AN ENVIRONMENTAL AND REGULATORY IMPACT ASSESSMENT

AUTHORISED MILEAGE RATES

The purpose and intended effect of the reform

1. Budget press release (Rev6) March 2000 announced:

   "…the Revenue will be considering how the AMRs for drivers who use their own cars for business journeys might be improved, on a revenue neutral basis, to send better environmental signals."

2. The review aimed to identify a system which would -
   - Give tax relief for amounts which represent fair reimbursement for car use;
   - Be easy to administer for companies and the Revenue
     - by reducing the number of rates and
     - allowing closer alignment of tax and NICs treatment;
   - Reflect wider environmental aims by
     - discouraging unnecessary use of cars for business
     - encouraging the use of more efficient, lower emitting cars.

3. Following that review, the Chancellor announced in the Budget his intention to replace the current administrative system of authorised mileage rates (AMRs) by a new statutory system of mileage rates from April 2002. These will be known as approved mileage allowance payments (AMAPs).

4. This measure will be implemented by clauses 57 to 59 Finance Bill 2001.

5. This will further reinforce the message that the Government wishes to incentivise people to buy and use more environmentally friendly cars. This is the rationale behind both the new company car tax and the new graduated vehicle excise duty. The new mileage rates regime will be complementary to these, but where they are based on a car's level of CO_2 emissions, it is not possible yet to introduce an emissions based system for employees' own cars used for business journeys as the majority of cars are more than 3 years old. CO_2 data would therefore be unreasonably hard, or impossible, to find.

6. As a simple to understand and administer alternative, the new system will be based on one single rate with a mileage breakpoint for all sizes of cars and vans. The rate will be generous for smaller, fuel-efficient cars and alternatively fuelled cars, such as gas or hybrid electric vehicles, but offer reduced reimbursement for business miles in larger cars.

7. This change may also discourage high business mileage drivers from "cashing-out" of large company cars and moving into private, possibly

older, less environmentally friendly cars. (There are currently only 190,000 employees using their private cars over 2000cc for business miles, the majority of whom do below 4000 business miles p.a.).

8. The current 4,000 miles breakpoint is to be raised to 10,000 business miles per annum which very few owner-drivers currently drive. This will make administration easier for employers and simplify the NICs treatment of mileage payments. The table below shows a breakdown of the number of business miles currently driven in different sized cars by employees using their own cars for business.

Distribution Of Private Cars Used For Business By Annual Business Mileage in thousands			
Level Of Annual Business Mileage	**Cars Up To 1500cc**	**Cars Between 1500cc And 2000cc**	**Cars Over 2000cc**
0 – 1,999	830	880	80
2,000 – 3,999	230	320	30
4,000 – 7,499	140	190	20
7,500 – 9,999	30	60	20
Over 10,000	40	130	40
Total	1,270	1,580	190

9. Rates will be set in statute with a power for the Treasury to revise them, as appropriate, in regulations.

10. The Chancellor has also announced a 5p per mile tax and NICs free passenger rate to encourage car sharing on journeys to business meetings, and an increased cycle rate set at a very generous level of 20p per mile to encourage use of bicycles.

11. Employers who reimburse employees at rates below those set in statute will not have to report payments to the Revenue. Employers who currently pay more than 40p per mile under the current AMR system covered by a dispensation, and decide to continue to pay rates above 40p per mile after April 2002, will have to calculate the profit liable to tax and NICs i.e. the amount above 40p per mile for 10,000 miles and 25p per mile thereafter, and report it to the Revenue on a P11D. This is a new, though relatively simple calculation. Any profit element in mileage rates paid already has to be calculated and put through the payroll for NICs within the pay period.

An assessment of the environmental benefits of the new system

12. ***Economic Rationale -*** the new AMAPs will provide better environmental incentives to drivers doing business mileage in private cars by increasing

the statutory reimbursement rates available for smaller, more fuel efficient cars, and reducing the rates available for larger, less fuel efficient cars. As a result, the new regime is expected to lead some drivers of larger cars to downsize to smaller makes and models.

13. The greater the level of emissions a car produces, the greater the social costs associated with its use. In the sense that it encourages the use of smaller, more fuel-efficient cars the measure should help to reduce such external costs. However emissions levels are also related to the amount of mileage done and the measure might lead to some employees doing more business mileage in private cars, although it will also give other employees a financial incentive to do less such mileage. The passenger rate and increased bicycle rate will lead to limited reductions in car use and so will reduce social costs of pollution and congestion associated with car use.

