EMPLOYER-PROVIDED VEHICLES

It is quite common for government entities to require their employees to use government-owned vehicles in order to accomplish their duties. When that is the case, factors are in place for a potential taxable effect to the employee driving the vehicle if any of the use is for personal purposes. Let's take a closer look at some of the provisions outlined in Publication 15-B, Employer's Tax Guide to Fringe Benefits, to gain a better understanding of these provisions.

Personal use of an employer-provided vehicle is taxable compensation to the employee driver when the use includes commuting, vacation, personal errands, or use by family members. When taxable use has occurred, the employer is obligated to value that use, report the value of the use as compensation on Form W-2, and withhold employment taxes. Let's describe personal use next.

The following scenarios of personal use of an employer-provided vehicle would be taxable:

- Commuting between residence and work station
- Vacation, weekend use
- Use by spouse or dependents

Example: An employee goes into his office on the weekend. This is personal commuting, regardless of whether it is required by the employer. Treasury Regulations §1.162-2(e);

Exception for De Minimis Nontaxable Personal Use:
An exception to the limitation on personal use applies for use that qualifies as de minimis. Examples of de minimis use of an employer-provided vehicle that can be excludable include:

- Small personal detour while on business, such as driving to lunch while out of the office on business.
- Infrequent (not more than one day per month) commuting in employer vehicle. This does not mean that an employee can receive excludable reimbursements for commuting 12 days a year. The rule is available to cover infrequent, occasional situations. Treasury Regulations §1.132-6(d)(3); Treasury Regulations §1.132-6(e)(2)

Another Example:
An employee uses a motor pool vehicle for a business meeting. The employer requires that motor pool vehicles be returned at the end of the business day, but the employee is delayed and the motor pool is closed when the employee arrives back at the office. The employee takes the vehicle home and returns it the next morning.

Assuming that this is an infrequent occurrence for that employee (generally happening no more than once a month) the commuting value of the trip is considered a nontaxable de minimis fringe benefit. If not an infrequent occurrence, the commuting would be taxable to the employee.

Surely it is not considered personal use for an employee to drive a deposit to the bank for their employer using the employer's vehicle – right? Usually not. But a lack of a vehicle use policy and a lack of monitoring or enforcement could make all vehicle use 100% personal in some cases and a taxable event to the employee if no records are kept as to who is driving vehicles. Let's explain.

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How to Avoid Problems:
With a good vehicle use policy, and enforcement of that policy, the small personal detour to purchase lunch or drop off mail while on business would be de minimis use and nontaxable. However, substantiation requirements must be in place, requiring that employees who drive their employers' vehicles record both the business and personal mileage. The date, driver, distance, purpose and vehicle identification must be recorded in order to ensure that only personal use is taxable compensation to the employee. If there are no records, the value of all vehicle use is compensation to the users/drivers of the vehicles.

Valuation of Personal Use:
If it has been established that there is personal use , then the employer must place a value on the personal use and include that value as compensation to the employee. There are three valuation methods that may be used for determining the fair market value of personal use.

General Valuation Rule:
In most cases, you must use the general valuation rule to value a fringe benefit. The general valuation is generally the lease value of the vehicle. In general, the fair market value (FMV) of an employer-provided vehicle is the amount the employee would have to pay a third party to lease the same or similar vehicle on the same or comparable terms in the geographic area where the employee uses the vehicle.

Do not determine FMV by multiplying a cents-per-mile rate times the number of miles driven unless the employee can prove the vehicle could have been leased on a cents-per-mile basis.

Cents-Per-Mile Rule:
You may use a cents-per-mile rule for vehicles placed in service in 2013, if the vehicle does not exceed a stated value for the year.

To apply the vehicle cents-per-mile rule the vehicle must be used regularly 50% or more in the employer's business or commuter pool, and meet the mileage test. To meet the mileage test the vehicle must actually be driven 10,000 miles or more per year unless the vehicle is not owned or leased for the full year. Additionally, the vehicle must be used during the year primarily by employees.

Obviously, without contemporaneous records this rule could not be applied. To calculate the cents-per-mile, multiply the personal use miles by the federal mileage rate. If fuel is not provided, reduce the value by no more than 5.5 cents per mile. This rule can be applied until the car no longer meets the requirements. If you and the employee own or lease the automobile together, see Treasury Regulations §1.61-21(e)(1)(iii)(B).

For the cents-per-mile rule, a vehicle is any motorized wheeled vehicle, including an automobile manufactured primarily for use on public streets, roads, and highways.

The cents-per-mile rule has a consistency requirement. You must begin using the rule on the first day you make the vehicle available to any employee for personal use. However you may convert to the cents-per-mile rule from the commuting rule. You must also continue to apply the rule for all later years in which the vehicle is made available to any employee and the vehicle qualifies with the exception of the commuting rule for any year during which use of the vehicle qualifies under the commuting rule. Finally, you must use the cents-per-mile rule if you provide a replacement vehicle to the employee (and

the vehicle also qualifies for the use of this rule) and your primary reason for the replacement is to reduce federal taxes.

Commuting Valuation Rule:
The commuting Valuation Rule is calculated by establishing the commute frequency of the driver and multiplying it by $1.50 each way for each employee commuting in the vehicle.

This approach cannot be applied for elected officials or "control employees". A control employee for a government entity is one whose compensation is equal to or exceeds Federal Government Executive Level V (this is available at www.opm.gov, the Office of Personnel Management web site) or an elected official. To qualify, all personal use other than commuting must be prohibited in written policy by the employer and the employer must require employee to commute in the vehicle for a valid non-pay reason.

