Lex Autolease

Best Practice Guide

Reducing your fleet costs.

BP MAR 10

Significant costs.

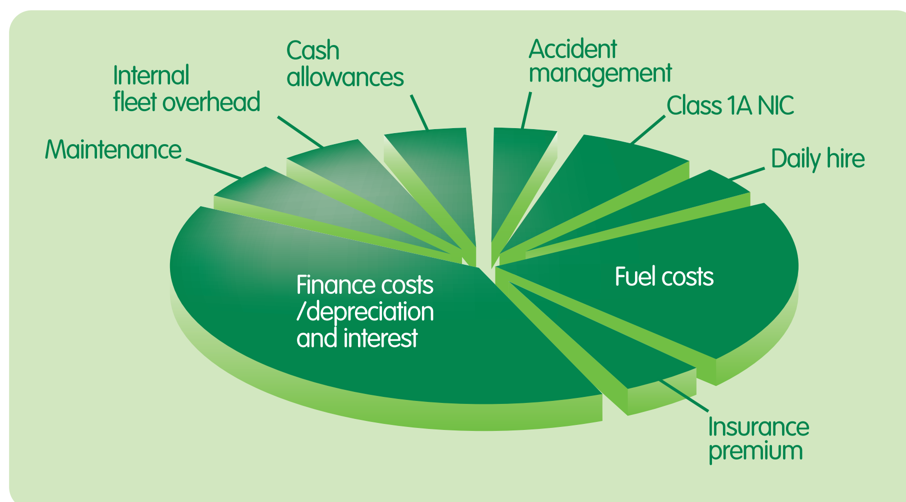
Company car and van fleets are often non-core areas of an organisation so reducing fleet costs may not necessarily be a key focus for directors and senior management.

However, the costs associated with fleet can often be a significant part of the organisation's profit and loss statement, especially in organisations within support services, construction, telecommunications and technology.

An example of the parts which make up fleet costs is shown in the chart below. Please note: the relative cost percentage is likely to vary between different organisations – for example, some may have a higher proportion of cash takers, or provide employees with private fuel, which will correspondingly increase these segments relative to other cost categories.

Typically, annual fleet costs represent £5,000 – £10,000 per vehicle (pre-tax) when all these elements are taken into account.

The actual cost will also be significantly impacted by car policy, for example, whether private fuel is paid, and whether there is a generous level of car or cash allowance offered to senior employees.



There are six main areas to focus on when looking at reducing fleet costs:

1. Fleet funding. Is your funding method efficient?
2. Manufacturer discounts. Are you offering your staff too much choice?
3. Car policy. Have you considered reviewing your car policy terms?
4. Fuel and National Insurance Contribution (NIC) savings. Are you managing the provision of fuel effectively?
5. Operational fleet model. Have you considered your operational fleet model?
6. Risk management. How can you minimise your risks and reduce costs?

1. Fleet funding.
Is your funding method efficient?

If your internal rate of return (IRR) for investment decision making is around 6% or greater then it would make financial sense to run some discounted cash flows to assess the most appropriate approach, taking into account your VAT recovery and effective corporation tax rates.

Most of the time, spreading the cash flows over the vehicle term can be financially beneficial allowing more efficient use of capital for core investment projects. Funding products such as contract hire or contract purchase provide an even spread of monthly repayments, whereas outright purchase can require a high initial capital outlay.

The choice of funding product can also result in further savings – for example, if you have a van fleet, it may be worthwhile, depending upon your VAT recovery position, to acquire these vehicles via contract purchase, as you can recover input VAT up front on the acquisition cost.

If you have expensive cars (with a tax list price greater than £12,000) funded via contract hire, there are currently potential corporation tax savings depending upon how you calculate Expensive Car Leasing Disallowance (ECLD). Most organisations will use the tax list price, whereas it is permissible to use the actual purchase price – which can be a significantly lower value – and result in a smaller proportion of the finance lease rental being disallowed for tax purposes.

However, this potential saving opportunity only applies to cars on lease contracts which commenced before April 2009. For cars where lease contracts commenced after April 2009 the tax disallowance is based on CO_2 emissions with a 15% tax restriction applicable to cars with CO_2 emissions greater than 160g/km, but the restriction will not apply to cars with emissions of 160g/km or less.

You should consider reviewing your fleet mix and car policy to make sure they are aligned to the new tax rules.

