



**salary sacrifice**  
schemes for cars:  
decision maker's guide

## Introduction

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Salary sacrifice schemes for cars have attracted increased levels of interest from fleets and the media over the past couple of years. Such schemes have the potential to deliver cost savings to organisations, and offer a cost-effective benefit to employees.

In our experience of working with fleets we have found that organisations are familiar with how generic salary sacrifice schemes work. However, salary sacrifice for cars is less well understood, and typically organisations underestimate what is involved and the areas of potential risk.

This publication gives an overview of salary sacrifice schemes, and sets out the areas you need to consider before implementing a scheme. It is not intended to constitute financial or other professional advice and you should always consult your professional advisors regarding tax and associated matters.

This guide will answer the following questions:

- ✔ What comprises a salary sacrifice scheme for cars?
- ✔ What are the potential benefits for the employer and employees?
- ✔ What are the risks and potential drawbacks?
- ✔ How can you ensure you operate an efficient, tax compliant scheme?

## What is a salary sacrifice scheme?

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A salary sacrifice scheme allows an employee to surrender part of their salary, under the terms and conditions of their employment, in return for the employer's agreement to provide a non-cash benefit.

Because the cost of the non-cash benefit is deducted from the employee's gross salary, before statutory deductions, their income tax and national insurance contributions are reduced.

Salary sacrifice has historically been used as a general method of improving employee remuneration, for example through the provision of child care vouchers or bicycles. Recently, there has been increased interest in providing cars via such an arrangement. There are two reasons underlying this trend. First, in 2008 a 10 per cent Benefit in Kind tax band was introduced for company cars with CO<sub>2</sub> emissions under 121 g/km, which helped organisations to design cost-effective salary sacrifice schemes. Second, in the current economic climate, organisations have to find innovative ways to reduce costs while attracting and retaining employees.

### **Savings generator or staff benefit?**

Most organisations explore such schemes due to the potential savings they believe are available. Others view them as a way of enhancing their employee benefits package to attract and retain staff. A well planned and implemented scheme can meet both of these objectives. Initially, there are two steps to take:

- ✔ Determine your objectives clearly. Which is more important – savings for the organisation or staff benefit?
- ✔ Undertake research to determine the suitability of a scheme, potential audience size, how best to manage and communicate the scheme, and potential costs and carbon savings.

The study should cover all areas of risk and identify solutions to mitigate them.

## Potential benefits

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### For employers

**There are three key areas in which a salary sacrifice scheme for cars can potentially deliver benefits to the employer:**

#### **1. HR**

- ✔ Significantly enhance the total benefits package
- ✔ Support employee recruitment and retention
- ✔ Provide an 'all employee' benefit
- ✔ Bespoke schemes can be tailored to individual corporate needs

#### **2. Financial**

- ✔ Reduce salary and National Insurance costs
- ✔ Control salary costs via the effective use of flexible benefits
- ✔ Lower business mileage reimbursement costs

#### **3. Corporate Social Responsibility**

- ✔ Improve compliance with Health and Safety and duty of care legislation
- ✔ Reduce employee travel carbon footprint by encouraging move from older, less efficient grey fleet vehicles to safer and more efficient vehicles

### For employees

**The benefits for employees entering a salary sacrifice scheme include:**

- ✔ Access to a new car every three to four years, usually at a lower cost than other methods of new vehicle provision
- ✔ Typically no deposit or credit checks and no impact on personal credit
- ✔ Tax and National Insurance liabilities are reduced as payments are deducted from gross salary
- ✔ All inclusive, hassle free motoring at a fixed monthly cost. This can include servicing and maintenance, breakdown and recovery, road fund licence, fully comprehensive insurance, replacement tyres and accident management
- ✔ Access to a tax efficient second or third car

