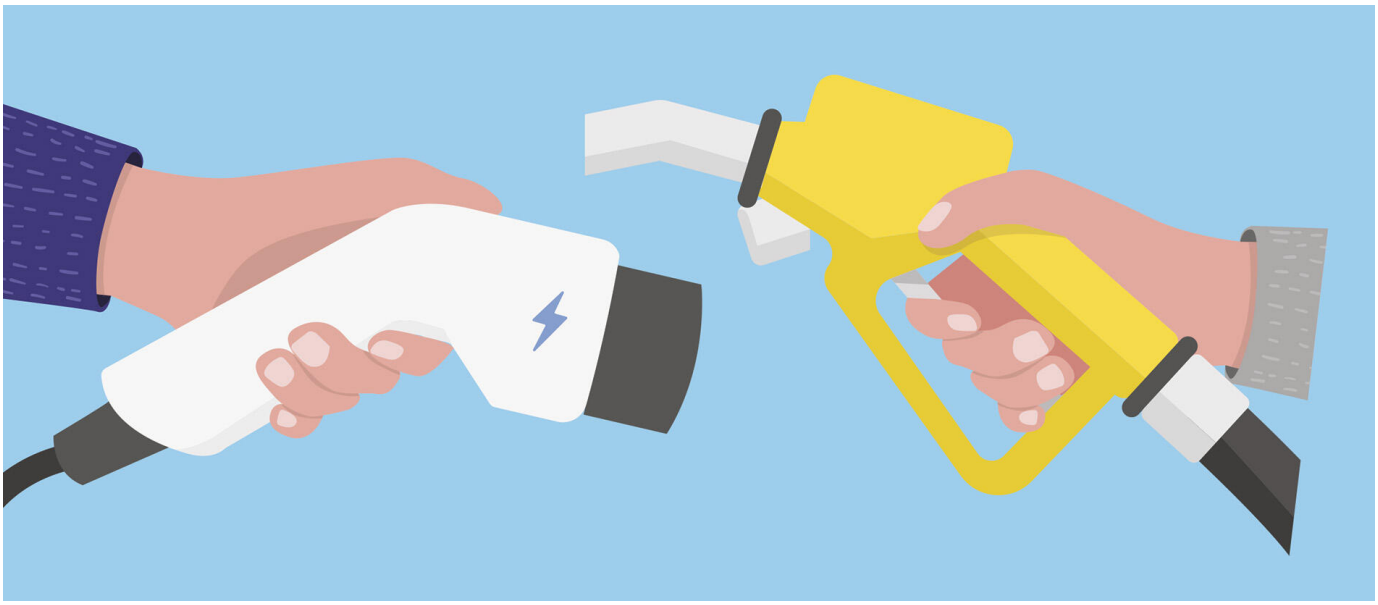
Choosing your lane: tax-efficient vehicle fleets

Large Corporate | Employment Tax | Indirect Tax



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Tax rules increasingly determine the true cost and composition of business vehicle fleets, making planning essential as incentives for electric vehicles fade.

Key Points

What is the issue?

Tax plays a decisive role in shaping business fleet choices, influencing whether companies buy, lease or switch to electric vehicles. As incentives for EVs begin to taper and costs for traditional vehicles increase, the tax environment is undergoing a shift that demands active strategic review.

What does it mean to me?

Fleet managers must navigate multiple interacting taxes – vehicle excise duty, benefit-in-kind, capital allowances and VAT – each affecting cash flow, employee costs and long-term planning. The phasing out of EV advantages and changes such as the reclassification of double cab pick-ups mean businesses can no longer rely on past assumptions about tax efficiency.

What can I take away?

Businesses should regularly review fleet policies, balancing buying and leasing, monitoring classification and allowance changes, and planning for the transition from incentive-based to penalty-driven taxation. Staying agile and anticipating tax shifts will be key to maintaining efficiency and avoiding rising costs as the fleet landscape evolves.

Businesses often underestimate how much tax shapes behaviour. Consider the 5p charge on plastic bags: a minor levy that fundamentally shifted consumer habits almost overnight. In the corporate world, the same principle applies to vehicle fleets. Any new company vehicle will be impacted by multiple taxes, making this an area where purchasers need to take a wider view. Tax rules – sometimes subtle, sometimes sweeping – shape not only how companies procure vehicles but also which types they choose.

From the 1960s, when cars were issued to staff as a way to save income tax, to today’s debates over electric vehicles (EVs) versus internal combustion engine (ICE) models, the fleet landscape is continually reshaped by the tax environment. Today’s tax system is far more sophisticated – designed both to encourage greener choices and to prevent abuse.