You may also wish to think about your short-term versus medium-term funding needs. If your business is seasonal, it might be appropriate to fund your core fleet by contract hire or contract purchase, whilst funding the seasonal element via a shorter term product, such as Minilease, or Daily Rental (for ad hoc requirements).

Selecting the most appropriate funding method for your business can achieve cash flow benefits and reduce your finance costs.
Lex Autolease can support you in this financial evaluation.

2. Manufacturer discounts.
Are you offering your staff too much choice?

Savings can be made by reducing car and van vehicle choices down to either dual or sole badge.

Manufacturers will often offer extra discounts on vehicles purchased if you choose to limit your selection to their vehicles alone. The leasing company can apply these discounts to the purchase of the vehicles which may have a significant impact on reducing your lease costs. If your company cars are funded via contract hire, any reduction in the lease rental will also result in a reduction in the amount of disallowed VAT you incur.

However, care needs to be taken not to apply a restrictive vehicle choice policy across your entire company car fleet, without considering the impact on driver morale. Reducing choice to a small number of manufacturers can have a negative impact as flexibility of vehicle choice is commonly ranked by employees as one of the most important elements a company car policy should have.

You may wish to think through the reasons why you have a company car fleet and whether the purpose is the same for the whole driver population – restrictive choice may work well for job need employees, but not for status or perk users.

A first step would be to talk to vehicle manufacturers about the level of discount they are willing to give you and the exclusivity that you are willing to give them. You should then link this back to your policy, thinking about the impact that a limited choice of vehicle will have on the perceived value of the car scheme by your eligible employees.

3. Car policy.
Have you considered reviewing your car policy terms?

Reviewing your current car policy can lead to a number of opportunities for potential cost saving.

A potential area for cost saving is to consider extending the contract period to take advantage of potentially lower average annual contract rentals from a longer period of hire – the saving in lower depreciation charges is likely to outweigh increases in maintenance charges.

Many organisations run their vehicle fleets over a 3 or 4 year period of hire – if you renew your vehicles every 2 or 3 years, consider extending this by 12 months to save costs.

If your stated replacement cycle is 3 or 4 years, but in practice you allow higher mileage drivers to replace vehicles before the end of the contracted term – if they reach a mileage threshold first, then this can lead to unnecessary depreciation costs. These costs can be avoided by ensuring that vehicles are driven to the end of the contract period, wherever possible, and mileage parameters are set at the outset based on mileage projections on a case by case basis.

Another key area of cost saving is the level at which cash allowances are set. This may be driven by a percentage of average pay per employee grade, without regard to the cost to your business of an equivalent company car – sometimes this can result in the level of cash allowance being set too generously.

A sensible approach to take is to ensure that the cash allowance level is set so that it is cost neutral for your business – i.e. whether the employee takes a company car or cash allowance, the whole life cost to the business (allowing for any variation in fuel reimbursement rates) is the same.

You should also consider incentives to encourage your employees to trade down wherever possible to a vehicle with lower CO_2 and fuel consumption – perhaps offering a partial cash payment of the whole life cost difference between the benchmark vehicle and the chosen vehicle can be beneficial for both employee and employer. It is important that this is properly communicated, so that employees are aware of this option.

Reviewing your current car policy may lead to options for change which can result in cost savings, although you should be mindful of the effect this may have on attracting and retaining employees, if the car scheme is seen as a key part of the total reward package.

For more information, see our Best Practice Guide – Reviewing your car policy.

4. Fuel and National Insurance Contribution (NIC) savings.
Are you managing the provision of fuel effectively?

Fuel is often a significant component of fleet costs. You may currently provide fuel cards to your drivers and provide fuel for private use. If this is the case, there is often a significant opportunity to reduce costs by removing the provision of free fuel – typically the private fuel element will cost you between £1,000 and £2,000 per driver per year.

Also, providing free fuel may encourage employees to drive more miles, leading to additional depreciation costs.

In many cases, the Benefit-In-Kind (BIK) cost of free fuel provision to the driver will exceed the value received.

Ways to remove free fuel include:

- A well communicated education programme to your drivers that will encourage a significant number to opt out, creating a win/win situation for you and your employees.
- Ensuring free fuel is not offered to new starters.
- Buying out existing employees via a one-off, non-pensionable lump sum payment.
- Setting a future date after which free fuel will no longer be paid.

In each case, you will need to assess the impact on your employees' motivation, relative to the projected savings.

