



## Taxation of Employees' Personal Use of Company Vehicles Simplified by New IRS Regulations

**Personal use of a company vehicle** generally results in taxable wages for the employee. But sorting out the amount to tax can be confusing. The following provides a high-level summary of the Internal Revenue Services' (IRS) current rules for taxing employees for their personal use of a company vehicle.<sup>1</sup>

The Tax Cuts and Jobs Act of 2017 (TCJA) drastically increased the maximum permissible base value for using special valuation rules for company vehicles. Recent **IRS proposed regulations** reflect those changes, including transition rules allowing employers to use the higher values for 2018 and 2019. Taxpayers may rely on the proposed regulations until final regulations are published.

### Background

If an employer provides an employee with a company vehicle that is available for the employee's personal use, in most cases, the value of the personal use must be included in the employee's wages. Accordingly, the value of such personal use is subject to both income and employment taxes, which the employer must withhold. Plus, the employer must pay its share of employment taxes on such amounts.

In calculating the value of an employee's personal use of a company vehicle, employers can use either the vehicle's fair market value (FMV), or one of two special valuation rules: (i) the "cents-per-mile" rule or (ii) the "average lease value" (ALV) rule, which includes a "fleet-average value" rule for employers with 20 or more vehicles that are available for employee personal use for an entire year. These special rules have additional requirements but are generally easier to apply than the FMV method.

However, neither of the special rules can be used if the FMV of the vehicle exceeds a base value, which is adjusted annually for inflation.<sup>2</sup> For 2017, which was the year before TCJA increased the base values, the cents-per-mile method could only be used if the FMV of the car placed in service during 2017 did not exceed \$15,900, from a \$12,800 base amount that had been adjusted for inflation. The 2017

inflation adjusted base for trucks or vans was \$17,800 and \$16,500 for fleet vehicles.

### TCJA Changes

TCJA expanded the availability of the two special rules by increasing the base amount for the cents-per-mile rule from \$12,800 to \$50,000 for all vehicles. TCJA also increased the base amount for the fleet-average value rule from \$16,500 to \$50,000, so that cars, trucks, and vans, even if fleet vehicles, are now all subject to the same base value dollar limit. The IRS released interim guidance explaining how these changes should be applied for 2018<sup>3</sup> and 2019,<sup>4</sup> which has now been formalized into proposed regulations.<sup>5</sup> The proposed rules also provide that the \$50,000 base value will be adjusted annually for inflation for 2019 and subsequent years. For 2019, the base value has been increased to \$50,400.

### Transition Rules

The proposed regulations include a transition rule for employers who did not qualify to use the fleet-average valuation rule before January 1, 2018, because they exceeded the maximum base value using pre-TCJA limits. Under the transition rule, employers may change to the fleet-average valuation rule for 2018 or 2019, provided the maximum values of \$50,000 for 2018 and \$50,400 for 2019 were met.

Similarly, the IRS has also proposed a transition rule for vehicles that were first made available to employees for personal use before 2018 if the employer did not qualify to use the cents-per-mile rule on the first day the employee used the vehicle for personal use because the vehicle's

<sup>1</sup> All references to Code, Section, or Regulation Section are to the Internal Revenue Code of 1986, as amended, and the Treasury Regulations promulgated thereunder, unless otherwise explicitly stated herein.

<sup>2</sup> Treas. Reg. § 1.61-21(e)(1)(iii)(A).

<sup>3</sup> Notice 2019-08.

<sup>4</sup> Notice 2019-34.

<sup>5</sup> Proposed Treas. Reg. § 1.61-21(d) and (e) issued August 22, 2019.



FMV exceeded the then-current limit but did not exceed the maximum values of \$50,000 for 2018 and \$50,400 for 2019. However, employers that adopt the cents-per-mile rule for a vehicle generally must continue to use that rule for all subsequent years in which the vehicle qualifies to use that rule.

### Insight

An employer who makes a change under these transition rules can amend Forms W-2 if necessary and file claims for any overpaid employment taxes.

## Summary of How to Tax Employees for Personal Use of Company Vehicles

### Part One: What is Personal Use of a Company Vehicle?

Personal use of a company vehicle occurs when an employee uses a company vehicle for any purpose that is unrelated to the employer's trade or business. Four common situations are discussed below.

#### 1. Employees with a regular place of work at a single location.

The cost of commuting from the employee's home to his or her regular place of work, such as an office, and vice versa is considered a personal expense. However, employees who leave their regular place of work for employer activities may have the following situations.

- *Transportation from employee's office to a temporary work location.* Such use is 100-percent business expense. Further, the trip from the temporary location to the employee's home is considered business miles in its entirety even when less than the mileage from the office to home, which would be personal commuting miles without the stop at the temporary work location.
- *Transportation from employee's home directly to a temporary work location without first commuting to the office.* The entire mileage from home to the temporary work location and home again is business mileage regardless of distance. However, if the employee drives to the office after the temporary work location, the transportation from the office to home will be personal mileage.

**2. Employees whose primary place of work is their home.** Employees who have a home office that qualifies as the employee's principal place of business (see [IRS Publication 587](#)) can treat all mileage to client sites and temporary work locations, including their employer's locations, as business miles.

