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Is the Value of a Take-Home Car Taxable?

An area of tax law which can cost an officer needless expense is the question of the taxability of take-home cars. Because, as a rule, all fringe benefits (which would certainly include a take home unmarked police car) are taxable under the sweep of Section 61 of the Internal Revenue Code, many municipal and county managers are under the mistaken impression this statute applies equally to take-home police cars. It does not.

Normally in this column I do not throw out many statutory citations, as it can quickly cause the reader's eyes to glaze over and lose interest. I will make an exception on this topic, however, so a PORAC member can go right to a manager with chapter and verse as to why their take home car is not income.

Section 132-1(a)(3) of the Code states: Gross income shall not include any fringe benefit which qualifies as a working condition fringe,

Then, Treasury Regulation 1.132-1(h)(1) goes on to say: 100 percent of the value of the use of a qualified non-personal use vehicle (as described in section 1.274-5T(k)) is excluded from gross income as a working condition fringe.

Treasury Regulation 1.274-5T(k)(2)(ii)(R) defines, among other things, a qualified non-personal use vehicle to include: Unmarked vehicles used by law enforcement officers (as defined in paragraph (k)(6) of this section) if the use is officially authorized

Treasury Regulation 1.274-5T(k)(6)(ii) says that "The term "law enforcement officer" means an individual who is 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 (including apprehension or detention of persons for such crimes), who is authorized by law to carry firearms, execute search warrants, and to make arrests (other than merely a citizen's arrest), and who regularly carries firearms (except when it is not possible to do so because of the requirements of undercover work).

Thus, in summary

- 1) Fringe benefits are normally income
- 2) Working fringe benefits are excluded from income
- 3) Qualified nonpersonal vehicles are working fringe benefits
- 4) Unmarked vehicles used by law enforcement officers are qualified non-personal vehicles
- 5) Law enforcement officers, for this purpose, are full-time armed and sworn members of an agency.

So if your members are given an unmarked take-home car, and they are full-time and armed, these vehicles may not be considered to represent income. This is a special, tax free fringe benefit.

Higher Income is not Always a Good Thing

As police incomes continue to rise, more and more of my clients are encountering some of the nasty surprises awaiting higher income earners. Among the most unexpected are the passive loss limitations which particularly affect taxpayers who own and manage rental property.

Rental activities are defined as passive under the Internal Revenue Code. As a result, in a normal tax year a loss on such an activity cannot be used to offset ordinary income, only other certain passive income. An exception exists, however, allowing a taxpayer to take a loss up to \$25,000 on a rental activity in which the taxpayer actively participates.

This exception, however, is “phased out” for taxpayers with adjusted gross incomes of between \$100,000 and \$150,000, whether they are single or married. At an adjusted gross income of \$125,000, for example, a loss of only \$12,500 is permitted. At \$150,000 the taxpayer may take no losses. The losses become “suspended” and may only be reclaimed if the taxpayer’s income falls in a subsequent year or the property is completely disposed of.

When two average California police wage earners marry, for example, and one or both have a rental, they will probably be blissfully unaware of these provisions because they will never have been affected as individuals. Their combined incomes, however, might easily send them right over the \$150,000 limit. If one or both taxpayers have relied on a loss from rental property to reduce income tax liability, they are in for a shock. Not only will the rental loss be completely disallowed in that year, the couple will be subject to the punitive nature of the so called “progressive” tax rates. When taxpayers double their income, as a result of marriage, for example, their tax does not double, it often triples or quadruples. Tax liability rises exponentially with a linear increase in income. This phenomenon also can include the loss of all child and educational credits. The result is more often than not a large tax bill for taxpayers used to a refund.

Keep Those Records

I know I sound like a broken record, but the enforcement activities of the IRS continue to increase. A simple calendar to log mileage to court, the range or off-site training can save the day years later if there is an audit. When donating property to charity, get receipts for everything and take photos of the property.

Another Scam

A tax scam against municipalities is making the rounds. Municipal organizations are being approached by unscrupulous tax preparers who offer, for a fee, to file refunds for

tax paid on fuel used by the municipality's fleet. Unfortunately, these claims are denied because most of the fuel was purchased tax-free anyway. By the time this is discovered, the preparers are gone.

A Later Filing Season

Contained in the latest budget bill is a provision extending the famous April 15 filing deadline to April 30 in order to encourage electronic filing. It remains to be seen whether this will actually encourage electronic filing or whether it will simply provide procrastinators with two more weeks to put off doing their taxes.