

Cars: capital allowances and lease/hire payments

Parts 11 and 11C

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Introduction

This instruction applies to vehicles that are essentially private passenger cars, defined in TCA 1997 (sections 373(1) and 380K(1)) as:

“a mechanically propelled road vehicle constructed or adapted for the carriage of passengers, other than a vehicle of a type not commonly used as a private vehicle and unsuitable to be so used.”

In relation to capital allowances, the usual plant and machinery provisions in Part 9 TCA 1997 apply to cars. However, an important qualification is that there is a limit on the allowable expenditure on a car. This limit also applies to lease/hire payments. The limit has been increased over time and is currently €24,000 – full details are in section 5. In relation to expenditure incurred on the provision or hiring of a car on or after 1 July 2008, the limit is determined by a car’s level of CO2 emissions.¹

The legislation governing capital allowances and expenses for cars is contained in Parts 11 and 11C TCA 1997.

1. Treatment of other vehicles

The vehicles in relation to which the limit applies are, in effect, ordinary motor-cars. It does not apply to any vehicle of a type not normally used as a private vehicle and unsuitable to be so used, for example, vans, trucks and tractors. Such vehicles can qualify for unrestricted capital allowances and deductions for lease/hire payments.

There is an exception relating to cars provided or hired wholly or mainly for the purpose of hire to or carriage of members of the public in the ordinary course of a trade, for example, taxis and cars used by car-hire businesses. Cars used for testing purposes by a manufacturer of cars or car accessories are also excluded, but if such a car is used to any substantial extent for non-testing purposes within five years of purchase the restriction is applied and the position adjusted by additional assessment.

2. Apportionment of business/private use

Section 284(1) TCA 1997 is the section that grants wear and tear allowances. The allowances are available where a car is used for the purposes of a trade (or profession or employment). While it is used for trade purposes, it must be wholly and exclusively so used. Thus, no allowances are available for the time that a car is used for private or non-business purposes. The annual wear and tear allowance must be apportioned on a time basis where a car is used for both business and non-business purposes.

¹ Introduced by section 31 Finance Act 2008 – now Part 11C TCA 1997.

To be fully deductible, lease/hire expenses must meet the 'wholly and exclusively' test. Thus, only the portion of the expenses that are attributable to the business use of the car is allowable. The fraction used for the purposes of determining the business use of the car is normally derived from the proportion that the business mileage bears to the total mileage incurred.

3. Rates of wear and tear allowances

For expenditure incurred on or after 4 December 2002, the annual rate of wear and tear allowance is 12½%. This rate writes off the allowable cost of a car evenly over 8 years.

For expenditure incurred on or after 1 January 2001 but before 4 December 2002, the annual rate of wear and tear allowance was 20%. This rate wrote off the allowable cost of a car evenly over 5 years. Transitional arrangements allowed this rate to be claimed (instead of the 12½% rate) where expenditure was incurred on or after 4 December 2002 if the car was acquired under a binding contract evidenced in writing before that date and the capital expenditure was actually incurred by 31 January 2003.

For expenditure incurred before 1 January 2001, the annual rate of wear and tear allowance was 20%, but on a reducing balance basis rather than on the current straight-line basis. However, in relation to chargeable periods ending on or after 1 January 2002, claimants could elect to have the 'tax written-down value' (TWDV)² of all pre-1 January 2001 expenditure pooled together to qualify for write-off on a straight-line basis at 20% per annum over the following 5 years.

² The TWDV is the amount of allowable expenditure still to be written off after a portion of the wear and tear allowances has been deducted. With the 'reducing balance' method the annual rate of wear and tear allowance is applied to the TWDV and not to the original allowable expenditure.

4. Limit on allowable expenditure (pre-1 July 2008 expenditure)³

The actual cost of a car is generally disregarded for capital allowances purposes. Where expenditure was incurred on the provision of a car before 1 July 2008 and where the actual cost of the car exceeded a specified limit, wear and tear allowances were based on the relevant specified limit. Where the actual cost of a car was lower than the relevant specified limit, wear and tear allowances were based on the actual cost of the car.

