The Latest on
Auto Mileage Regs

IRS Has Issued New “Temporary” Rules, But Are They Any Better?

by Martin S. Morris

Temporary regulations implementing the provisions of the Repeal of Contemporaneous Recordkeeping Requirements Act of 1985 were published in the Federal Register on November 6, 1985. The regulations make revisions to the previous log keeping requirements for company vehicles and other items of “listed property.” The standards for substantiating the business/personal use of a company vehicle or other items of listed property must be met before an employer can claim investment tax credits or depreciation deductions. Once business and personal use is established employers must attribute income to employees (Form W2) in order to be able to obtain the full tax benefits of property ownership.

The new regulations provide less stringent recordkeeping requirements than the original log requirements but the elimination of two safe harbor rules in the earlier rules will result in more cumbersome recordkeeping responsibilities for some taxpayers. Previously automobile/truck use could be proportioned on the basis of 70%/30% and 80%/20% business/personal use respectively. These safe harbor rules are eliminated in the new regulations. A 75%/25% business/personal safe harbor is only available for vehicles used in farming now.

Other provisions of the new temporary regulations offer significant improvements over earlier IRS regulations. Many pick-ups and vans will not be subject to any recordkeeping requirements and employees taking these vehicles home at night will not be subject to taxes for personal use. The improvements follow the provisions of the Repeal Act which required that the IRS expand the classification of vehicles that are not susceptible to personal use because of their physical characteristics (e.g. painted signs and physical alterations appropriate to work functions).

General Use Substantiation Requirements . . .

For taxable years beginning after January 1, 1986, no deduction or credit is allowed for company vehicles and other items of “listed property” unless the taxpayer substantiates each element of the expenditure or use of the property. Taxpayers are required to substantiate each separate expenditure such as the cost of acquisition, cost of capital improvements, lease payments, maintenance costs, repairs and other expenditures. The taxpayer must also prove the amount of business use based on the appropriate measurement (i.e. mileage for vehicles and time for other types of listed property such as computers). Taxpayers must also substantiate the date the property is used, business use and allocate business and personal use based on total usage. If the personal use value is added to an employee’s income the employer may fully depreciate the rest (subject to depreciation limits such as those for automobiles).

Taxpayers are required to substantiate use on the basis of “adequate records or by other sufficient evidence” as to each element of use. The regulations do not limit proof to a special log or diary but state that written evidence has considerably more probative value than statements. Probative value is enhanced if the record of use is prepared at or near the time of use and the corroborative statements not made at or near the time of use will have less credibility.

When taxpayers substantiate use under the “adequate records” standard it is not necessary to maintain a separate log or diary if the required information can be found in other...

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Taxpayers failing to meet the “adequate records” standard must establish each element of use by his own statement and by other corroborative evidence, if possible. The evidence may be circumstantial but must include the cost, time, place, purpose, and date of use. Statements of other individuals may be used but the probative value is diminished by the passage of time.

Qualified Nonpersonal Use Vehicles . . .

The term “qualified nonpersonal use vehicle” means any vehicle which, by reason of its nature (i.e. design) is not likely to be used more than a de minimis amount for personal purposes. Any vehicle fitting this classification is not subject to the use substantiation requirements. In addition, as of January 1, 1985 all value of using such a vehicle is excluded.
from an employee’s gross income as a working condition fringe benefit. Roth investment tax credits and depreciation deductions may be claimed without any substantiating records or employee income attributions, as a result. The regulations provide guidance in interpreting this classification with a specific list of vehicles and a special example of qualifying trucks and vans.

The following vehicles are specifically qualified in the regulation’s list: any cargo vehicle with a loaded gross vehicle weight over 14,000 pounds; bucket trucks; dump trucks; 20 plus passenger buses; and, utility repair trucks (not including pick ups or vans). Utility trucks must be specifically designed to carry heavy tools, testing equipment or parts and must have appropriate shelves or racks. In addition, the employer must require the employee to drive home to be able to respond to emergency situations for restoring electricity, gas, telephone, water, sewer or steam utility services.

The regulations also contain a special example of qualified trucks or vans for the qualified nonpersonal use designation. A truck or a van qualifies if it has been specifically modified with the result that it is not likely to be used more than a de minimus amount for personal purposes. The regulations give an example of a van that has only a front bench seat, with permanent shelving, that constantly carries equipment and that has been specially painted with advertising or the company’s name. This generic example is expected to provide substantial relief for employees with construction site vans and pick ups.