Businesses planning a tax-efficient fleet strategy must therefore keep one eye on the current rules and another on future policy. Incentives for EVs were generous when adoption was low, but they are already tapering as electric models move into the mainstream.

Vehicle excise duty

Vehicle excise duty (VED), commonly referred to as road tax, remains one of the simplest but most visible levers that government uses to encourage cleaner

transport. For cars first registered before April 2017, VED is based on CO_2 emissions, with bands ranging from zero (for the cleanest vehicles) to several hundred pounds per year for high-emission models. After 2017, however, the system was simplified into a flat standard rate for most vehicles, with only the first year's tax reflecting emissions, starting at £10 for an EV.

Electric vehicles previously enjoyed a zero rate but this ended in April 2025, when EVs joined the standard regime. As well, while not an immediate issue, Electric Vehicle Excise Duty (eVED) has recently been proposed. This would charge EV owners an additional amount from 1 April 2028 of 3p per mile, or 1.5p per mile for a plug in hybrid, increasing costs yet again. Additionally, EVs with a list price over £40,000 (rising to £50,000 from 1 April 2026) are now subject to an expensive car supplement of £425 per year for five years. Electric vans and light goods vehicles are now subject to the same charges as their ICE models.

For fleet managers, this transition is significant. While VED savings are relatively modest compared to other costs, a fleet of 50 cars could face thousands of pounds in new annual charges once EV exemptions are removed. Whereas staff might once have had more freedom in car selection, now could be the time to introduce a £40,000 limit on the price of any company car. Manufacturers may well factor this into their pricing, and a quick internet search shows the Hyundai Ioniq 5 listed at £39,995 at the time of writing.

Benefit-in-kind

For employees, the real impact of a company car comes through benefit-in-kind (BIK) taxation. HMRC calculates BIK based on the car's list price when new (not the discounted cost the company pays) and an emissions-based percentage. This percentage can range from as little as 3% for fully electric cars to over 37% for high-emission ICE vehicles, with diesel subject to a 4% surcharge (up to the same 37% cap).

The difference created by the rise of EVs is stark. Back in 2015-16, cars emitting up to 50g/km of CO2 were taxed at 5%, with no specific provisions for EVs. In 2025-26, the same ICE car is charged at 15%, while hybrids are taxed across multiple bands based on their electric mileage ranges. Only fully electric vehicles qualify for the lowest rate.

This contrast is striking for drivers still using the same car as 10 years ago, compared to those who have switched to a new EV. An employee with a £50,000 electric company car may pay tax on only £1,500 worth of benefit (3%), while a similarly priced diesel car could generate a taxable benefit of £18,500 – amounting to thousands in extra tax each year for higher-rate taxpayers.

Many employers now offer cars through salary sacrifice arrangements, which fall under the optional remuneration arrangements rules. Under these rules, the value of the benefit will be the higher of the calculated BIK value or the cash forgone. Critically, however, these rules do not currently apply to EVs – further extending their advantages over ICE cars.

Vans, by contrast, attract a flat-rate BIK if available for personal use – £4,020 for 2025/26, plus an additional charge of £769 if fuel is provided for ICE models. Electric vans, by contrast, have no BIK charge. This makes vans far more predictable, though the reclassification of double cabs continues to create complexity (more below).

The difference between cars and commercial vehicles remains a familiar battleground. In simple terms, it hinges on whether a vehicle is designed to carry people or to carry goods, or whether it is not suitable to be used as a private vehicle. Some clients still argue their new car should qualify as a van to benefit from lower BIK rates – the Land Rover Defender certainly springs to mind here. However, Income Tax (Earnings and Pensions) Act 2003 s 115 is written negatively, meaning that anything not specifically excluded is classed as a car. HMRC can, of course, review the same specifications and classifications as everyone else.

Employers should note that Class 1A National Insurance contributions on BIKs can be substantial, making low-emission vehicles doubly attractive. For those wishing to avoid BIK altogether, the vehicle must not be *available* for private use – not merely unused privately. This stricter test catches out many and has been the subject of repeated HMRC disputes.

If company vehicles are not intended for private use, companies should implement and communicate a clear written policy to that effect; otherwise, arguments about lack of insurance or vehicle storage at business premises are unlikely to succeed with HMRC.

