

THE EMPLOYMENT TAX RESPONSIBILITIES FOR EMPLOYER PROVIDED VEHICLES

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This fact sheet is designed to provide awareness of social security coverage and reporting responsibilities for Kentucky state and local government employers. This fact sheet should not be cited or used as authority with respect to federal employment taxes. The Internal Revenue Code and the Social Security Act, along with the associated regulations, rulings and case law, are the only valid citations of authority.

EMPLOYER PROVIDED VEHICLES

When a Governmental employer provides a vehicle for an employee's personal use, the value of that use is generally treated as a taxable fringe benefit. This means the value of the employee's use of the vehicle must be reported as wages on Form W-2 and all appropriate taxes (income and FICA) must be withheld on the value of personal use.

If the vehicle is used 100 percent for business reasons (which must be substantiated) then the use of the vehicle is considered a "working-condition fringe benefit," not a taxable fringe benefit, and as such, the value of the use of the vehicle is not included in the wages of the employee. If the vehicle is used for both business and personal purposes, an allocation between the types of use is required which is based on the number of miles driven. The portion allocated to the employee's personal use is generally taxable to the employee as a fringe benefit. The remaining business usage is generally considered a working-condition fringe benefit and excluded from the employee's income.

If the employee's personal use of the vehicle is so small as to make accounting for it unreasonable or impracticable, a "de minimis" exception can be applied. In making the determination of a "de minimis" exception, the frequency with which the benefit is provided to the employee must be considered. A "de minimis" exception would apply in situations where the personal use of a vehicle would be limited to an occasional lunch trip or an occasional detour to go shopping while driving an employer vehicle on business. Care must be exercised to ensure that such personal use does not become so frequent or significant that it is removed from the "de minimis" exception.

Personal Use

An employee's personal use of an employer provided vehicle (other than de minimis use) must be treated as taxable wages using one of four rules:

- (1) the general valuation rule, which is based on what a person would pay locally to lease a comparable vehicle on similar or comparable terms;
- (2) the annual lease valuation rule, which assigns an IRS-determined annual lease value to the vehicle depending on its value when first provided the employee;
- (3) the cents-per-mile valuation rule, which values each personal use mile at the mileage allowance rate), or 5.5 cents less than the mileage rate if fuel is not provided; or
- (4) the commuting valuation rule, which is generally \$1.50 per one-way commute.

Withholding and Payroll Tax

Employers have a great degree of flexibility when it comes to employment tax treatment of personal use of their vehicles. Generally, the value of such personal use is subject to federal income tax withholding and FICA tax, depending on the social security and/or medicare coverage of the employee. An employer can, however, elect not to withhold federal income tax if it properly notifies affected employees of this choice.

Compensation due to personal use generally is treated as paid on a regular pay period basis. It must, however, be treated as paid no less frequently than annually. An exception to this rule allows employers to elect to treat fringe benefits provided during November and December (or shorter period) of each year as provided during January of the next. This election eases the year-end paperwork burden for employers and provides employees with valuable tax deferral.

Business Use Substantiation Requirements

Employers and employees are required to maintain adequate records or sufficient corroborating evidence to substantiate the business use of an employer provided vehicle. The substantiation must consist of written records, documents, statements or other information sufficient to corroborate the claimed business use of the vehicle.

Safe Harbor Substantiation Rules

The business use substantiation requirements do not apply if the employer issues a written policy that either prohibits employees from having personal use of the employer's vehicles or restricts personal use to commuting trips only. Employees using the following type vehicles are not required to keep detailed records of vehicle use, if the employer maintains a written policy restricting such use.

Vehicle not used for personal purposes

1. The vehicle is owned or leased by the employer and is provided to the employee for use in the employer's business;
2. The vehicle is kept on the employer's premises when not being used for business purposes;
3. No employee using the vehicle lives on the employer's premises;
4. The written policy prohibits personal use, except de minimis use; and
5. The employer believes that there is no personal use, except de minimis use.

Vehicles not used for personal purposes other than commuting

1. The vehicle is owned or leased by the employer and is provided to the employee for use in the employer's business;
2. The employee is required for bona-fide non-compensatory business reasons to commute in the vehicle;
3. The written policy prohibits personal use, except commuting or de minimis personal use;
4. The employee is not an elected official or earns less than an established amount per year;
5. The employer believes that there is no personal use, except de minimis or commuting use; and
6. The value of commuting is included in the employee's income.

