Automobiles under the Tax Cuts and Jobs Act of 2017

By: Ellen S. Brody, JD, CPA, Esq., and Cory M. Paul, JD

Published Date: Mar 1, 2020

The Tax Cuts and Jobs Act (TCJA) has dominated headlines since its passage in late 2017. More than two years later, the tax and accounting community are still trying to implement all of its changes, as final regulations are issued piecemeal for various IRC provisions modified by the TCJA. While much press coverage is given to clarifications of big-ticket items, such as qualified opportunity zones and the long-term effects of the TCJA as a whole, it is important to remain aware of the myriad smaller changes that were also enacted.

One such modification was an update to IRC section 280F(a), concerning the limits on depreciation deductions for automobiles (including some trucks and vans). Prior to the TCJA, the limitation was $12,800 of depreciation recovery over a five-year period, adjusted yearly for inflation. The TCJA’s authors recognized that an approximately $13,000 cost no longer accurately reflected the purchase price of a typical automobile—let alone a luxury vehicle. Accordingly, IRC section 280F(a) was amended to allow depreciation deductions of approximately $50,000 over five years, more closely approaching the modern concept of a “luxury automobile.”

These changes were undoubtedly welcome, but the regulations still in effect were based on the lower dollar value for a luxury automobile that had been previously reflected in this IRC section. In February 2020, however, the Treasury Department issued final regulations that made conforming changes to the updated figures in IRC section 280F(a). In particular, IRS Final Rules (T.D. 9893) updates the rules used by employers to value a fleet of vehicles in determining the amount of fringe benefit income properly attributable to their employees who make personal use of the vehicles.

Valuing a Fleet

When an employer provides a vehicle for an employee’s use and that use is not exclusively restricted to time spent on the job, the employee is deemed to have a certain amount of income due to her ability to utilize the vehicle for personal reasons. The standard methodology for the employer to value that benefit is conceptually simple: the income to the employee equals the fair market value of the use of the vehicle. In the Treasury Regulations, fair market value is spelled out as “the amount that an individual would have to pay in an arm’s-length transaction to lease
the same or comparable vehicle on the same or comparable conditions in the geographic area in which the vehicle is available for use.”

That methodology sounds relatively easy when calculating the fair market value of a single car provided to one employee for an entire year. The employer determines the fair market value of the vehicle, then uses IRS tables to find the “annual lease value.” The annual lease value is then multiplied by the percentage of the employee’s personal use of the vehicle to determine an amount includible in income. But what if the employer provides cars to a hundred employees? What if it provides cars to employees in the form of a fleet, and each night the employees might go home in different cars? Determining the fair market value of each employee's fringe benefit income becomes much more complicated.

The regulations recognize this, however, and provide special valuation alternatives. For employers with a fleet of vehicles, the regulations provide a fleet-average valuation rule under Treasury Regulations section 1.61-21(d)(5)(v), which allows an employer with a fleet of more than 20 vehicles to, generally speaking, use the average fair market value of the fleet to determine the fair market benefit received by each employee who has access to the fleet. There is an important caveat, though: no luxury vehicles are allowed under this method. Prior to the February 2020 amendments, the regulations relied on an outdated fair market value limitation, which meant that any vehicle costing more than $16,500, as adjusted annually for inflation, was excluded from the fleet-average valuation and had to be accounted for separately.

A second special valuation rule permits the personal use of vehicles to be valued on a cents-per-mile method. Treasury Regulations section 1.61-21(e) provides that vehicles that are driven at least 10,000 miles per year for the benefit of the employer, and that the employer regularly expects to be used in its trade or business, can be valued as a taxable fringe benefit for the employee by multiplying the employee’s personal use mileage by a standard cents-per-mile rate. Much like the fleet-average valuation rule, however, this methodology is restricted to vehicles below a certain value. In this case, the prior regulations explicitly limited this special valuation rule to $12,800 as adjusted for inflation, which in 2017-dollar terms, meant that a passenger vehicle could only be valued on a per-mile basis if its fair market value was $15,900 or less.

The February 2020 final regulations brought both of these special valuation rules into conformity with the new IRC section 280F(a) standard by allowing employers to utilize the fleet valuation and the cents-per-mile methods for vehicles with a fair market value of $50,000 or less. This change simplifies matters by eliminating the different maximum vehicle fair market values in the old fleet valuation and cents-per-mile regulations. The effective date is for taxable years beginning on or after Feb. 5, 2020, but a special provision allows the $50,000 figure to be used in the special valuation rules for tax years beginning on or after Jan. 1, 2018, if the taxpayer so elects.