Whether you offer private fuel or not, effective management of fleet CO_2 emissions will reduce your fuel bill as well as employers NIC payments and at the same time will help you achieve your environmental objectives.

Fleet costs can also be dramatically reduced by the introduction of video conferencing for meetings – thus reducing the amount of time the vehicles are on the road and hence leading to reduced fuel consumption and improved vehicle depreciation performance.

Reviewing your current fuel provision policy as well as your CO_2 emissions policy may lead to cost savings.

5. Operational fleet model.

Have you considered your operational fleet model?

The benefits of outsourcing parts of your fleet management include:

- Potential cost saving from greater purchasing power and cheaper maintenance rates.
- Removing residual value risk and the potential to achieve higher residual value on resale.
- Removing the risk from future unforeseen maintenance costs.
- No requirement for increased staff should your fleet size increase over time.

Consider the cost of retaining pool cars compared with utilising daily hire vehicles on an ad hoc basis. Daily hire usually offers the opportunity for cost savings since you only pay on use whereas pool cars incur costs whether used or not.

Where your fleet is associated with core activities, such as delivery vans or maintenance engineers, telematics can be used to monitor and improve utilisation. Speed limiters can also be fitted to ensure the vehicles are not driven beyond a maximum speed enabling better fuel efficiency and lower maintenance costs.

The key issue to think about is what is the most appropriate operational fleet model for your business. You need to consider whether you can effectively manage the risks and costs of running a fleet internally, whilst meeting the service needs of the organisation, or whether it is more effective to outsource your fleet, and redeploy your staff in core business activities.

6. Risk management.
How can you minimise your risks and reduce costs?

Minimising fleet risk can have a significant impact on costs.

Such risks might include:

- Disposal risk
- Accidents
- End of contract damage
- Downtime

Disposal risk relates to the actual value achieved on vehicle disposal – this risk can be significant for your business if you outright purchase your vehicle fleet – effectively you will be basing your budgets and forecasts on your predicted resale values, which may or may not be realised, and which could leave you exposed to unforeseen cost. The alternative is to outsource the risk by leasing your fleet through one or more of the leasing products described earlier.

To minimising the cost of accidents, end of contract damage and downtime, you will need to focus on identifying and managing the occupational road risk which your organisation and drivers face. Undertaking a comprehensive risk assessment to identify where the greatest risks lie in terms of individual drivers, vehicles, and journeys undertaken is not only good practice, and will ultimately lead to cost saving, (if action is taken to mitigate such risks e.g. through selective driver training), but is also a key focus of recent duty of care legislation:

- Under the Management of Health and Safety at Work Regulations 1999, every employer is required to carry out and record a risk assessment with regard to the Health and Safety of their employees and examine how risks can be reduced. This applies to those driving on company business whether in a company car or not. Employers should consider the risks to employees on the road in the same manner as those in a workplace.
- The Corporate Manslaughter and Homicide Act gained Royal Assent in July 2007 and became law in April 2008. The Act outlines companies' duty of care responsibilities to all employees (whether company car or private car users) when driving on company business; particularly as private cars being used for business purposes, including cash takers, have been acknowledged as high risk.
- The Health and Safety Offences Act 2008 updates the Health and Safety at Work Act 1974 and increases the penalties for breaches of duty of care towards employees, raising the maximum fine to £25,000 and broadening the range of offences for which individuals can be jailed.

Effective and detailed risk assessments demonstrate that your organisation takes employee safety seriously and cost savings may be achieved by improving driver awareness and lowering insurance costs by demonstrating a safer fleet.

The first step is to evaluate the risk environment, identifying who are your 'at risk' drivers, what risks are associated with the vehicles they drive, and the types of journey undertaken. Lex Autolease can offer advice and support in this area.

Online information.

You can also read more by visiting the following links:

The Health and Safety Executive (HSE)
www.hse.gov.uk

Road Safe
www.roadsafe.com

About our consultancy service.

The Lex Autolease Strategic Fleet Consultancy team works with board directors and senior managers to identify how the provision of fleet can better support key business objectives.

Our consultancy covers cost reduction, policy, tax, the environment, duty of care and fleet delivery strategy. In addition to core fleet issues, we consult on related areas such as fuel and cash schemes.

Our consultants have depth and breadth of knowledge in a range of technical areas and have prior experience in major advisory firms or industry. We combine leading edge thinking with the operational experiences that come from being part of Lex Autolease, the UK's leading fleet provider.

To find out more, contact our dedicated Strategic Fleet Consultancy team

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