Determining the Value of

Personal Use

General Valuation rule:

The amount included in an employee's wages for employment tax purposes due to personal use is determined by the fair market value of its availability. This is generally the cost of leasing the same car (or a comparable model) in an arm's length transaction from a third party on terms comparable to those found in the geographic area in which the car is used. An example of a comparable term is the amount of time that the vehicle is available to the employee for use, e.g., a one-year period.

Use the following formula to calculate the value of personal use under the fair market valuation rule:

$$\text{FMV} \times \frac{\text{Personal Use Miles}}{\text{Total Use Miles}} = \text{Personal Use Value}$$

Annual Lease Valuation Rule:

This rule is based on the fair market value of the car and is determined under the annual lease value table (see appendix A) provided by the Internal Revenue Service. This rule may be used only if it was adopted at the time a vehicle was first made available to an employee. The fair market value of the car, for purposes of calculating the annual lease value, may be deemed to be the employer's cost of purchasing the car in an arm's length transaction. The fair market value may also be determined by using the retail value of such car as reported in a nationally recognized publication that reports car retail values.

The IRS table is based on a four-year lease term. The annual lease value determined from the table remains in effect for the period that begins with the first date the valuation rule is applied by the employer and ends on December 31 of the fourth full calendar year following that date, if the car continues to be available to the employee. At the beginning of the fifth year (and every four years thereafter) the annual lease value must be re-determined based on the fair market value of the car on January 1 of that year. A recalculation must also be made if a car is transferred to another employee, based on the fair market value as of January 1 of the year of the transfer.

- ? *Example: Assume that an employee was provided a car in 2010 and that employee continues to use the car for personal purposes through 2014. The fair market value of the car was \$10,200 when it was made available. The annual lease value, according to the IRS table, was \$3,100. Include \$3,100 in taxable wages for 2010, 2011, 2012 and 2013. For 2014, the annual lease value of the car is required to be recalculated. Assuming that the fair market value of the car on January 1, 2014, is \$5,750, the annual lease value is re-determined to be \$1,850 (the annual lease value taken from the IRS table for the \$5,000 to \$5,999 value range).*

Maintenance and insurance are included in the annual lease value table because it is

assumed that the employer provides these services. The annual lease value table does not include the value of any fuel provided by the employer. This fuel may be calculated at fair market value or 5.5 cents per mile driven. This must be included in the employee's taxable wages.

Use of the annual lease valuation rule is optional. However, an employer may not use it unless it was adopted when the car was first made available to an employee for personal use. An employee may adopt the annual lease valuation rule only if the employer adopts the rule and only if adopted when the car was first made available to the employee. Once the rule is adopted it must be used for all subsequent periods (except when the commuting valuation rule is used).

- ? *Example: An employee is provided a car and allowed personal use during 2013. The fair market value of the car when it was made available, was \$14,500. The annual lease value for the \$14,000 to \$14,999 value range, taken from the annual lease value table, is \$4,100. The employee drove 20,000 total miles during 2013, of which 4,000 were personal miles. Calculate the personal use based on miles driven ($4,000/20,000=20\%$ personal use). The taxable value of employer provided fuel is \$220 ($4,000 \times 5.5$ cents). The employer is required to include \$1,040 ($\$4,100 \times 20\% + \220) in the employee's 2013, taxable wages for personal use of the car.*

Cents-per-Mile Valuation Rule:

The personal value may be calculated by multiplying the standard mileage rate by the number of miles the vehicle is driven for personal use. The cents-per-mile rule may be used only for a car that:

1. Is reasonably expected to be regularly used in the employer's business throughout the calendar year,
2. Is driven for at least 10,000 miles in a calendar year and used primarily by

employees, and

3. Has a fair market value less than an established, "luxury car" amount (see appendix B for applicable amount), on the day it was first made available to the employee.

Employer provided maintenance, insurance and fuel are included in the cents-per-mile rate. Once this rule has been adopted for a particular vehicle, the employer must continue to use this rule for this vehicle unless the vehicle no longer meets the requirements. However, a change to the commuting valuation rule is permissible.

