

## The Ins and Outs of Vehicle Expenses

A frequent question by clients involves the deduction of business related expenses for motor vehicles.

There are two acceptable methods for determining vehicle expenses. They are the flat rate mileage method and the actual expense method. Taxpayers, with certain exceptions, are entitled to use that method which yields the larger deduction.

### Business Purpose

In one of the most glaring differences between self-employed individuals and employees, the law is quite different regarding miles driven between the taxpayer's home and places of employment. For most employees, and certainly for all public sector employees, driving from home to a regular place of work is considered commuting, and commuting is considered to be a personal expense. For a few employees and any self-employed taxpayers who qualify to have a home office, driving from the office to any work site will be deductible mileage.

This discussion is not about having a home office, but in practicality the only employees who qualify for the home office deduction are those whose employer does not have any other kind of presence in the area where the taxpayer lives and works. A common example of such employees are insurance adjusters and pharmaceutical salespersons. These employees work out of their homes simply because there is no other office to go to. Their employers are based in far away cities and require these employees to work locally, thus necessitating the use of their homes for business purposes. Finally, in answer to a commonly asked question, employees who telecommute but who also have an office to go to do not qualify for a home office under the Internal Revenue Code.

### Reimbursement

A very important point is that only business expenses for which reimbursement is not available are deductible. In other words, if you could be reimbursed for an expense, but because of the difficulty or burden of the reimbursement process you choose not to, you will not be able to legally deduct anything. Taxpayers do not have a "choice," of tax benefit or reimbursement. If reimbursement is available, therefore, no deduction is available.

### Mileage Logs

Keeping accurate logs of vehicle mileage is required no matter which method is selected. Don't be fooled by the fact one method is called the "mileage" method and the other is not. Always keep these records. You are not required to keep actual odometer readings. Instead, for each day a vehicle is driven for business you should record the number of miles driven, the origin and destination and the business purpose.

For many taxpayers, some of these elements will be self explanatory and need not be recorded. When a police officer, for example, has mileage incurred in response to a subpoena and must go to Superior Court in, for example, Santa Monica, a simple notation like "SM Court." will suffice, especially if the travel is always from home on a day off. The business purpose is self evident and the mileage from home to the court will always be the same. A single entry of the number of miles involved in this trip on the very first entry of its kind will support all other entries of a similar nature for purposes of calculating mileage.

On the other hand, once a year type entries might require more detail. If there is a range training day once a year, for example, the entry would have to be far more detailed because the purpose would otherwise not be clear. That entry would look something like this, "Range Training – Ramirez Canyon, 60 miles."

### The Physical Log

As a rule, the more sophisticated role driving takes in your business, the more fastidious you must be in record keeping. Real estate agents, for example, should be keeping detailed logs in professional logbooks because mileage is a very large part of their business and represents an important expense which must pass exacting scrutiny. Law enforcement officers, on the other hand, would do just as well not to try and keep a small log which might be neglected or even lost. A wall calendar, with a pen attached by a string, located near the garage is actually the best solution for the profession. The calendar is easy and convenient to update for unreimbursed business trips and will not get lost. Only a few minutes each year to add up trips to court, the range, the dry cleaners, uniform stores and training will yield an accurate, well documented tax deduction.

### The First Choice - Flat Rate Mileage

This is by far the easiest method for most employees, including most public safety professionals. Using a log, as described above to substantiate the mileage, the taxpayer merely multiplies the applicable rate for a given period by the number of miles to arrive at a deduction amount. As long as proper documentation is used, this is the easiest method to deduct business mileage.

In addition, the Treasury Regulations, which supplement the Internal Revenue Code, allow some taxpayers to just use a sample of their mileage during the year instead of keeping records for every day. This is appropriate where the taxpayer can demonstrate his or her mileage is very consistent. A good example of this is a salesperson that has a consistent route, where the same customers are visited on a regular basis. Another good example may be seen in the miles driven by physicians who are assigned to the same outlying facilities on a regular basis. However, I do not recommend this for public safety officers because of the irregularity of court, training and range visits.

Flat rate mileage takes into account all vehicle expenses, with two exceptions, which apply only to self-employed persons and do not apply to employees. These exceptions are

interest on financing for the vehicle (only if the vehicle is owned, not if it is leased) and fees paid to DMV for registration. Both of these expenses are deductible in the same proportion as the business miles represent of total miles driven.

### The Second Choice – Actual Expenses

Instead of just using a flat rate for mileage, taxpayers may elect to use their actual expenses. These expenses include fuel, repairs, tires, insurance, car washes, financing interest or lease fees, DMV fees and finally, depreciation. Because of depreciation, large benefits are possible using this method if the vehicle is of a special type (such as a panel truck) or weighs over 6000 pounds (Gross Vehicular Weight Rating).

The taxpayer must keep records on all these expenses individually. At the conclusion of the year these expenses become deductible in the same proportion as the business use of the vehicle. If, for example, a vehicle is driven 10,000 miles during the year for both business and personal use, and 40%, or 4000 of these miles are logged as deductible business miles, then 40% of the total expenses will represent the deduction available. The other 60%, because they represent a proportional share of personal expenses, will not be deductible.

Once a taxpayer has used actual expenses for a vehicle, a change to the flat rate mileage method is no longer permitted. In addition, the use of accelerated depreciation, which can yield huge tax benefits, must be used cautiously because of the restrictions which may result in unexpected taxable income when the depreciated vehicle is later sold.

### Proof of Mileage

A little known item the IRS likes to see during an examination is proof of total mileage. This means a document showing the odometer reading near the beginning and end of the year. This is the only time an odometer reading is really relevant. It is most easily accomplished by having a professional oil change, or other shop work done, once a year in either late December or early January. The difference between the two odometer readings should accurately reflect the total number of miles driven on that vehicle during the year. By the same token, when a new vehicle is acquired and an old one sold, these documents should be preserved because odometer readings are a part of the sales transaction.