Capital allowances

Capital allowances determine how quickly the cost of a vehicle can be written off against taxable profits, and the rules vary significantly depending on the type of vehicle. Under Capital Allowances Act 2001 s 268A, the capital allowance definition of a car is deliberately broad, capturing all vehicles unless they can be excluded, such as vans.

Petrol and diesel cars receive the least favourable treatment. They do not qualify for the annual investment allowance (AIA) or full expensing, and instead can only claim writing down allowances of 18% or 6% per year, depending on whether emissions are above or below 50g/km respectively. As a result, relief is spread over many years, making ICE cars relatively inefficient from a tax perspective.

New electric cars currently qualify for a 100% first-year allowance, allowing the full cost to be deducted in the year of purchase. This makes them far more attractive to profitable businesses seeking immediate relief. However, this favourable treatment is expected to end following the 2025-26 tax year. It was, though, previously due to expire a year earlier but was extended, and perhaps may be again if EV uptake remains below government targets.

Vans and other commercial vehicles are treated as plant and machinery, meaning they qualify for full expensing or the AIA, allowing the cost to be deducted in full. The key exception is double cab pick-ups, which no longer benefit from this treatment.

In practice, this means vans and electric cars deliver immediate tax relief, while ICE cars tie businesses into gradual, long-term deductions. That difference alone can significantly influence fleet planning and the timing of vehicle purchases in a tax-efficient strategy.

VAT treatment

VAT rules around vehicles can be surprisingly nuanced. While the differences between cars and commercial vehicles is broadly similar to that used for BIK purposes, it differs in key ways for VAT. Under the Value Added Tax (Cars) Order 1992, a car is defined as a vehicle that carries passengers, or that has roofed accommodation with side windows behind the driver. This is a positively framed test and, although it often produces the same answer, there are cases where a vehicle is treated differently for VAT and direct tax purposes. That distinction can significantly

affect overall fleet costs.

For most cars, input VAT on purchase is blocked if there is any private use, which in practice means that almost no business can reclaim it. HMRC applies an extremely high bar for proving exclusive business use, and even minimal private use will prevent recovery. By contrast, vans and other commercial vehicles are classed as plant and machinery, allowing full input VAT recovery where the vehicle is used for business purposes.

The treatment changes again for leased vehicles. For cars that are leased and available for private use, businesses can generally reclaim 50% of the VAT on lease payments. If the vehicle is strictly limited to business use, 100% recovery is possible, although proving this to HMRC’s satisfaction can be difficult. Vans are more straightforward: VAT on lease payments is usually recoverable in full.

Depending on the composition of your fleet, input VAT recovery may therefore be 0%, 50% or 100%, either upfront or over time. For businesses making multiple new vehicle purchases, these differences can have a real impact on cash flow planning.

Other vehicles

Most fleets will consist of cars and commercial vehicles, but some businesses use alternative means of transport. Motorbikes, bicycles, helicopters, planes and yachts are all possibilities, depending on the nature of the business. Cars attract the most attention due to their prevalence but what about these other choices?

Broadly speaking, such vehicles are treated as business assets, meaning input VAT can be recovered (subject to private use) and capital allowances claimed through AIA or full expensing where eligible.

The main difference lies in how the BIK is calculated: it is assessed at 20% of the asset’s market value when it is available for private use. For a bicycle, this is a nominal amount; but I had to inform one sailing client that the taxable benefit for the use of a luxury yacht could reach tens of thousands of pounds.

Clients considering alternatives to the company car should evaluate the full tax implications before making a decision.

Double cab pick-ups: the rule change

Historically, double cab pick-ups enjoyed favourable tax treatment. They were classified as commercial vehicles, allowing businesses to claim AIA, reclaim all VAT, and offer employees a predictable flat-rate BIK. As a result, many businesses provided these vehicles to staff even where there was little genuine business need for their capabilities.

From 2025-26 onwards, however, most double cab pick-ups have been reclassified as cars for capital allowance and BIK purposes (after a previous short-lived attempt to do the same). This change significantly reduces their appeal as a fleet option, particularly for businesses that had used them as a tax-efficient compromise between a car and a van.

Some transitional relief exists for vehicles acquired before the end of 2024-25, but for new purchases or leases the rules are clear: tax efficiency now lies elsewhere. One area of continuity, though, is VAT – double-cab pick ups remain classed as plant for VAT purposes, meaning input VAT recovery is still allowed. This softens the impact for businesses that continue to prefer these vehicles.

Fuel and charging

Fuel is another area where tax rules influence behaviour. Company-provided fuel for private use creates a BIK, calculated using a fixed multiplier and the car's BIK percentage. This often turns 'free fuel' into a costly benefit for employees rather than a genuine perk. Employers must restrict input VAT claims to business use, either through detailed mileage logs or use of a scale charge.