Commuting Valuation Rule:

The value of the commuting use of an employer-provided car is \$1.50 per one-way commute, if the following requirements are met:

- 1) The vehicle is owned or leased by the employer and is provided for use in the employer's trade or business.
- 2) The employer requires the employee to commute in the vehicle for bona fide non-compensatory business reasons.
- 3) The employer has established a written policy forbidding the use of the vehicle for personal purposes other than commuting and "de minimis" personal use.
- 4) The employee does not use the vehicle for any personal purpose except commuting and "de minimis" personal use.
- 5) The employee, required to use the vehicle for commuting, is not a "control employee" of the employer. A control employee of a governmental employer is an elected official or an employee whose annual compensation exceeds an established amount.

Excluded Vehicles

Some vehicles, by nature, are not likely to be used more than a minimum amount for personal purposes and are excluded from wage considerations as a working condition fringe benefit. The exclusion from income as a working condition fringe benefit applies to the use of a qualified non-personal use vehicle because of its design and not because of the nature of the employee's services (such as being on 24 hour call). Additionally, the IRS does not require record keeping and substantiation by the employee for such vehicles.

Qualified non-personal use vehicles are:

- 1) clearly marked police and fire vehicles (see definition below);
- 2) ambulances and hearses;
- 3) any vehicle designed to carry cargo with a loaded gross weight of more than 14,000;
- 4) bucket trucks (cherry pickers);
- 5) cement mixers;
- 6) combines;
- 7) cranes and derricks;
- 8) delivery trucks with seating for the driver only or for the driver plus a folding jump seat;
- 9) dump and garbage trucks;
- 10) flatbed trucks;
- 11) forklifts;
- 12) passenger buses with a capacity for at least 20 passengers;
- 13) qualified moving vans;
- 14) qualified specialized utility repair trucks (see definition below);
- 15) refrigerated trucks;

16) school buses;

utility services.

17) tractors and other special purpose farm vehicles;

18) unmarked vehicles used by law enforcement officers if the use is officially authorized (see definition below).

Clearly Marked Police and Fire Vehicles

A clearly marked police or fire vehicle is defined as a vehicle owned or leased by the employer, that is required to be used for commuting by a police officer or fire fighter whom, when not on a regular shift, is on call at all times, provided that any personal use (other than commuting) of the vehicle outside the limit of the police officer's arrest powers or the fire fighter's obligation to respond to an emergency is prohibited by such employer. A police or fire vehicle is clearly marked if, through painted insignia or words, it is readily apparent that the vehicle is a police or fire vehicle. A marking on a license plate is not considered a clear marking.

Qualified Specialized Utility Repair Trucks

A specialized utility repair truck is defined as any truck (not including a van or pickup truck) specifically designed and used to carry heavy tools, testing equipment or parts if:

1. the shelves, racks or other permanent interior construction that has been installed to carry and store such heavy items is such that it is unlikely that the truck will be used more than a "de minimis" amount for personal purposes, and
2. the employer requires the employee to drive the truck home in order to be able to respond in emergency situations for purposes of restoring or maintaining electricity, gas, telephone, water, sewer or steam

Unmarked Law Enforcement Vehicles

Substantiation requirements do not apply to officially authorized uses of an unmarked vehicle by a law enforcement officer as long as a governmental employer owns or leases the vehicle, employs the officer and any personal use is incident to law enforcement functions. (Such as being able to report directly from home to a stakeout, surveillance site or to the scene of an emergency.)

A "law enforcement officer" means an individual employed on a full time basis by a governmental unit that is responsible for the prevention or investigation of crime involving injury to persons or property, who is authorized to carry firearms, execute search warrants and to make arrests and who regularly carries firearms.

Trucks and Vans

A pickup truck or van with a loaded gross vehicle weight not over 14,000 pounds is a qualified non-personal use vehicle if it is clearly marked with permanently affixed decals or with special painting or other advertising associated with the employer's trade, business or function and meets the following requirements. It is not such a vehicle unless it is specifically modified to be unlikely to have more than de-minimis personal use.

A pickup truck is a qualified non-personal use vehicle if it falls into one of the following two categories:

1. The truck is equipped with at least one of the following items:
 - a) a hydraulic lift gate;
 - b) permanently installed tanks or drums;
 - c) permanently installed side boards or panels materially raising the level of the sides of the truck bed; or
 - d) other heavy equipment, such as an electric generator,

welder, boom or crane used to tow automobiles and other vehicles.

