

# CBS perspective

## The HR challenges of ECO implementation

For companies considering implementing an Employee Car Ownership ("ECO") scheme, it is widely recognised that the first stage of the process involves the completion of a detailed Feasibility Study which includes the design of the proposed technical structure of the scheme and the financial consequence to the business arising from its introduction. As part of an overall change management initiative, this particular work stream is normally led by finance, tax and legal experts. Once completed, however, there is traditionally a shift in the responsibility for successfully implementing the ECO towards the Human Resource function.



The initial task for the HR community is to design and develop a scheme policy for the eligible employees and, as with all aspects of the ECO implementation, this process must also give due consideration to those employees who may elect to receive a 'cash alternative'. The policy needs to be definitive and should extend to give due consideration of all aspects of

the arrangements ranging from proposed contract parameters around term and mileage to whether or not new recruits should take reallocated vehicles and potentially how to accommodate participating employees on maternity leave or long-term sickness absence.

With the scheme architecture in place and HR policies defined, the next step is for the level of employee benefit to be set. The level of the benefit is usually influenced by the overall objective of the ECO. This could be to maximise savings for the employer, protect employees against rising company car tax or possibly to realign the employee benefit to the specific labour market. The level at which the employee benefit is set is almost entirely up to the employer, with few

legislative considerations restricting the boundaries they must work within. In terms of minimising the potential complexity of individually tailored calculations, it is advisable to reference the employee's basic contribution not on the company car tax previously payable, but instead to a basket of typical vehicles for their grade/entitlement level.

In addition to the basic allowance levels and corresponding contributions from the employees, the employer must also decide on the overall level of support they wish to offer in the operation of their ECO scheme. For example, will the company support the employee in the event of an early termination or excess mileage charge and who pays for and provides motor insurance? This latter point is particularly important. With the daunting prospect of corporate manslaughter claims now such a serious risk, employers have to be satisfied that employees making business journeys are adequately insured. It is not surprising that an increasing number of companies operating ECO arrangements now include motor insurance as part of the benefit and in many cases this policy is being extended to cover those employees deciding to take cash.

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## Managing Directors Viewpoint



Martin Maguire  
Managing Director

CBS recently carried out a national Car Benefit Survey. Throughout the UK, 550 car fleet operators were surveyed and the results have given an insightful perspective into the state of fleet provision in the UK's major companies. The results have also highlighted the key concerns and issues facing both employees and employers.

The immediate message from the survey is that company sponsored car benefit is here to stay! Over 50% of respondents felt that the provision of a car benefit is an essential tool for recruitment and retention of staff and that it would always be considered part of the remuneration package. The respondents concern with fleet provision however lies in the actual efficient delivery of the benefit.

The survey results showed that health and safety compliance is becoming increasingly critical and was deemed of greater importance than both enhancing the level of benefit to employees and ensuring that employees do not have any benefit-in-kind issues. CBS believe that this trend will increase with the planned introduction of corporate killing legislation.

The research finds that half of respondents source and fund their fleets via multiple options. Still the most popular choice for procuring company car fleets is Contract Hire. Outright purchase is also still popular although this is likely to reduce as companies introduce performance measurement criteria which will ultimately force car fleets off the balance sheet.

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# Topical Issues in Focus

One of the key benefits of restricting vehicle choice is that subsequent reallocation of vehicles is usually much easier. On the other hand, a reduction in choice is often seen as a reduction in benefit.

## Company Car Tax - Who really pays?

With the migration to diesel vehicles in the wake of the introduction of emission-based tax assessment reaching almost epidemic proportions, it is becoming increasingly the case that employers are effectively suffering creeping vehicle related overheads as a result of company car drivers looking to minimise their individual liabilities.

This phenomenon stems from a fundamental premise. Despite the fact that diesel cars cost more to buy than their petrol equivalents, historically their whole life costs were comparable due to the combination of lower servicing costs and higher residual values. As a consequence of the more frugal diesel fuel consumption,

## ECO - Vehicle Choice

It is a common misconception by employers and indeed motor manufacturers, that a switch to an ECO means an unrestricted choice of vehicle for the employee, something that not all employers wish to promote.