Electricity, however, is not classified as fuel and so is treated differently. Workplace charging for employees – whether for company or personal vehicles – is not considered a taxable benefit, provided charging takes place at or near the workplace. Home charging, if reimbursed, may be subject to different rules but overall the tax environment strongly favours EVs, at least for now.

The government has also introduced advisory electricity rates for reimbursing business mileage in electric cars: currently 8p per mile when charging at home and 14p per mile for public charging, similar to the advisory fuel rates for petrol and diesel.

Buying or leasing

The choice between buying and leasing vehicles is one of the most important strategic decisions a fleet manager faces, with tax treatment playing a major role in determining the best approach.

Buying outright – whether through cash or hire purchase – provides ownership and access to capital allowances and input VAT recovery. This can be particularly valuable when acquiring electric cars or vans that qualify as plant and machinery. These allowances enable businesses to offset purchase costs quickly and reduce taxable profits. However, outright ownership ties up capital and exposes the business to residual value risk, especially for new vehicles that depreciate rapidly in their early years.

Leasing offers a different set of advantages. Instead of capital allowances, lease payments are deductible as revenue expenses, spreading tax relief evenly across the life of the lease. For vehicles with private use, leasing also allows 50% VAT recovery – compared with none on purchased cars – making it appealing from a VAT perspective.

Leasing provides flexibility in a landscape where technology, tax rules and environmental policies are all changing rapidly, helping businesses avoid being locked into assets that risk becoming outdated or tax inefficient. That being said, leasing limits control over the vehicle, and businesses are bound by the contract’s duration, with potential penalties for early termination or excess usage.

There is no single right answer to the buy-versus-lease question. Each business must weigh the pros and cons against its own priorities and cash flow needs. Special mention should be made of personal contract purchase (PCP) arrangements, which sit between buying and leasing. Depending on how the deal is structured – especially regarding the balloon payment (the final lump sum needed to take ownership of a car) – PCP can be treated as either a purchase or a lease. It should not be assumed that PCP is equivalent to hire purchase, even if it appears similar.

Regardless of the acquisition method, businesses should also consider their fleet refreshment cycle. A business that refreshes vehicles every three years may be more responsive to changing tax incentives or new technologies, but at higher cost. Conversely, holding vehicles for longer may reduce expenses but risks being left

with inefficient or less tax-advantaged assets, highlighting the importance of timing in fleet planning.

In summary

Tax has always been a powerful tool in shaping business behaviour, and vehicle fleets are no exception. From VED to capital allowances, BIK and VAT, the tax framework determines whether a fleet strategy delivers savings or drains resources.

The current environment strongly favours electric vehicles, offering rapid capital allowances, ultra-low BIK rates and advantageous charging rules. However, this window of opportunity is beginning to narrow. EV incentives are gradually being withdrawn – electric vehicles are not exempt from VED, and BIK rates for EVs are scheduled to rise by 1% each year from 2025-26 onwards.

This raises an important strategic question: once EVs achieve cost and performance parity with ICE vehicles, will the government shift from incentivising EVs to penalising ICEs more heavily? The trajectory suggests that it will. Businesses must therefore plan for a world where ICE vehicles face escalating tax costs, and EVs merely enjoy neutrality rather than special tax treatment.

That said, uncertainly remains. The planned bans on the sale of new ICE vehicles by 2030, and of hybrids by 2035, continue to face political and industry resistance. Is it possible the government of the day will extend the transition period to allow more time for businesses to adapt? The reclassification of double cab pick-ups has also reinforced this broader trend, pushing companies and employees away from vehicles that no longer deliver tax advantages.

Businesses should therefore:

- review fleet policies regularly in light of evolving tax rules;
- consider a mix of buying and leasing to balance tax efficiency and flexibility;
- pay close attention to classification changes, such as double cab pick-ups;
- plan fuel and charging strategies to minimise BIK exposure; and
- align fleet replacement cycles with anticipated tax changes.

Sometimes clients will just ignore our advice. A company director once asked me how to replace his car while keeping both company and personal taxes low. After

explaining all the rules and explaining how electric vehicles offered the most efficient route, he eventually decided he simply liked the Lamborghini hyper car, regardless of the tax. Cars can be emotional purchases, and sometimes logic takes a back seat. For most, however, a tax-efficient fleet strategy requires not only understanding today’s rules but also anticipating those to come.

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