As a practice matter, these regulations provide an opportunity to review the methodologies that clients use when providing vehicles for employee use, and perhaps to offer simplifications. It is also possible that employers, having been advised of the difficulty of meeting the fleet or cents-per-mile valuation standards in prior years, may choose to revisit the costs and benefits of having a fleet available for employee use.
Unreimbursed Employee Expenses

The calculus for employers concerning the decision to provide vehicles for employee use may also be impacted by a more commonly discussed TCJA provision: the elimination, at least for now, of an individual’s ability to deduct from income any unreimbursed business expenses, including gas and vehicle expenses.

IRC section 67(g) prevents any individual from taking miscellaneous itemized deductions for the taxable years 2018 through 2025. Nonetheless, cases under the prior law are still being decided in the courts. And because issues of personal versus business use of vehicles are still relevant for employers, these decisions are worth discussing.

In the recent Tax Court case *Christensen v. Commissioner*, deductions claimed by the taxpayer for unreimbursed vehicle mileage expenses were disallowed. The case clarifies some rules related to the distinction between commuting expenses, which are generally treated as personal nondeductible expenses—even under the old IRC section 67 rules—and business expenses for which a deduction was allowed prior to 2018.

Dean Christensen was a part-time professor who taught at two separate campuses, one located one mile from his home and another approximately 25 miles away. Generally speaking, travel from one work site to another is a business expense, while commuting from home to the job is a personal expense. Christensen kept his students’ records under lock and key in his office at the campus near his home, so he visited this campus every morning, even when his work for the day was at the other campus. He took the position that the trip from the first campus to the second was a business expense, as opposed to a commuting (and personal) expense.

But Christensen’s employer did not require him to keep students’ records locked up at his campus office. Quite curtly, the Tax Court reminded Christensen (and all of us) that personal choices of this nature, while perhaps prudent and even reflective of best practices, do not generate business expenses when not explicitly required by the employer. A level of personal fastidiousness does not convert a personal choice into business travel.

While working as a professor, the taxpayer was also the sole shareholder, employee, and president of CYBER, a corporation in the business of providing software solutions for training and educational purposes. Ostensibly for CYBER, the taxpayer drove multiple times across the country to meet with individuals he believed would be useful in acquiring clients or improving the business, which had not had a client in more than five years. He deducted his vehicle mileage expenses related to these trips as well.

To tell the end of the story first, Christensen’s vehicle mileage expenses for CYBER were dismissed as perfunctorily as his mileage as a professor. But the Tax Court’s rejection is informative in terms of what the Tax Court looked for—and what it found lacking.

Most of Christensen’s cross-country trips were to Nevada. While he claimed to be considering relocating CYBER, he could not provide the Tax Court with any rationale for this relocation. The only recorded individual he visited on any trip to Nevada was a friend of his, and the Tax
Court noted that this friend had become Christensen’s spouse by the time of trial. While the court wasn’t explicit, it heavily implied that there had been an ulterior motive to Christensen’s visits.

His other travels for CYBER involved a trip on Christmas Eve and Christmas, but he had no explanation as to whom he spoke with or how it benefited CYBER. He also took a deduction for travel of about 3,500 kilometers in Norway but admitted to the Tax Court that not only were any such expenses not valid business expenses, he had no evidence to show that he had used a car at all during the trip.

While Christensen likely had some travel during the year with CYBER at the forefront of his mind, without documenting his mileage accurately and without being able to articulate a clear purpose, he was not persuasive in the context of an audit or a Tax Court proceeding. Pairing some of these expenses with others that had a distinct air of vacation or courtship undoubtedly made it easier for the court to wind its way to a complete dismissal of all of the mileage. This is an important reminder to keep detailed records and keep business and personal expenses separate.

Implications

The more minor—yet important—changes brought about by the TCJA impact both companies and individuals. As a result, tax professionals would do well to familiarize themselves with these matters and remain abreast of Tax Court proceedings in order to best inform their clients.

This article originally appeared in the March 2020 TaxStringer and is reprinted with permission from the New York State Society of Certified Public Accountants.

**Ellen S. Brody, JD, CPA, Esq.,** is a partner at Roberts & Holland LLP. Ms. Brody can be reached at 212-903-8712 or ebrody@rhtax.com.

**Cory M. Paul, JD,** is an associate at Roberts & Holland LLP. Mr. Paul can be reached at 212-903-8774 or cpaul@rhtax.com.