailor the solutions they offer to meet the changing demands of employees and to offer maximum flexibility.

Such an approach has the advantage of being more likely to offer options that appeal to a wide range of prospective employees, with obvious advantages for recruitment and retention. They also indicate a concern for employee welfare, and account for the differing priorities of staff, whose needs are likely to vary with a wide range of factors. These are not merely limited to the nature of their transport needs, but frequently reflect differing generational priorities.

Legislative changes

Optional Remuneration Arrangements

At Autumn Statement 2016, the Government announced changes to the tax treatment of benefits received through OpRA – either salary sacrifice or cash allowance schemes. The new legislation changes the amount on which employees have to pay Income Tax and employers have to pay National Insurance Contributions. As of April 2017, these levies are imposed on the highest of the taxable value of the benefit and the salary sacrificed or cash foregone.

However, there are some important exceptions. Arrangements that were already in place before 6th April 2017 will not be hit by the changes until April 2021. And ultra-low emission vehicles (ULEVs) – those emitting less than 75 gCO_2/km – will be exempt entirely.

The introduction of this new legislation brings tax implications for many company car schemes, but its financial impact has been limited – and plenty of non-financial advantages remain. However, the changes have created a great deal of uncertainty. In a recent survey, 41% of respondents were unaware of their implications.[3]

Company Car Tax

CCT rates have been rising steadily for several years. In April 2017, the rates for all cars increased by 2 percentage points. In April 2018, they went up by another 2 points for most cars and by 3 for diesel cars, as the diesel supplement was increased from 3% to 4%.[4] In April 2019, all cars will see their rates go up by another 3 points.

In 2020-21, the Government is introducing a new set of CCT bands to create more distinction between different ULEVs and incentivise the uptake of the cleanest cars.

Zero-emission cars will see their rates fall to just 2%. For those with average emissions of between 1 and 50g CO_2/km, the rate will vary from 2% to 14%, based on the number of zero-emission miles that the vehicle can travel. Other ULEVs – those with emissions between 51 and 74g CO_2/km – will be divided into five bands ranging from 15% to 19%. Meanwhile, cars with emissions of 90g CO_2/km or more will see their CCT rates increase by 1 percentage point, up to a maximum of 37%.

The table on page 7 illustrates these changes to CCT by showing the rates for a typical car of each main fuel type over the years 2016-17 to 2020-21:

[3] *Benefits and Trends Survey: January 2018*, Aon
[4] New, cleaner diesels that meet the Real Driving Emissions step 2 (RDE2) standard will not have to pay the diesel supplement.

Company Car Tax rates

Fuel type	CO_2 emissions	2016-17	2017-18	2018-19	2019-20	2020-21
Petrol	120g/km	21%	23%	25%	28%	29%
Diesel	110g/km	22%	24%	27%	30%	31%
Hybrid	70g/km	11%	13%	16%	19%	19%
Electric	0g/km	7%	9%	13%	16%	2%

Source: HM Revenue & Customs

The Government has not yet published the CCT rates for 2021-22 or beyond.

What's next? The future of rewards

The regulatory environment – and not merely that surrounding the tax regime for benefits, but also issues from the minimum wage to legislation on the gender pay gap and pensions – makes it more vital than ever that employee reward schemes offer flexibility, fairness and affordability.

Company cars are a key part of such reward schemes. And they are likely to become more and more important to employers' efforts to attract and retain the most talented staff, particularly at a time when unemployment is low and recruitment of the brightest and best is becoming increasingly competitive.

The kinds of company car that employees drive are changing. Electric and hybrid vehicles are growing rapidly in popularity, and the recent changes to OpRA and the forthcoming changes to CCT create extra financial incentives to choose them.

There may, too, be far-reaching changes to the ways in which people use cars in the near future. Consumers are increasingly shifting from ownership to subscription models for a wide range of products – including cars. The rise of autonomous vehicles will only accelerate that trend.

Whatever the future brings, it will be crucial for firms to continue to emphasise the benefits that they offer to employees – beyond simply the size of their pay packets – and to offer the widest and most flexible programmes they can, recognising the differing needs and priorities of their workforce.

Further reading

- *Comprehensive Guide to Funding and Taxation: 2017*, LeasePlan UK
- *Autumn Budget 2017: Your Guide*, LeasePlan UK

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