In relation to expenditure incurred on or after 1 July 2008, the allowable expenditure for wear and tear allowances is determined by the car's level of CO₂ emissions. See section 7 below.

The specified limit has been increased over time and details are set out below.

Date expenditure incurred	Specified (cost) Limit ⁴	
	New cars	Second-hand cars ⁵
16 May 1973 to 28 January 1976	£2,500	£2,500
29 January 1976 to 5 August 1986	£3,500	£3,500
6 April 1986 to 27 January 1988	£4,000	£4,000
28 January 1988 to 25 January 1989	£6,000	£6,000
26 January 1989 to 29 January 1992	£7,000	£7,000
30 January 1992 to 26 January 1994	£10,000	£10,000
27 January 1994 to 8 February 1995	£13,000	£10,000
9 February 1995 to 22 January 1997	£14,000	£10,000
23 January 1997 to 2 December 1997	£15,000	£10,000
3 December 1997 to 1 December 1998	£15,500	£10,000
2 December 1998 to 30 November 1999	£16,000	£10,000
1 December 1999 to 31 December 2000	£16,500	£10,000
1 January 2001 to 31 December 2001	€21,586	€21,586
1 January 2002 to 31 December 2005	€22,000	€22,000
1 January 2006 to 31 December 2006	€23,000	€23,000
1 January 2007 –	€24,000	€24,000

³ Section 374 TCA 1997.

⁴ Limits contained in section 373 TCA 1997.

⁵ With effect from 1 January 2001 the increased limit applied to both new and second-hand cars.

5. Restriction of capital allowances (pre-1 July 2008 expenditure)

The effect of imposing a limit on the amount of allowable expenditure is detailed below:

- Where a car costs over the specified limit the allowances are restricted to what they would be if the cost were the specified limit.
- Balancing allowances and charges are computed on the basis that the original cost of the car was the specified limit and the wear and tear deductions to be taken into account in computing the amount still unallowed are to be the allowances as restricted.
- If the car is put out of use and there are sale, etc., monies then, in the computation of balancing allowances and charges, any such sums will be reduced to the proportion which the specified limit bears to the actual cost of the car.
- Where the car changes hands otherwise than by sale in the open market so that the provisions of sections 289(5) or (6), section 312 or section 313(1) TCA 1997 apply, the allowances to the purchaser, donee or successor should be scaled down in the proportion which the specified limit bears to the cost to the prior owner. So long as there is no sale in the open market the reduction to be applied to the deemed proceeds of sale at each successive transfer in a chain of transfers is in the proportion which the specified limit bears to the cost to the **first** owner in the chain.
- Where an election is made under section 290 TCA 1997 to have wear and tear allowances on a replacement car computed on the amount by which the cost of the car exceeds the balancing charge which might have been made on the car it replaced the cost of the car bought in replacement is first restricted to the specified limit before the balancing charge on the old car is deducted.
- Where the claimant purchasing a car costing more than the specified limit receives a subsidy directly or indirectly from the State or a public authority so that, pursuant to section 317(2) the expenditure to be taken into account for the purposes of balancing allowances and balancing charges is the net expenditure only, the net outlay should be restricted in the proportion which the specified limit bears to the gross cost of the car.

Example

Cost of new car in June 2003 €30,000, (used exclusively for business purposes) restricted to		€22,000
Wear and tear 12½% (year 1)	Deduct	<u>€2,750</u>
TWDV at 31 December 2003		€19,250
Wear and tear 12½% (year 2)	Deduct	<u>€2,750</u>
TWDV at 31 December 2004		€16,500
Sold for €20,000 2005 – $20,000 \times \frac{22,000}{30,000}$	Deduct	<u>€14,667</u>
Balancing allowance		€1,833

There would be a balancing charge of €2,567 if the car had been sold for €26,000. The claimant could elect under section 290 to have the allowable cost of a replacement car reduced by the amount of the balancing charge. The following example illustrates this. This time, the car is only used 90% of the time for business purposes.