The reality however can be quite the opposite, as ECOs can be implemented with as much or as little vehicle choice as the employer desires. The ECO structure determines the delivery method of the car benefit and the financial efficiency of providing it. Around this structure, the employer can fit almost whatever policy regarding vehicle choice that they wish.

The choice available to an employee can be managed in different ways. An employer may choose to define what they deem to be a suitable vehicle, thus excluding vehicles that they would prefer their employees did not to drive, such as convertibles. This policy can also be applied to cash takers who by virtue of taking cash usually have greater flexibility in their vehicle choice.

Alternatively, the employer may simply select the vehicles available to choose from. This can, for example, allow a single badge arrangement to continue under the efficiency of an ECO structure.

# CBS Poll

In each issue of the CBS Perspective we will be posing a topical question and asking for your opinion. This issues question...

*From a Health and Safety perspective, what is of most concern to you?*

- 1 High business mileage
- 2 Employees taking cash and buying second hand cars
- 3 Drivers not having undergone driver training
- 4 Ensuring cars are maintained correctly
- 5 Employees selecting high risk cars

Register your opinion by submitting your vote on our website  
[www.carbenefitsolutions.co.uk](http://www.carbenefitsolutions.co.uk).

The results of this poll will feature in the next edition of CBS Perspective. Remember, your opinion counts!

### Results from previous CBS Perspective's topical question

In the last edition of CBS Perspective, the Poll question asked fleet and benefit decision makers "What is the most important objective you have with regard to delivering a car benefit to your employees?"

The clear message from the poll was that cost is still the number one concern for companies offering a car benefit with reducing the direct cost and also the reduction of the administration overhead being by far the most popular responses. These findings are supported by the results of the Car Benefit Survey conducted by CBS in November 2004.

The next most popular response was to protect employees from benefit in kind increases. This reflects employers' experience of employees either incurring increasing tax costs since the introduction the CO<sub>2</sub> emissions based tax charges or having to choose cars with a perceived lower benefit in order to keep their tax costs down.

The objective of having control over employees choice of car scored higher than providing a hassle free benefit to drivers. The rationale appears to be twofold. Firstly, benefit providers believe that it is easier to control costs by restricting the choice of cars offered to employees mainly through discount arrangements. Secondly, there is increasing awareness of health and safety issues relating to employees driving on company business and related insurance costs. ■■■



## ask the expert

If you have a question you would like to ask our experts, please forward it to:-

[mail@carbenefitsolutions.co.uk](mailto:mail@carbenefitsolutions.co.uk),  
alternatively visit our website.

This issues questions include;

Lots of potential providers we have spoken to about sponsored ECO implementation have stated that it doesn't work for low business mileage users. Would you agree?

The short answer is not necessarily. This is a common misconception but it does depend on the benchmark cars and the



additional economies for the employer were realised from the sub-population of those essential user drivers who cover high levels of business mileage.

Demographic research has highlighted that some 40% more company car drivers are currently selecting diesel vehicles due to their low carbon dioxide emissions than was the case prior to 2002. This makes sound economic sense for the drivers in question but what about their employers? Such a dramatic supply shift is not lost on those who take risk against predicted future values of vehicles to the extent that the previously mentioned residual value

level of depreciation due to mileage. By striking a happy medium between a 'one size fits all' approach to contract parameters (i.e. term and mileage combinations) and the undesirable alternative of bespoke individual contracts and corresponding cash allowances, it is possible to manage costs efficiently for perk drivers under ECO such that their participation is not compromised.

By definition, perk drivers will travel less miles than their essential user colleagues. Many employers think that because perk drivers have low business miles, this means that 'like-for-like' their allowances will suffer unacceptably punitive engrossment costs due to the inability to pay the allowance via the free-of-tax AMAP mechanism.

However, by ring-fencing perk drivers and writing generic contracts on a lower mileage than their colleagues, the operating cost of vehicles is reduced such that the quantum of allowance falls, suppressing the engrossment costs that historically have given financial concerns, especially in the case of higher rate tax payers.

In your opinion, what is an average uptake amongst eligible employees when introducing an ECO scheme?

This will ultimately depend on how the scheme is perceived by the employees when compared with both legacy arrangements and car benefit provision that is in place with your competitors!

