DOERING LEASING CO.

TRENDS & TOPICS

CONSEQUENCES OF DRIVER REIMBURSEMENT & ALLOWANCE PROGRAMS

By Adam Berger, Vice President

Organizations often look at replacing company owned or leased vehicles with a driver reimbursement or allowance program. Such programs are touted as reducing administration and transferring liability.

1. **Liability is Not Transferred to Employee:** The organization is liable for driver behavior during business hours no matter if the vehicle being driven is a company vehicle or an individual's vehicle. A strong corporate auto policy stating that company vehicles must not be used for personal use outside of business hours is a key step in overcoming any non-business-hour liabilities. Liability is effectively increased through reimbursement because the company can not regulate how an employee maintains their personal vehicle (used during business hours).
2. **Taxable Income:** Monthly car allowances are taxable income to an employee, subject to federal and state income taxes. A $600 monthly car allowance incurs an estimated tax liability of $240, leaving the employee with a net allowance of only $360/mo for car + fuel + insurance.
3. **Social Security Taxes / FICA:** Monthly car allowances are also subject to FICA withholding taxes of 7.65% for the employee **and** employer, reducing the employee's net to $314 and costing the organization another $45.90/month. FICA taxes can not be reduced by itemizing deductions.
4. **AGI Threshold:** The IRS allows employees to deduct un-reimbursed business-related expenses by itemizing deductions. Not all taxpayers do this. If a taxpayer does not itemize, they are not eligible for any tax deductions for the use of a personal vehicle for business purposes. The 2% AGI floor means that business related expenses must exceed 2% of AGI before the first dollar may be deducted. This significantly limits the tax benefits of business related vehicle expenses (even more so for married filers filing a joint return).
5. **Interest Payments Not Deductible:** Interest payments implicit in a finance or lease are not deductible to an individual, even when used as a business vehicle. The restriction does not apply to businesses financing or leasing vehicles – the expense is deductible/expensed!
6. **IRS Audit Prone:** The audit rate for individuals claiming business related vehicle and mileage deductions is substantially higher than the typical taxpayer. The burden falls on the taxpayer to substantiate all business-related vehicle expenses or risk them being disallowed.
7. **** Exaggerated Mileage Reports:** When a per-mile reimbursement plan is used, studies have shown that employees are exaggerating mileage reported by 30% on average. Such reimbursement programs are subject to a high level of administration, skepticism, and fraud. Employees view them as a secondary source of income commonly.
8. **** Turnover Increased:** The best organizations are comprised of the best people. They should be protected, defended and retained. Studies have shown that employee turnover increases by over 10% "when companies go to a driver reimbursement from a company-provided vehicle," says Jim Fredlund of General Electric.
9. **BOTTOM LINE: Company vehicles remain the preferred method.**