Example		Business use element
Cost of new car 2005 €35,000, restricted to	€22,000	
Balancing charge	<u>€2,567</u>	
Balance for wear and tear allowances	€19,433	
Wear and tear 12.5% (year 1) 90% business use	<u>€2,429</u>	€2,186
TWDV at 31 December 2005	€17,004	
Sold for €30,000 2006 – $€30,000 \times \frac{€22,000}{€35,000}$	<u>€18,857</u>	
Balancing charge	€1,853	€1,667

6. New CO₂ emissions regime (post 1 July 2008)

The new CO₂ regime for wear and tear allowances applies where expenditure is incurred on or after 1 July 2008. The availability of wear and tear allowances, and the amount of such allowances, is now linked to the CO₂ emissions of a car. Cars, both new and second-hand, are now categorised by reference to the bands of CO₂ emissions that are used to determine Vehicle Registration Tax (VRT). The original CO₂ emissions figure at manufacture determines the band and not the CO₂ emissions of the car at the date of registration. For income tax purposes, the 7 VRT categories are divided into 3 different groups as follows:

- **Group 1** contains categories A, B and C with CO₂ emissions up to and including 155g/km. The allowable expenditure for these cars is the relevant specified limit (currently €24,000 as set out in section 5 above), regardless of the actual cost of the car. Thus, wear and tear allowances are based on deemed expenditure of €24,000 even if the car actually cost less than this amount.
- **Group 2** contains categories D and E with CO₂ emissions from 156g/km up to and including 190g/km. The allowable expenditure for these cars is the lower of 50% of the relevant specified limit or 50% of the actual cost of the car. This means that cars in this group can get wear and tear allowances on a maximum of €12,000 no matter how expensive they are.
- **Group 3** contains categories F and G with CO₂ emissions that exceed 190g/km. These cars get no wear and tear allowances whatsoever.

The new regime is summarised in the following table.

Group	VRT Category	CO ₂ Emissions (grams per km)	Allowable Expenditure €
1	A	0 - 120	24,000
	B	121 – 140	
	C	141 – 155	
2	D	156 – 170	50% of 24,000 or, if lower 50% of actual cost
	E	171 – 190	
3	F	191 – 225	Nil
	G	more than 225	

6.1 Verification of CO₂ emissions

A car's CO₂ emissions will have been established when it was registered for VRT purposes.⁶ The emissions on which the claim for wear and tear allowances is based can be verified by checking the details on the IBI system⁷ or by getting a copy of the Vehicle Registration Certificate from the claimant. Where Revenue is not satisfied with the documentation provided, or where there is no documentation, then the vehicle will be deemed to be in Category G with no entitlement to capital allowances.⁸

7. Restriction of capital allowances (post 1 July 2008 expenditure)

The various treatments outlined in section 6 also apply to cars whose wear and tear allowances are determined by their level of CO₂ emissions. In relation to cars in Group 1, "the specified limit" referred to in section 6 is that specified limit regardless of the actual cost of the car. In relation to cars in Group 2, references to the "specified limit" in section 6 should be substituted by the lower of 50% of the specified limit or 50% of the actual cost of the car. In relation to cars in Group 3, section 6 is not relevant as no capital allowances are due.

Example

On 1 July 2009 an individual purchases 2 cars, one for himself and one for his deputy manager. Car 1 has CO₂ emissions of 120g/km and cost €48,000. Car 2 has CO₂ emissions of 140 g/km and cost €16,000. The cars are used exclusively for business purposes. Wear and tear allowances are given as follows:

	Car 1	Car 2
Actual cost 2009	€48,000	€16,000
Specified limit (group 1)	€24,000	€24,000
Wear & tear allowance (12½%)	€3,000	€3,000
TWDV 31/12/2009	€21,000	€21,000

⁶ Instruction 1.4.3 of the VRT Manual outlines the processing of declarations for registration and the documentation acceptable to Revenue for such purposes.