Accepting that many employers offer a 'gross cash' alternative under their company

premium compared with petrol cars has all but disappeared with the result that monthly lease costs are on the increase. This coupled with the fact that the typical business mileage for a diesel driver is now substantially lower means that the marginal economies previously attributable to high business mileage are also under challenge.

One potential upside to the employer in the current climate could be attributable to the ongoing provision of fully expensed cars, i.e. those that feature private fuel benefit (the popular terminology 'free fuel' is both misleading and factually incorrect). All other things remaining equal, the more drivers who select diesel cars as their choice of company vehicle, the less private fuel is likely to prove attractive as a benefit due to the increased threshold of private mileage required to effectively 'break-even' when compared with the considerable tax liability associated with this increasingly unfashionable benefit. Where this is the case, drivers are better off surrendering their entitlement and will effectively save money by paying for their own fuel for private use. As such, employer costs are

car policies that would not constitute an ECO scheme, in our experience and opinion, uptake levels are critically dependent on the schemes design structure, of which there are three main types.

### 1. Sponsored ECO Schemes

Description: The employer designs a structured car scheme for those with car benefit entitlement with the objective of absolutely replicating the 'look and feel' of company cars in the most tax efficient manner. Typical uptake is 90%-98%.

### 2. Unsupported / 'Arms Length' ECO Schemes

Description: The employer offers cash allowances and access to a preferred supplier capable of delivering vehicles under bespoke term and mileage contracts. Unlike the sponsored scheme described above, employees are not 'held harmless' to potential costs arising from early termination or excess mileage charges. Typical uptake is 50%-60%.

### 3. All Employee / Affinity ECO Schemes.

Description: Employees (including those without car benefit entitlement) are offered the ability to source a vehicle and optional services from a nominated supplier with whom preferable terms have been negotiated by the employer. Typical uptake is 2%-5%. The percentages above are purely indicative. ■■■

reduced to zero but not without a little education in the discipline of financial gymnastics with the drivers first!

CBS recently designed and implemented a structured ECO scheme that delivered a 'win-win' to employer and employees alike. In recognition that some petrol vehicles had lower whole life costs than their diesel counterparts (excluding fuel), employees where given access to a choice of either but had their contribution based on the diesel tax liability. Irrespective of their choice of vehicle, employees were reimbursed for business fuel at the diesel rate, thereby managing the businesses fuel cost without compromising employee choice and importantly creating an environmentally sensitive policy that suppressed the potential for unnecessary trips where employees perceive the fuel reimbursement policy to be generous. The result? The best of both worlds for the economic family. ■■■

## The HR challenges... Cont.

At this stage in the implementation it is recommended that the original financial analysis is revisited. This is to ensure that, following the development of the scheme policies and setting of employee benefit levels by the HR community, future fleet costs remain at the desired levels.

Possibly the most crucial step in the implementation process is the communication of the ECO to the business and particularly to the eligible employee population. If poorly communicated, many employees could easily feel confused, concerned or even sceptical and suspicious about the objectives of the ECO. The burning issue is how it will affect them personally. It is widely recognised that not all employees are receptive to change (particularly where such an emotive benefit is concerned) but these negative emotions can easily be avoided with clear, concise, open and timely communication.

The communication strategy, which would normally encompass a variety of media, is heavily influenced by the transitional arrangements to be adopted by the company. For example, a transition based on the normal replacement cycle of vehicles may require a less intensive but lengthier communication process, than that of a 'big bang' approach where vehicles are refinanced into the ECO immediately. The transitional arrangements adopted are usually dictated by financial factors normally outside the control of the HR community.

It is clear to see that the role of the HR community is central to the successful implementation of an ECO. As such, it is equally vital that they seek, and are provided with, the necessary guidance and support by their ECO provider not only throughout the scheme's implementation but also on an ongoing basis. ■■■

The results also show that 10% of respondents fund their vehicles via ECOs, a percentage that is ever increasing. The fleet industry believes that up to 70,000 cars will be provided under an ECO scheme in 2004 compared with 25,000 in 2002. However, the fleet industry uses the term "ECO" very loosely and applies this term to both basic Personal Contract Purchase (PCP) arrangements as well as highly tax efficient structured schemes which are usually implemented by blue chip organisations.