**3. Employees with no regular place of business.** For employees with no regular place of business, i.e., no office provided by employer and their home office does not qualify as their principal place of business under the IRS guidance, mileage from home to a worksite is generally treated as personal commuting miles. Mileage between the first worksite and subsequent worksites is considered business miles. Mileage between the last worksite of the day and home is treated as personal commuting miles. However, if the employee drives directly from home to a temporary worksite *outside* the metropolitan area where the employee resides, then the mileage between the employee's home and the temporary worksite is treated as business miles. The same applies to the trip home from the temporary worksite outside the metropolitan area of residence. Generally, the metropolitan area is the city limit and the surrounding suburbs.

**4. Employees who take work vehicles home for safe keeping but who do not have any personal use other than the commute to and from work.** A special commuting valuation rule applies for employer-provided vehicles that are used entirely for business but required to be taken home by the employee. The distance between the workplace and the employee's residence remains personal commuting miles but can be valued at a favorable rate per commute. To apply the commuting valuation rule, a written policy should be in place that prohibits any personal use other than the commute.

### Part Two: How to Value Personal Use of a Company Vehicle

IRS rules require employers to impute taxable wage income to employees for employees' personal use of company vehicles. Employers have several methods to choose from in determining the value of such personal use. The two special methods that are commonly used for calculating the value of such personal use are discussed below.



**1. Cents-Per-Mile.** Employers may use the cents-per-mile method if the employer reasonably expects the vehicle to be regularly used by employees in the employer's trade or business throughout the year (or such shorter period as the vehicle may be owned or leased by the employer), or the vehicle is at least driven 10,000 miles.<sup>6</sup> If an employer wants to use the cents-per-mile rule, they must begin using it as of the first day on which the vehicle is used for personal employee use and generally must use it for all subsequent years that it qualifies. If the requirements for the cents-per-mile method are satisfied, then an employee's taxable amount for personal use of an employer-provided automobile could be calculated by multiplying the standard mileage rate by the total miles the employee drives the vehicle for personal purposes. For 2019, the **IRS standard mileage rate** for the use of cars, vans, pickups or panel trucks is 58 cents per mile driven for business use. However, employers should not also reimburse employees for fuel if they reimburse employees using the standard mileage rate, as that rate includes fuel.

### Insight

Currently, the IRS's standard mileage rate assumes a traditional gas-powered vehicle and does not yet include different rates for hybrid, electric or alternative fuel vehicles, which can have much lower fuel costs.

Any amounts paid to the employer for personal use of the automobile or excluded under a different Code section would reduce the amount taxable to the employee.

**2. Average Lease Value Rule (including Fleet-Average Value).** If the employer provides a vehicle to an employee for an entire year, the value of the benefit that is included in the employee's income is the Annual Lease Value (ALV) of the vehicle.<sup>7</sup> As discussed in greater detail below, the amount of the imputed income for this benefit is calculated by first determining the FMV of the vehicle as of the first day that the vehicle is made available to the employee and then using the table in the regulations<sup>8</sup> to find the ALV that corresponds to the vehicle's FMV.

- Determining FMV. Generally, the FMV is the vehicle's purchase price, including all amounts attributable to the purchase, such as sales tax and title fees.<sup>9</sup> Alternatively, the FMV may be determined by using the vehicle's retail value as reported in a nationally recognized pricing source that regularly reports new or used automobile retail values.<sup>10</sup> Other special rules may be used to determine FMV in the case of employer-leased automobiles.<sup>11</sup>
- Determining ALV. Once the vehicle's FMV has been determined, employers use the ALV table in the regulations to determine the ALV that corresponds to the vehicle's FMV. The amount of the ALV that is included in the employee's income is the portion relating to the availability of the vehicle for commuting and other personal use. Mileage records must be kept to determine what portion of the total automobile use is for personal purposes. Maintenance and insurance are included in the ALV.<sup>12</sup> However, fuel, whether furnished in kind (as from the employer's gas pump) or by reimbursement, is not included.<sup>13</sup> Special rules are available for valuing fuel furnished by the employer and used by the employee for personal purposes.
- Fleet-average valuation rule. An employer with 20 or more vehicles may average the FMV of all fleet automobiles that do not exceed the base value in the regulations, as indexed for inflation. The ALV for vehicles in the fleet must remain in effect for a period that begins with the first January 1 that the fleet-average-value rule is used and ends on December 31 of the subsequent calendar year. The value is calculated as of the first January 1 of such period. Employers may cease using the fleet-average value rule as of any January 1.<sup>14</sup>
- General valuation principles. If the valuation rules discussed above cannot be used, the value of the employer-provided vehicle may be determined under general valuation principles. That value is the FMV that an individual would pay to lease such vehicle in an arm's-length transaction in the same geographic area under similar or comparable conditions.

<sup>6</sup> Treas. Reg. § 1.61-21(e)(1).

<sup>7</sup> The value of vehicles provided for less than an entire year is a pro-rated Annual Lease Value or the Daily Lease Value.

<sup>8</sup> Treas. Reg. § 1.61-21(d)(2)(iii).

<sup>9</sup> Treas. Reg. § 1.61-21(d)(5)(ii)(B).

<sup>10</sup> Treas. Reg. § 1.61-21(d)(5)(iii).

<sup>11</sup> Notice 89-110. FMV may be based on the manufacturer's invoice price, including option plus 4 percent; or the manufacturer's suggested retail price less 8 percent.

<sup>12</sup> Treas. Reg. § 1.61-21(d)(3)(i).

<sup>13</sup> Treas. Reg. § 1.61-21(d)(3)(ii).

<sup>14</sup> Treas. Reg. § 1.61-21(d)(5)(v)(B).