

# Personal Use of a Vehicle – Consequences and Choices

By Dennis Walsh CPA

Most nonprofits operate a vehicle or will consider purchasing or leasing one at some point. Accordingly, you should be familiar with the IRS rules relating to personal use by organization personnel. The tax code treats the value of vehicle use not falling within your official activities as a taxable fringe benefit of employment. If you allow individuals in your organization to use a vehicle for personal purposes such as commuting, private errands, or other unofficial travel and don't comply with the IRS requirements, you're a sitting duck for a big headache, and the consequences might be more than you imagine.

If personal vehicle use is not properly reported to the IRS and by the user of the vehicle on his or her income tax return, there will be unreported income subject to tax, interest and penalty. The consequences to the organization may include penalties and interest for failing to withhold and remit employment taxes as well as for failing to report this compensation to the IRS and the employee.

In the case of an employee who is an insider, that is, an officer, director, or someone else in a position to exert substantial influence on management, the value of personal vehicle use is added to cash wages and other fringe benefits in determining whether the total compensation package is reasonable, or may have instead resulted in an excess benefit transaction. The value of an excess benefit must be returned to the nonprofit along with the payment of a 25% excise tax. Additional monetary sanctions may be imposed on the vehicle user and nonprofit as well.

Further, when an individual uses an organization vehicle personally, even if the person is not an insider, an issue of prohibited private inurement may result if the value of the personal use exceeds reasonable compensation for services performed as an employee. A nonprofit cannot tolerate any personal use of its assets, except where specifically authorized by law, without placing tax exempt status at risk.

How is personal use valued?

The fringe benefit value of vehicle Use for employees of for-profit and nonprofit organizations alike is based on a hypothetical lease value. In theory, this value is what you would pay for use of a vehicle in an 'arm's-length' lease with an unrelated person. The IRS has prescribed alternative rules to calculate a fair lease value that considers factors such as vehicle value, personal miles driven, and operating costs paid by the organization. In most instances it will be preferable to rely on one of the valuation rules rather than assuming the burden of proving that fair lease value is less than the IRS prescribed amount.

The following sections provide an overview of the specific requirements of each valuation rule.

### Cents per mile rule

The value of personal mileage for a vehicle used primarily in the activities of your nonprofit may be eligible to be determined under the cents per mile rule. You calculate the value of a vehicle made available for personal use by multiplying the standard mileage rate (48.5 cents for 2007) by the total miles driven for personal purposes. The resulting amount must be included in wages or reimbursed by the individual. This is the same rate used to reimburse an employee for business use of a personally owned automobile.

You cannot use the cents-per-mile rule for a vehicle if its value when first made available for personal use is more than \$15,100 for a passenger automobile or \$16,100 for a truck or van (2007 amounts, adjusted annually). Also, the vehicle must be driven at least 10,000 miles during the year to qualify for this method. The cents-per-mile rate includes the value of maintenance, insurance, and the value of fuel provided. If you do not provide fuel, you can reduce the rate by 5.5 cents.

### Lease Value Rule

If the facts do not satisfy the requirements of the cents per mile rule, the lease value rule is most likely to apply. Under this rule, you determine the value of an automobile you provide to an employee by using its annual lease value. The annual lease value is based on a hypothetical 4-year lease that takes into account an estimate for the decline in value of the vehicle over this period. The reportable value will remain the same for each of the four years unless use of the vehicle is transferred to another employee. If the vehicle is still in service at the end of the initial four year period, you will need to determine a revised lease value based on the vehicle's value at this later time.

If the employee uses the vehicle for both personal and business purposes, you generally reduce the reportable lease value to the extent the vehicle is used in the activities of your nonprofit. Alternatively, you can choose to include the entire lease value in the employee's wages, in essence requiring the employee to account to the IRS for business use instead of the nonprofit.

In this situation, the employee will need to follow IRS rules in order to account for any business use and then deduct the costs relating to such use of the vehicle on his or her individual tax return. However, because of limitations on the deduction of employee business expenses, it will normally be most advantageous to the employee to account to the nonprofit for business use. In this way, only the value of personal use is included in gross wages.

You determine the vehicle lease value from the annual lease value table in [IRS Publication 15B](#); using the vehicle's fair market value at the time it is first made available for personal use. If you provide fuel for personal use, you must include the value of the fuel as additional wages. You may value the fuel at cost or 5.5 cents per mile.

If the vehicle is made available for at least 30 days during the year but less than the entire year, the annual lease value is prorated based on the number of days available. If you provide an automobile to an employee for a continuous period of less than 30 days, you should use the daily lease value to figure its value. Refer to [IRS Publication 15B](#) for an explanation of the alternative computations of daily lease value.

### Special rules for commuting

There are two special rules for certain commuting arrangements. Both rules result in tax-favored treatment to the employee for commuting costs paid by the nonprofit. The commuting rule pertains to an employee commuting in an employer-provided vehicle. The unsafe conditions commuting rule applies to the purchase of commuting transportation for qualified employees.

### Commuting rule

If the personal use of a vehicle is limited to qualified commuting only, use of the commuting rule will normally be preferable to the other valuation rules. Under this rule, you determine the value of a vehicle you provide to an employee for commuting by multiplying each one-way commute, that is, from home to work or from work to home, by \$1.50. If more than one employee commutes in the vehicle, this value applies to each employee. This amount must be included in the employee's wages or reimbursed by the employer. You can use the commuting rule if all of the following requirements are met:

- You provide the vehicle to an employee for use in your nonprofit and, for bona fide non-compensatory reasons, you require the employee to commute in the vehicle. You can meet this requirement if the vehicle is generally used each workday to carry at least three employees to and from work in an employer sponsored commuting pool. This rule may also apply where a risk of theft or vandalism makes it prudent for the vehicle to be parked off site overnight or weekends.
- 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, such as a stop for a personal errand in route.
- The employee does not use the vehicle for personal purposes other than commuting and incidental personal use. Thus, you must look at how the vehicle is actually used each year to determine if this rule is available for a particular year.

- The employee who uses the vehicle for commuting does not receive more than \$100,000 in compensation. Obviously, Congress wasn't thinking of nonprofits when this requirement was added.

#### Unsafe conditions commuting rule

Under this rule, the value of purchased commuting transportation you provide to an employee, such as cab fare, solely because of unsafe conditions is \$1.50 for a one-way commute. This amount must be included in the employee's wages or reimbursed by the employee. Use of this rule may result in a tax-favored fringe benefit for qualified employees without access to a vehicle for commuting.

You can use the unsafe conditions commuting rule for employees that are paid hourly, not exempt from the payment of overtime wages, and whose compensation does not exceed \$100,000, if each of the following additional requirements are met:

- The employee would ordinarily walk or use public transportation for commuting.
- You have a written policy under which you do not provide the transportation for personal purposes other than commuting because of unsafe conditions.
- The employee does not use the transportation for personal purposes other than commuting because of unsafe conditions.

According to the IRS, unsafe conditions exist if, under the facts and circumstances, a reasonable person would consider it unsafe for the employee to walk or use public transportation at the time of day the employee must commute.

#### Last word

For the rules relating to the withholding and depositing of taxes on fringe benefits and reporting fringe benefits to employees, see [IRS Publication 15 \(Circular E\)](#), section 5. For a comprehensive discussion of the personal vehicle use valuation rules discussed in this article, refer to [IRS Publication 15B](#).

Finally, don't forget to make certain your vehicle insurance agent /carrier is aware of your policy and practices regarding personal use of vehicles. Your terms of coverage may limit or exclude vehicle use other than for official activities of your nonprofit, as stated in the insurance policy or policy application.

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