14. ***Gainers/Losers:*** the theoretical numbers are evenly split, with around 1.56 million potential gainers and 1.48 million potential losers from the measure. The amounts of tax and NICs gains and losses are mostly small, as the majority of employees drive less than 4,000 business miles per year. The numbers of potential gainers and losers represent estimates on the basis that all business mileage is paid at the current and future authorised rates. In practice, DETR-commissioned research suggests that only around one-third of private sector employers (covering around 16% of private sector employees who can reclaim business mileage) and 4% of public sector employers who reimburse employees using their own vehicles for business travel pay at the current authorised rates. However the research suggests that much larger proportions are influenced by the authorised rates in setting their rates.

15. ***Behavioural Effects –*** the restructuring of rates may induce some drivers, particularly those for whom business use of their car is a major percentage of its usage, to downsize to smaller cars. We estimate only around 75,000 drivers, mainly with cars of 2,000cc or above, will face significant downsizing incentives. There is no *direct* incentive under the proposed AMAP changes to induce individuals to reduce their business mileage in the same way that there is under the new company car tax regime where business mileage discounts are being abolished. There is also no incentive to downsize by *explicitly* being more generous to cars under 2000 cc and less generous to those over 2000 cc in terms of reimbursement. However running costs per mile will often be relatively higher for larger cars than smaller cars and the new AMAPs regime will not make any allowance for this. There is therefore a limited incentive to downsize.

16. The regime is expected to lead to some changes in business mileage driven – with those getting more reimbursement under the new rules possibly choosing to drive more frequently, those getting less reimbursement possibly cutting back their business mileage. In both cases this can only happen where business travel is flexible.

17. We believe the net effect on CO_2 emissions is likely to be modest, with expected savings in CO_2 carbon emissions estimated at around 2,000 tonnes per year after full adjustment. This is due to a combination of some reduction in business miles being driven and some downsizing of cars. This compares with a lower range estimate of 500,000 tonnes per year in CO_2 carbon savings arising from the company car tax reforms after full adjustment.

18. But the AMAP changes are expected to lead to some reduction in the previously forecast level of net cashing-in under the new emissions-based company car taxation regime to be introduced in 2002/3. . We previously estimated a net cashing-in of approximately 180,000 company cars after full adjustment, which would be reduced to approximately 150,000 after full adjustment under the new AMAPs regime to be introduced in 2002/3 (But these estimates are subject to fairly wide margins of error). This could reduce the environmental impact if many drivers move into larger, older, less fuel efficient cars rather than company cars.

Risks

19. There are no major identifiable risks in either implementing or not implementing this measure.

Sectors affected:

20. Information from IR data and the National Travel Survey tells us that three million people use their private car for business. Of these, 2.3 million receive some compensation from their employers for business mileage. Nearly 80% of them drive less than 4000 business miles per year, whilst only 5% drive more than 12,000 miles.

21. We have considered the likely effects of different options for change on key groups of employees who claim AMRs. Many public sector workers, such as nurses and local government employees, are likely to be driving smaller, more fuel-efficient cars and so may gain from the proposals

Gender differences

22. National Travel Survey data suggests at least 60% of small cars up to 1500cc are driven by women, while the majority of larger cars (nearly 80% of cars above 2000cc) are driven by men. More men than women drive over 4,000 business miles per year, and nearly 80% of drivers exceeding 10,000 miles per year are men. It is therefore likely that an unintended affect of this reform will be to benefit women drivers more than men.

How will businesses be affected

Employers

23. Employers will be able, as now, to pay whatever they consider to be suitable mileage rates to their employees. They will not have to pay the statutory rate. They will know that if they pay more the 40p per mile rate the excess will be subject to tax and NICs. This could mean some employers who currently pay rates within the current AMRs and so are covered by a dispensation, having to report profit elements if they do not move to paying at or below the new statutory mileage rate.

The effect on car manufacturers

24. This change will further add to the encouragement to buy smaller, more fuel efficient cars. Car manufacturers are already responding to the likely demand. This and the other business travel tax changes such as the new company car tax and graduated vehicle excise duty regimes may encourage more people to trade in their existing car for a new one sooner.

Recurrent and non recurrent costs/ savings

25*. Non recurring costs* arise from: the transitional costs of moving to the new rate structure, management and staff training, and minor changes to computer software. In practice though, these costs will be small, as nothing in essence has changed with the new rates.

26. The new structure of mileage rates may trigger some employers to review their own policy for paying mileage rates (perhaps due to employee or union pressure). This could impose additional costs upon businesses in cases where costs of reviewing and changing business mileage rates are greater than those which would have arisen anyway had the changes to the Inland Revenue's AMRs not taken place.