The following requirements must all be met:

- You own the vehicle and provide it for use in your trade or business, and, for bona fide non-compensatory reasons, you require the employee to commute in the vehicle.
- You establish a written policy under which you do not allow the employee to use the vehicle for personal purposes other than for commuting or de minimis personal use.
- The employee does not use the vehicle for personal purposes other than commuting and de minimis personal use.
- The individual who uses the vehicle is not a control employee.

Lease Valuation Rule:
You may determine the value of an automobile you provide to an employee by using its annual lease value (ALV). Generally, ALV is figured by determining the fair market value, applying the IRS Annual Lease Value Table (Table 3-1 in Publication 15-B) and multiplying the ALV by the ratio of personal mile to business miles. For an automobile provided only part f the year use either its prorated annual lease value or its daily lease value. The lease valuation is calculated by multiplying personal miles of use times the lease value. The lease value is determined using the fair market value and the IRS lease value tables. Also, add 5.5 cents per mile if the employer also provides fuel. This approach, or the computed value remains in effect for that vehicle until 12/31 of the 4th full calendar year of the year in which the rule is first applied.

If the vehicle is used by the employee in your business you generally reduce the lease value by the amount that is excluded from the employee's wages as a working condition benefit. In order to do this, the employee must account to the employer for the business use. This is done by substantiating the usage, the time and place, and the business purpose of the travel. Written records made at the time of each business use are best. Any use of a company-provided vehicle that is not substantiated as business use is included in income. The working condition benefit is the amount that would be an allowable business expense deduction for the employee if the employee paid for the use of the vehicle. However – an employer may choose to include the entire value of the vehicle in the employee's wages.

If you use the lease value method you must begin using the rule on the first day you make the vehicle available to any employee for personal use, with two exceptions:

- If you use the commuting rule when you first make the vehicle available, you can change to the lease value rule
- You use the cents-per-mile rule when you first make the vehicle available you can change to the lease value rule on the first day on which the automobile no longer qualifies for the cents-per-mile rule.

Vehicle use is a working condition fringe benefit. If you provide a car for an employee's use the amount you can exclude as a working condition benefit is the amount that would be allowable as a deductible business expense if the employee paid for its use. (See Publication 535) When records are kept, the portion of use that is business is the value of the working condition benefit. In other words, the business use of the vehicle is excluded from recognition as compensation. Alternatively, you can include the entire annual lease value of the car in the employee's wages. The employee can claim any deductible business expense for the vehicle as an itemized deduction on his or her personal income tax return. (This is only possible when you use the ALV rule)

Special Rule for Qualified Non-personal-Use Vehicles:
Certain types of vehicles are excluded from the rules for recognizes wages from personal use because the employee is not likely to use it more than minimally for personal purposes because of its design. All of the use of such vehicles is deemed qualified non-personal-use vehicles and a working condition benefit.

Generally the following vehicles may be deemed qualified non-personal-use vehicles and a working condition benefit:

- Clearly marked police, fire, and public safety vehicles.
- Unmarked vehicles used by law enforcement officers if the use is officially authorized.
- An ambulance or hearse when used for its designated purpose.
- Any vehicle designed to carry cargo over 14,000 pounds.
- Delivery trucks with seating for the driver only or with a folding jump seat.
- A passenger bus with a capacity of at least 20 passengers used for its specific purpose.
- School buses.
- Tractors and other special-purpose farm vehicles.
- Bucket trucks, cement mixers, combines, cranes, derricks, dump trucks, garbage trucks, flatbed trucks, forklifts, qualified moving vans, qualified specialized utility repair trucks, and refrigerated trucks.

Pickup Trucks: A pickup truck with a loaded gross vehicle weight of 14,000 pounds or less is a QNP vehicle if it has been specially modified. Some ways a pickup might be modified include;

- A hydraulic lift gate
- Permanent tanks or drums
- Permanent side boards or panels that materially raise the level of the sides of the truck bed
- Other heavy equipment like booms, welders, generators or cranes permanently affixed,
- A truck that is used primarily to transport a particular type of load in a construction, manufacturing, processing, farming, mining, drilling, timbering, or other such operation for which it was specially designed or significantly modified.

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Vans qualify if they have a loaded gross vehicle weight of 14,000 pounds or less if it has been specially modified so it is not likely to be sued more than minimally for personal purposes. Something such as vehicle that is clearly marked with permanently affixed decals special painting or other advertising associated with the trade or business and either a permanent shelving that fills most of the cargo area or an open cargo area and the van always carries merchandise, material, or equipment used in your trade or business.

Example:
A government entity paid several employees for the use of their personal vehicles while conducting the business of the entity. The employees provided mileage logs. However, the logs were not reviewed by management to determine whether the employees were being paid amounts in excess of their actual business use. Therefore, it was determined that there was excess reimbursement and that excess had to be included on the Form W-2 for each of the employees involved. The excess was computed by multiplying the standard vehicle rate by the actual business miles. Any reimbursement to the employees over the amounts so computed was income to be included on the employees' Forms W-2.

Example: Employee was paid $1,000.00. However, employee only had 500 miles on his log for the year. The standard mileage rate was 55 cents a mile. Therefore, 55 cents X 500 miles is only $275.00. The excess is $1,000 less the $275 which equals $725.00. That $725.00 is wages included on the employee's W-2, subject to withholding for social security, Medicare, and income taxes.

Refer to Section 3, beginning on page 22, of Publication 15-B for more information on the Valuation Rules.

With this training we hope to clarify how to comply with the requirements outlined in the tax code and regulations – please refer to the publications we have offered and consider how your situation applies. If you still have questions, you may with to either follow up with your FSLG Specialist or email FSLG at tege.ask.fslg@irs.gov.