2. The truck is used primarily for transporting a particular type of load, other than over the public highway, in connection with a construction, manufacturing, processing, farming, mining, drilling, timbering or other similar operation, and for which it was specially designed or significantly modified.

A van is a qualified non-personal use vehicle if it has a seat only for the driver or the driver and one other person, and either permanent shelving has been installed that fills most of the cargo area or the cargo area is open and the van constantly carries merchandise, material, or equipment used in the employer's trade, business or function.

NOTE: Internal Revenue Code Section 402(l)(4)(C) provides that the term "public safety officer" shall have the same meaning given such term by the Omnibus Crime Control and Safe Streets Act of 1968, as codified at 42 U.S.C. 3796b(9)(A). The definition of public safety officer is part of the Public Safety Officer's Benefits Act which was enacted as part L of Title I of the Omnibus Crime Control and Safe Streets Act of 1968. 42 U.S.C. 3796b(9)(A) defines public safety officer as "an individual serving a public agency in an official capacity, with or without compensation, as a law enforcement officer, a firefighter, a chaplain, or as a member of a rescue squad or ambulance crew."

The determination of the status of an individual as a public safety officer is made pursuant to a facts and circumstances analysis based on an evaluation of the relevant criteria in the Public Safety Officers' Benefits Act of 1978 and its regulations (PSOB Regulations, 28 CFR part 32). The PSOB regulations set forth criteria to be used in determining whether individual workers are public safety officers. For example,

the PSOB Regulations at 28 CFR 32.3 define "rescue squad or ambulance crew" as follows: a squad or crew whose members are rescue workers, ambulance drivers, paramedics, health-care responders, emergency medical technicians, or other similar workers who:

- (1) Are trained in rescue activity or the provision of emergency medical services; and
- (2) As such members, have the legal authority and responsibility to:
 - (i) Engage in rescue activity; or
 - (ii) Provide emergency medical services.

Rescue activity means search or rescue assistance in locating or extracting from danger persons lost, missing, or in imminent danger of serious bodily harm. Emergency medical services means:

- (1) Provision of first-response emergency medical care (other than in a permanent medical-care facility); or
- (2) Transportation of persons in medical distress (or under emergency conditions) to medical-care facilities.

As a general rule, the determination of the status of an individual as a rescue squad or ambulance crew member is based on whether that individual is trained to engage in rescue activity or to provide emergency medical services and whether that individual has legal authority and legal responsibility to engage in rescue activity or provide emergency medical services.

Thus, an individual's job title is not determinative of his or her status as a public safety officer. Instead, the determination is made based on the facts and circumstances of the individual's employment, including their training, legal authority and legal responsibility.

Appendix A - Annual Lease Value Table

<i>Automobile fair market value</i>	<i>Annual Lease Value</i>
\$0 to 999	\$ 600
1,000 to 1,999	850
2,000 to 2,999	1,100
3,000 to 3,999	1,350
4,000 to 4,999	1,600
5,000 to 5,999	1,850
6,000 to 6,999	2,100
7,000 to 7,999	2,350
8,000 to 8,999	2,600
9,000 to 9,999	2,850
10,000 to 10,999	3,100
11,000 to 11,999	3,350
12,000 to 12,999	3,600
13,000 to 13,999	3,850
14,000 to 14,999	4,100
15,000 to 15,999	4,350
16,000 to 16,999	4,600
17,000 to 17,999	4,850
18,000 to 18,999	5,100
19,000 to 19,999	5,350
20,000 to 20,999	5,600
21,000 to 21,999	5,850
22,000 to 22,999	6,100
23,000 to 23,999	6,350
24,000 to 24,999	6,600
25,000 to 25,999	6,850
26,000 to 27,999	7,250
28,000 to 29,999	7,750
30,000 to 31,999	8,250
32,000 to 33,999	8,750
34,000 to 35,999	9,250
36,000 to 37,999	9,750
38,000 to 39,999	10,250
40,000 to 41,999	10,750
42,000 to 43,999	11,250
44,000 to 45,999	11,750
46,000 to 47,999	12,250
48,000 to 49,999	12,750
50,000 to 51,999	13,250
52,000 to 53,999	13,750
54,000 to 55,999	14,250
56,000 to 57,999	14,750
58,000 to 59,999	15,250

For vehicles having a fair market value in excess of \$59,999, the Annual Lease Value is equal to: (.25 x the fair market value of the automobile) + \$500.