## Potential risks

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### For employers

#### The employer needs to consider the following:

- ✔ There may be a delay between the organisation paying the leasing company for the vehicle and collecting the sacrifice from the employee's salary, which can impact on cash flow.
- ✔ Adding the lease cost of several vehicles may impact on the ability of the organisation to arrange credit elsewhere.
- ✔ Unforeseen changes to HMRC tax rules.
- ✔ Employee resignation, redundancy, maternity/ paternity leave, or long-term sickness may lead to a charge for early termination of a vehicle contract. Bear in mind that, as the employer is leasing the vehicle on behalf of the employee, any such charge will be invoiced to the employer, and these costs can be significant.
- ✔ Excess mileage charges or the cost of unfair wear and tear damage will be invoiced to the employer. A contingency fund can help mitigate against these risks.
- ✔ The majority of salary sacrifice schemes include motor insurance, typically by extending the organisation's existing vehicle policy. Adding vehicles to the policy may lead to increased premiums.

### For employees

#### There are three key areas which must be considered before joining a scheme:

- ✔ An employee who joins a salary sacrifice scheme when they previously used their own private car for business purposes will experience a reduction in their business mileage reimbursement rate.
- ✔ Employees joining a salary sacrifice scheme may be subject to company car tax for the first time and will need to understand how this relates to the CO<sub>2</sub> emissions and P11d value of their chosen vehicle. The cost of company car tax will increase during the time the employee has use of the vehicle – for more information please refer to our free publication [Company cars: a guide for drivers \(pdf\)](#).
- ✔ Entering into a salary sacrifice scheme for cars can affect other areas including working tax credit, child tax credit, child maintenance payments, student loan repayments, mortgages and occupational pensions.

Whilst there are benefits to be enjoyed by both employer and employee from implementing a scheme, there are also risks that need to be considered by both parties. This is an area that, in our experience, some organisations overlook.

## Know your audience

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**It is important to understand the potential rate of uptake in order to estimate the savings that the scheme can deliver.**

A well-structured scheme, complemented by an effective communication campaign, could achieve anything between three per cent and 10 per cent take up in the first year, although some organisations predict up to 15 per cent.

It is crucial to understand the difference between the total number of employees in your organisation and the true level of your employee base from which you can estimate the likely take up. The current employee profile of your organisation will determine the true scheme audience and therefore the likely take up.

For example, using an estimated take up of 10 per cent, if you currently have 1,000 employees in your workforce, you should not assume that 100 employees will take a car through the scheme. Certain sections of your employee base will either not be eligible or will not be interested due to their personal situation.

Employees cannot sacrifice salary to a level that it takes them below the national minimum wage. Therefore, the number of part-time and low income workers needs to be considered. Similarly employees cannot sacrifice salary if they have no salary to sacrifice, so employees within three years of retirement may be ineligible. Alternatively, an early termination fee may be payable.

Adjustments should be made to account for the natural staff turnover rate as well as the number of employees who typically take maternity and paternity leave each year. If an employee who has joined the scheme then takes maternity leave, you may be responsible for covering the cost of the vehicle, but a contingency fund can help to offset these costs.

## How much will your organisation save?

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Once you understand the true potential audience for a salary sacrifice scheme, you are in a position to estimate the likely savings.

There are a number of assumptions that make estimating the savings difficult. These include:

- ✔ True scheme audience – calculations must be based on the true scheme audience, rather than on the total employee population.
- ✔ Vehicle choice – it is impossible to predict which vehicles employees will choose, and therefore the level of salary that is to be sacrificed.
- ✔ Any restrictions within the scheme policy – such as whether it is open to all employees or just as a company car replacement option.
- ✔ The average salary of the participating employees – participants may be primarily higher earners maximising the tax benefit or lower earners gaining access to a new car.
- ✔ Whether employees are using the scheme to acquire their primary vehicle or as a cost-effective way of operating a second car.

A scheme provider should be able to estimate potential savings on your behalf based on existing lease rates and example staff profiles.

## Scheme design

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Having considered all of the areas highlighted so far, your next step should be to consider how the scheme will operate.