27. The DETR-commissioned research found that around 8 out of 10 private sector employers paying business mileage reimbursement - and roughly half of public sector organisations - use the Inland Revenue AMRs as a guide to setting their own rates. However the research also found that around 53% of private sector employers and around 32% of public sector employers who pay business mileage review their business mileage rates annually or on another regular basis anyway (and of course after some of these reviews business mileage rates will be changed). Therefore any changes in the AMRs is likely to have a knock-on effect on many employers, although any one-off costs associated with this are likely to be

relatively small and fall below £5 million.

28. *Recurrent savings:* there are unlikely to be any significant ongoing cost savings arising from the new AMAP structure, as records of business mileage will still need to be kept in order to determine reimbursement levels. But the new AMAPs will apply to all cars, meaning that records no longer need to be kept of engine size in order to determine the appropriate level of reimbursement. This may speed up the administration process slightly and make it easier to understand, but is unlikely to result in any real quantifiable savings in monetary terms for those organisations who adopt the new rates.

29. A similar argument applies to raising the breakpoint to 10,000 miles breakpoint (compared to 4,000 miles at present) as relatively few employees drive over 10,000 business miles in private cars.

Small businesses

30. The research suggests that smaller, private sector firms that reimburse their employees are significantly more likely to be using the Inland Revenue's current AMRs than larger private sector firms. So relatively small firms that reimburse their employees are probably more likely to change their rates in response to the changes in the Inland Revenue's AMRs than larger firms and to be more affected financially (relative to their turnover levels) by the changes.

31. However we also need to consider how likely private sector firms of different sizes are to be reimbursing employees who use their own vehicles for business journeys at all. The research suggests that around 28% of firms with 1 to 49 employees do this. This compares to around 47% of firms with at least 500 employees and around 69% of firms with between 50 and 499 employees. Smaller firms are less likely to reimburse business mileage done in non-company cars than larger firms and so may be less likely to be affected by changes to the AMRs. But those that do reimburse employees are likely to be relatively more affected than larger private sector firms which offer reimbursements. This is not only because the smaller firms are more likely to pay business mileage at the Inland Revenue's AMR rates than at other levels. It is also because those that do pay business mileage on average have greater proportions of employees claiming it and doing greater average annual amounts of business mileage than the relatively larger firms.

32. The research found that the proportion of employees who claim for business mileage in non-company cars in small firms with 1 to 49 employees in the private sector that reimburse such claims was around a third. The average number of miles claimed around by employees in such firms was around 3,600. The equivalent levels for medium-sized firms of 50 to 499 employees in the private sector were around 16% of employees claiming an average of around 2,300 miles annually each. For large

private sector firms with at least 500 employees they were around 2% of employees claiming an average of around 900 miles annually.

Other costs/savings

33. *Employees* will no longer be able to make a claim for tax relief based on actual receipted bills, nor claim capital allowances or interest on loans related to car purchases. Only a few thousand employees currently make such claims, which involve keeping comprehensive records of all the costs associated with business mileage and running their vehicle. In future, employees will be able to claim tax relief on their business mileage up to the statutory rate if their employer has paid them less.

34. *The Inland Revenue* will have less individual claims to deal with. But it will have an initial job of identifying and amending tax codes of a small minority of those already receiving regular mileage rates

Estimated overall costs

35. The estimated overall net exchequer costs and net regulatory costs to business of the changes between 2001/2 and 2003/4 are shown in the following table:

Year	2001/2	2002/3	2003/4
Net Exchequer Cost	-£40m	-£45m	-£45m
Net Regulatory Cost to Business	Neg	-£5m	Neg

Note that in the table above, net costs are shown as negative numbers and net savings are shown as positive numbers.

The consultation process

36. The Revenue has consulted widely with interested parties including representatives of the main umbrella employer organisations, NHS Executive and Local Government representatives, and motoring organisations.

37. The DETR, working with the Revenue, commissioned research to understand more fully why, when and how much individuals use their own cars for business, and what makes companies offer company cars - or not.

Guidance for employers

38. The proposed changes will be outlined in the *Employer Bulletin* issued to all employers in April 2001. Further details will be provided in the September edition of the Bulletin with the low-level guidance being supplied in the 2002/03 Employer Annual Pack which will be issued in January 2002.

39. For those employers using a commercial payroll IT product or service similar details are being supplied to software programmers via *IR Notes for Payroll Software Developers.*

Securing compliance

40. Existing enforcement methods and penalties will apply.

Monitoring And Review

41. The impact of this measure will be monitored and reviewed as considered appropriate.

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Statement of Ministerial Approval

I have read the regulatory impact assessment and I am satisfied that the benefits justify the costs.

STEPHEN TIMMS.
FINANCIAL SECRETARY TO THE TREASURY

2 April 2001