⁷ On the IBI system, follow the links – applications/assets/vehicles.

⁸ Section 380K(3).

If, instead, the two cars had CO₂ emissions of 160g/km and 180g/km, the position would be as follows:

	Car 1	Car 2
Actual cost 2009	€48,000	€16,000
Specified limit (group 2)	(50% €24,000)€12,000	(50% €16,000)€8,000
Wear & tear allowance (12½%)	€1,500	€1,000
TWDV 31/12/2009	€10,500	€7,000

8. Renewals/Replacement Allowance

Where the renewals or replacement basis is used, wear and tear allowances cannot be claimed on the initial capital expenditure, but a revenue expense deduction is allowed when the car is replaced. Any sale or other disposal proceeds are deducted from the cost of the replacements and only the net expenditure on the new car(s) is allowed. The renewals or replacement basis is used in relation to items of relatively small value that tend to wear out and need replacement frequently, for example, small tools. It would be highly unusual for it to be appropriate for cars. However, section 375 TCA 1997 outlines how the basis is to apply for cars in relation to the need to restrict the allowable expenditure. This section is not reproduced in Part 11C that provides for the new CO₂ emissions regime from 1 July 2008.

Where a car is purchased for more than the relevant capital limit and a renewals allowance is claimed, whether in connection with a Schedule D computation or otherwise the allowance is to be computed by reference to the relevant capital limit. Where, however, the car is replaced in its turn (whether the car then bought costs more or less than the relevant capital limit) the renewals allowance on that occasion is computed on the footing that its value or sale proceeds are scaled down in the proportion which the relevant capital limit bears to its cost.

Example

Cost of car A in January 2002	€25,000
Cost of car B in June 2002	€30,000
Car A sold June 2002	€18,000
Cost of car A restricted to	€22,000
Proceeds of car A restricted to – €18,000 x $\frac{€22,000}{€25,000}$	€15,840
Cost of Car B restricted to	€22,000
Renewals allowance - €22,000 less €15,840	€6,160

9. Lease/Hire payments

Where expenditure was incurred, up to 30 June 2008, on the hiring (otherwise than under a contract of hire-purchase) of a car, the original retail price (when car was new) of which exceeded the specified limit, only that proportion of the expenditure is allowable which the specified limit bears to the retail price. The following formula gives the deductible lease expenses:

$$\frac{\text{Lease payments} \times \text{specified limit}}{\text{Lease price of car (when new)}}$$

As with capital allowances, the new CO₂ emissions regime outlined in section 7 applies to lease/hire payments incurred on or after 1 July 2008⁹ as follows:

- **Group 1** cars get a proportionately higher deduction than the actual leasing expenses where the cost of the car is less than the specified limit. The following formula gives the deductible lease expenses:

$$\frac{\text{Lease payments} \times \text{specified limit}}{\text{Lease price of car (when new)}}$$

- **Group 2** cars get half of the leasing expenses where the retail price of the car (as new) is less than or equal to the specified limit. Where the retail price of the car (as new) exceeds the specified limit, the deductible lease expenses is the amount produced by the following formula:

$$\frac{\text{Lease payments} \times 50\% \text{ of specified limit}}{\text{Lease price of car (when new)}}$$

- **Group 3** cars get no deduction for leasing expenses.

10. Hire Purchase.

Where a car is acquired by hire-purchase, the 'interest' element in the payments is allowable with no restriction by reference to capital cost. As a safeguard against claims that the capital element should be calculated by reference to the value of the car when the property in it passes, thereby increasing the revenue element in the instalments, it is provided that the capital element shall be equal to the price which, at the time when the hire-purchase contract was entered into, the person acquiring the car would have been charged on a cash sale.