Nearly half of respondents admitted to only conducting a fleet review in response to a specific problem. With the introduction of new compliance issues, it is imperative to be proactive as it is very

easy to either be operating a fleet in a non-compliant manner or miss opportunities to operate the fleet more efficiently from an administrative or savings perspective.

Although implementing a successful company provided car strategy through the maze of options available is not an easy task, if it is done properly, it can be tremendously beneficial for both the employee and employer. Careful navigation through the multitude of compliance issues and prudent monitoring of all health and safety rulings over the next twelve months will ensure your fleet and employees are well serviced and well protected. ■■■

## ■ Pre-Budget Report Review

In his Pre-Budget Report issued in December 2004, the Chancellor set out a number of measures that will impact on the provision of company car benefits to employees. The measures, which generally reflect the Government's objective of promoting environmentally friendly policies, are summarised below:

- The Government announced its intention to simplify the alternative fuel discounts for company car tax in the 2005 Budget to make the use of low emission fuel cars more attractive to company car drivers.
- From April 2006 the waiver of the 3% diesel supplement for diesel cars that meet the Euro IV emissions standards will cease for cars registered on or after the 1st January 2006. This reflects the loss in tax revenue due to a significant increase in the number of employees selecting diesel cars and the rate at which the motor industry has been able to develop and supply Euro IV compliant cars.
- The basis of capital allowances is being reviewed to encourage the take up of low emission cars by possibly linking the level of capital allowances to CO<sub>2</sub> emissions.
- It is proposed that VAT fuel scale charge for employees receiving private fuel benefit will be aligned with the company car benefit charge, i.e. away from engine cc to CO<sub>2</sub> emissions based criteria.

### EU VAT ruling means companies could face increasing costs

The Advocate General for the European Court of Justice gave an opinion in December 2004 supporting the EU challenge of the UK's interpretation of the European 6th Directive on VAT. Currently HMC&E allow businesses to claim VAT on business expenses which have been paid for in the first instance by employees then claimed back through expenses. If the EU challenge is upheld, VAT can only be recovered on items purchased directly by companies.

The most common business expense to which this challenge applies is reimbursement of fuel for business mileage. Fuel bills could increase by 16p per litre if companies did not change their method of procuring business fuel. This increase in costs could be avoided if employees are provided with company charge cards although this means changes to administration processes.

The opinion is not binding but in four out of five ECJ cases the judge rules the same way as the Advocate General. The judgment is expected sometime in 2005. CBS will keep you advised of the developments in this case. ■■■

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## Do **YOU** have permission to carry out regulated insurance activities?

New regulations governing selling and other intermediary services relating to regulated insurance activities came into force on 14th January 2005. In accordance with the Financial Services and Markets Act (FSMA) 2000, all parties wishing to act as insurance intermediaries for regulated insurance activities must be either directly authorised to do so by the Financial Services Authority (FSA) or be an Appointed Representative of such an Authorised Person.

What constitutes a regulated insurance activity is very widely drawn. For example, providing breakdown and recovery services is a regulated insurance activity as is claiming under a manufacturer warranty under ECO arrangements where an employee owns the car but the claim is made by the finance company.

The above regulations are mainly apply to leasing companies who provide Contract Hire and support ECO arrangements. However, these regulations are of equal concern to those companies who have set up their own internal finance company to provide an ECO to their own employees.

It should be noted that failure to comply with these requirements can result in fines for the companies providing regulated insurance activities without the proper authorisation and potentially imprisonment for their directors.

The CBS group has authorisation from the FSA to carry out regulated insurance activities from 14th January 2005. In addition, CBS is able to offer services to clients to assist them in ensuring that they fully comply with the regulations. ■■■

## Next Edition

The next edition of the CBS Perspective will be available in April 2005.

If you would like to submit a question or discussion topic please send them to us at [mail@carbenefitsolutions.co.uk](mailto:mail@carbenefitsolutions.co.uk).

You will find the result of our CBS Poll in the next edition and on our website at [www.carbenefitsolutions.co.uk](http://www.carbenefitsolutions.co.uk).

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