Areas to focus on include:

- ✔ Whether to operate the scheme internally or outsource to an external operator. In the latter case, how to select a provider.
- ✔ In joining a salary sacrifice scheme, an employee will forfeit their contractual right to a proportion of their salary in return for the car benefit. HMRC will want to see that both employment contracts and employee payslips have been revised appropriately. We recommend reading the [HMRC guidance on salary sacrifice](#).
- ✔ Any restrictions you wish to place on the vehicles that employees can choose, in terms of the types of cars and their CO<sub>2</sub> emissions.
- ✔ Employee guidance to explain the benefits and risks to potential participants.
- ✔ Scheme communication and promotion.

## Alternative salary sacrifice scheme structures

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There are three different approaches to structuring a salary sacrifice scheme for cars:

1. Set the rates as 'employer neutral' and pass all the savings onto the drivers as a benefit to the employee.
2. Allocate some of the savings to your organisation and recoup some of this money from the employee. This can help to build a contingency fund to mitigate against some of the potential risks.
3. Set the drivers' salary sacrifice as the same amount as the monthly rental for their chosen vehicle. The employees will still enjoy savings, and a proportion of these are passed to the organisation.

**We recommend discussing these options with your selected scheme provider to see how they may be able to meet your specific objectives.**



## Case study

In 2012, a leading university engaged the Energy Saving Trust to produce a feasibility study for the implementation of a salary sacrifice scheme for cars.

The key findings in the report were:

- ✔ The Benefit in Kind percentages from tax year 2013/14 favour a scheme offering sub 100 g/km cars, while still enabling employees to select from a wide range of cars that meet their requirements.
- ✔ The rate of uptake depends on scheme communications and promotion and could be as low as one per cent if these factors are not properly considered.
- ✔ Although there is a wide range of potential savings to the organisation, the calculations yielded an indicative cost saving of £35,000 to £40,000 over three years per one per cent of eligible staff entering the scheme.

The tables show the financial implications of a basic rate (20 per cent) tax payer taking a BMW 116d Efficient Dynamics diesel for three years, with the employee's sacrifice equal to the lease rental. The vehicle has a P11D value of £21,040, CO<sub>2</sub> emissions of 99 g/km and a combined MPG of 74.3.

### Employer costs/savings

	2013/14	2014/15	2015/16
Net rental cost	£2,405	£2,405	£2,405
Net maintenance cost	£232	£232	£232
Class 1A NIC on benefit	£406	£436	£494
Insurance and admin	£720	£720	£720
Salary sacrifice	£3,764	£3,793	£3,851
NI on salary sacrifice	<b>£519</b>	<b>£523</b>	<b>£531</b>
Receipt from employee	£3,244	£3,270	£3,320
<b>Employer savings</b>	<b>£0</b>	<b>£0</b>	<b>£0</b>

### Employee costs/savings (20 per cent tax payer)

	2013/14	2014/15	2015/16
Salary sacrifice (SS)	£3,244	£3,270	£3,320
Income tax saved on SS	<b>£649</b>	<b>£654</b>	<b>£664</b>
NI saved on SS	<b>£389</b>	<b>£392</b>	<b>£398</b>
Income tax on car benefit	£589	£631	£715
<b>Net cost to employee</b>	<b>£2,795</b>	<b>£2,854</b>	<b>£2,793</b>

## Summary and conclusion

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This guide has illustrated that you need to look at more than the headline potential savings on offer in order to plan and implement a successful salary sacrifice for cars scheme. The key steps are:

- ✔ Be clear about your reasons for offering a salary sacrifice scheme, and research the suitability of any scheme for your organisation.
- ✔ Ensure you and your employees understand the potential benefits and risks that are associated with salary sacrifice schemes.
- ✔ Work with your scheme provider to estimate the true potential audience, and the realistic savings that could be achieved.
- ✔ Design a scheme that is robust, HMRC-compliant, and properly communicated to the target audience.

## Further information

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[HMRC full guidance on salary sacrifice \(pdf\)](#)

[HMRC salary sacrifice Q&A](#)

[Company cars: a guide for drivers \(pdf\)](#)

[Energy Saving Trust fleet advice and consultancy services](#)

**Energy Saving Trust**

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