⁹ In practice Revenue will not seek to impose the new rules where a lease was entered into before 1 July 2008 but the lease payments are made after that date.

10.1 Hirer does not take ownership of car

There may be cases where a contract provides both for the hire and purchase of a car the retail price of which is over the specified limit, and the person incurring the expenditure ceases to be entitled to the benefit of the contract without becoming the owner of the car. In such cases the payments under the agreement are to be disregarded for the purposes of wear and tear allowances. Instead, all payments under the agreement, including the "interest" element in the instalments are to be treated as pure hire payments and restricted accordingly.

Example

A car costing €27,000 was purchased in January 2005 on hire purchase over a 3-year period. The 'interest' charges were €9,000. After 2 years the taxpayer ceased to be entitled to the benefit of the contract.

Capital paid after 2 years (2/3)	€18,000
'Interest' allowed (2/3) in full	<u>€6,000</u>
Amount to be regarded as hire	€24,000

Restricted to $\frac{€22,000}{€27,000} \times €24,000 = €19,556$

Adjustments

1 st year	Allow hire €19,556 ÷ 2	€9,778
	Less 'interest' already allowed	<u>€3,000</u>
	Additional allowance for hire	€6,778
	<u>Less</u> W & T €22,000 @12.5%	<u>€2,750</u>
	Additional allowance	<u>€4,028</u>
2 nd year	Allow hire less 'interest' (€9,778 – €3,000)	€6,778
	<u>Less</u> W & T allowance €22,000 @12.5%	<u>€2,750</u>
	Additional allowance	<u>€4,028</u>

11. Lease/Hire of Cars (not hire-purchase)

Where a car is hired otherwise than by way of hire-purchase, and the person hiring it subsequently becomes the owner, then if the retail price of the car at the time of the hire contract exceeded the specified limit he or she is to be treated as having incurred, when the hiring began, capital expenditure on the acquisition of the car up to the amount of that retail price. The amount by which his or her total expenditure on hire and subsequent purchase exceeds the retail price is to be treated as expenditure on hire and apportioned rateably over the hire period with consequential adjustment of the deductions for hire already allowed.

Example

The original retail price of a car hired under a contract in January 2005 was €28,000. At the time the contract was made the then current retail price of the car was €25,000. The hire charges were €8,000 per annum. After two years the car was purchased for €18,000.

Hire charges allowed	Year 1	€8,000 x $\frac{\text{€22,000}}{\text{€28,000}}$	€6,286
	Year 2		€6,286
Revised position	Purchase price		€18,000
	Add hire paid		<u>€16,000</u>
			€34,000
Retail price at time of contract			<u>€25,000</u>
Hire			<u>€9,000</u>

Allow hire $9,000 \times \frac{22,000}{28,000} = €7,071$ spread rateably over 2 years, i.e. €3,535 per annum. Give wear and tear allowances on €22,000 from Year 1 and deal subsequently on sale on the basis of an original cost of €25,000.

12. Discounts.

Where an expensive car is purchased at a price which is considerably below the list price suggesting an abnormally high discount, the transaction should be examined to ensure that part or all of a discount applicable to a commercial vehicle (on which capital allowances or lease/hire payments would not be restricted) is not applied instead to the car. If it appears that this has occurred the discount should be adjusted to a uniform rate over the two transactions, for example:

	Van	Car
List Price (2007)	€70,000	€35,000
Discount	<u>€3,500</u>	<u>€7,000</u>
Cost for capital allowances (and lease/hire charges)	€66,500	€28,000
		(Restricted to €24,000)
Overall discount €10,500 on €105,000	10%	
Revised position:		
List Price	€70,000	€35,000
Discount at 10%	<u>€7,000</u>	<u>€3,500</u>
Cost for capital allowances (and lease/hire charges)	€63,000	€31,500
		(Restricted to €24,000)