$3.00/Day Commuting Rule...

A special rule may be used to meet the employer substantiation requirements and to value commuting for employees. If the following conditions are met the employer is not required to keep additional records and can value commuting at $3.00 per day for his employees ($1.50 in the case of a one way commute).

a.) The vehicle is owned or leased by an employer and made available to employee(s) in connection with the employer’s trade or business,

b.) The employer requires the employee to commute to and/or from work in the vehicle for bona fide non-compensatory reasons,

c.) The employer has a written policy prohibiting the personal use of the vehicle, other than for commuting and de minimus personal use,

d.) The vehicle is not used for personal purposes by the employee or any individual whose use of the vehicle would be taxable to the employee, and

e.) If the vehicle is an automobile, the employee is not a control employee. A control employee is board or shareholder appointed, a director, or a 1% owner in the employer.

A written “commuting only” policy is not required for valuing commuting under the special $3.00 per day rule prior to January 1, 1986. For commuting use in 1985 the control employee restriction is replaced with a restriction applying to an officer or 5% shareholder/owner which was in the original regulations.

No Personal Use Vehicles . . .

A policy statement that prohibits an employee’s personal use of a vehicle satisfies an employer’s substantiation requirements if all the following conditions are met:

a.) The vehicle is owned or leased by an employer and made available to employee(s) in connection with the employer’s trade or business,

b.) When the vehicle is not used in the business, it is kept on the employer’s premises,

c.) No employee using the vehicle lives at the employer’s business premises,

d.) Under a written policy, the employer prohibits the personal use of the vehicle, except for de minimus personal use (such as a stop for lunch between two business deliveries), and

e.) The employer reasonably believes that the vehicle is not used for personal purposes.

The regulations also require that there must be evidence that would enable the IRS to determine whether the use of the vehicle meets the preceding five conditions. Employees may rely on the same criteria in lieu of substantiating their fringe benefit exclusion.

Vehicle Treated as Personal Use Vehicles. An employer may satisfy the substantiation requirements for a tax-
accounting for those expenses.

An employer is not required to provide the date that the vehicle was placed in service, the percent of business use, whether evidence is available to support the amount of business use, and whether the evidence is written. Employers are expected to obtain use records from employees as needed. Vehicle use need not be recorded on the tax return if more than five business vehicles are owned by the employer. However, the taxpayer must retain the appropriate use data for IRS audits.

**Working Condition Fringe Benefit Exclusion.** Generally, the value of property or services provided to an employee by an employer may not be excluded from the employee’s gross income unless certain substantiation requirements are met. For example, employees who file meal expense reports with their employers do not have the value of the meals included on their Form W2. With respect to items of listed property, the substantiation requirements in the new regulations do not apply to the determination of an employee working condition fringe benefit exclusion before the first taxable year of the employer beginning in 1986. After the effective date, the substantiation requirements (adequate records or sufficient corroborating evidence) will be required to obtain a working condition fringe benefit exclusion for employees.

**Employer/Employee Non Cash Fringe Benefit Deductions.** If an employer includes the value of a non cash fringe benefit in an employee’s gross income, the employer may not deduct this amount as compensation for services. The employer may deduct only the actual costs incurred in providing the benefit to the employee.

Employees may deduct the value of the business use of a vehicle if the employer treats the entire value of the vehicle as personal. Employees must substantiate the business/personal uses of the vehicle as prescribed in the regulations. A cents per mile formula cannot be used by the employees in this situation. In addition, if the employer has elected to treat the last two months of the taxable year as occurring in the next taxable year, the employee may not deduct expenses for those two months (or shorter period if such a period is elected by the employer).

**Tax Withholding and Payment Procedures . . .**

The new regulations do not change the different tax withholding and payment procedures previously announced by the IRS. Employers electing to withhold both income and wage (FICA and FUTA) taxes may do so in any regular fashion, i.e., weekly, monthly, quarterly, semiannually or annually. Employers may also elect to treat the last two months of the taxable year as occurring in the next taxable year. This election should assist in easing the administrative burdens in compiling information. Employers may also treat fringe benefit amounts as supplemental wages and withhold tax at a flat 20% rate without allowance for exemptions. Finally, employers may forego income tax withholding, provided they notify employees of the election and pay the appropriate wage taxes before the end of the year. Employees may adjust their withholding exemptions to compensate for not having income taxes specifically withheld on such fringe benefit amounts, of course.