



**Johnson County Auditor**  
Johnson County, Kansas  
**PERFORMANCE AUDIT**

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**May 24, 2007**

**Review of Take Home Vehicles**

*"The County must consider and ensure personnel understand  
the tax implications of using take home vehicles"*



## Johnson County Audit Services

May 24, 2007

To: The Johnson County Board of County Commissioners  
Michael Press, County Manager  
Tom Franzen, Director of Financial Management

In accordance with the approved audit plan, we performed a County-wide audit of the use of employee take home vehicles. Our objectives were to identify how many take home vehicles were assigned to employees, if the vehicles met IRS fringe benefit exemptions or were properly reported for tax purposes, and if departments and agencies complied with Johnson County policies, procedures, and internal controls applicable to these vehicles.

The audit disclosed that most of the directors were not aware of proper procedures for recording the use of the take home vehicles and the tax implications for the County and the employees applicable to these vehicles. As a result, 53 of the 67 County take home vehicles lacked proper documentation and reporting. This exposes the County and the affected employees to assessments for past due taxes. Since there is no County policy or procedure, immediate interim action will be needed to ensure proper tax withholding and to prevent continuing tax liabilities from mounting. (*See page 1*)

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards, except that Peer Review has not been performed. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence that provides a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

I appreciate the cooperation received from County staff during this audit.

William D. Miller, CIA, CGFM  
County Auditor

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**REVIEW OF TAKE HOME VEHICLES**

**TABLE OF CONTENTS**

	<b><u>Page</u></b>
<b>RESULTS AND RECOMMENDATIONS</b> .....	1
Taxable Fringe Benefits for the Use of Take Home Vehicles Have Not Been Reported.....	1
Recommendations.....	1
Management Comments .....	1
Discussion.....	2
<b>APPENDIX</b>	
OBJECTIVES, SCOPE AND METHODOLOGY .....	7

## **RESULTS AND RECOMMENDATIONS**

### **Taxable Fringe Benefits for the Use of Take Home Vehicles Have Not Been Reported**

Department and agency directors did not have appropriate guidance to ensure they managed take home vehicles properly and accounted for the taxable fringe benefits associated with these vehicles. The directors made their own interpretations of allowable tax-free uses of vehicles which did not coincide with federal tax reporting requirements. Most departments had no mileage records or logs to segregate business and personal use mileage. The lack of records results in the required use of Federal default criteria for determining what is or what is not taxable as a fringe benefit as well as the timing and amount of reported income for employees. Most directors believed the assignment of the vehicle based on the County's need for services on a 24/7 basis justified the vehicle as "business use only" and did not require categorization of any vehicle use as a fringe benefit. Operating in this manner subjects the County to a high risk of assessments for past due taxes and subjects the employees to the risk of large, and unexpected, tax assessments.

### **Recommendations**

We recommend the County Manager and the Director of Financial Management:

- 1.1 Develop an interim solution providing immediate guidance to the departments and agencies which currently allow take home vehicles. This solution should be designed to minimize the impact on the County and employees until a more permanent solution can be devised. It should include:
  - Minimum requirements for business use documentation,
  - Notification to affected employees describing the potential impact of the situation, and
  - Making elections under the Internal Revenue Code that will best serve the County's and employees' interests.
- 1.2 Develop and adopt a policy or procedure which:
  - Clearly defines the minimum recordkeeping requirements for take home vehicles,
  - Provides for timely withholding for income and payroll taxes, and
  - Provides the affected employees with sufficient notice and information to properly plan payment for the related taxes.
- 1.3 Take action deemed necessary to comply with the Internal Revenue Code and regulations for take home vehicles.

### **Management Comments**

- 1.1 *Instead of developing an interim solution, OFM has chosen to quickly develop permanent procedures addressing take home vehicles. The new procedures will address the County's method for IRS compliance on the personal use of County-*

*owned vehicles, provide explanation on County-owned vehicles that are tax exempt, provide guidance on motor pool vehicles, and supply administrative guidance on matters such as recordkeeping, etc. These procedures were communicated with the E-Team during the May meeting.*

- 1.2 *OFM staff has worked with Human Resources and Legal Services staff to develop a new Human Resources procedure that addresses the taxable fringe benefit of vehicles to include: 1) a Personal Use of County-Owned Vehicle agreement form; and 2) an Employee Personal Use Commuting Log form that will be submitted monthly to OFM –Payroll for payroll processing.*
- 1.3 *OFM believes that the creation of the new “Taxable Fringe Benefit – Vehicles procedure (301-13)” and the existing “Use of County Property – Take Home Vehicles procedure 404-3” will provide the necessary guidance to direct departments to comply with Internal Revenue regulations. OFM will confirm departmental understanding after the initial reporting period.*

### **Discussion**

Johnson County provides “take home vehicles” to some of its employees. A “take home vehicle” is a County owned or leased vehicle which the employee keeps at his or her place of residence. This arrangement is made when County management believes that such an arrangement is in the best interest of the County. This most commonly occurs in those departments or agencies that have 24/7 response duties such as MED-ACT, Public Works, and Emergency Management.<sup>1</sup> Over time, the practice has expanded to allowing take home vehicles when the employee regularly attends after-hours meetings or has occasional after-hours response duties.

#### **Kansas law addresses take home vehicles**

K.S.A 8-301 prohibits the use of publicly owned vehicles for private use. In 1993, the Kansas Attorney General issued opinion 1993-077 which provided that take home vehicles can be used for incidental private use when the employee was responsible for 24/7 response.

#### **Take home vehicles are considered fringe benefits unless otherwise justified**

The United States tax code and the related Internal Revenue Service (IRS) regulations generally treat a take home vehicle as a taxable fringe benefit. The value of the fringe benefit is included in the employee’s income and is subject to payroll taxes such as Medicare and Medicaid. The employer providing the vehicle is required to withhold taxes based on the income and provide matching Medicare and Medicaid contributions as with any other employee compensation.

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<sup>1</sup>This review does not cover marked or unmarked police cars. Both are exempt from the general rules related to take home vehicles.

IRS Publication 15B (Pub 15B) provides a readable summary of the tax law and the related regulations along with a complete guide for employers in calculating the taxable portion of the fringe benefit and providing some safe harbor rules for reporting. The value of the take home vehicle is based on the lease value of the vehicle plus any additional employer provided benefits, such as fuel. The IRS provides a table for converting vehicle cost to lease value and a value of 5.5¢ per mile for the fuel. The total value determined is then prorated to business and personal use based on mileage logs.

Pub 15B also provides detailed instructions on determining when a take home vehicle is exempt from the fringe benefit category. The exemptions fall into a number of categories but the primary exemptions are for marked police vehicles, other special function vehicles, and for vehicles that have permanently installed equipment and/or storage that effectively precludes their use for personal transportation. These exemptions include ambulances, hearses, vehicles with a gross loaded weight exceeding 14,000 pounds, and vehicles seating more than 20 persons.

There are specific exemptions from fringe benefit rule

### **How we conducted the audit**

We identified pertinent Federal and State laws and County policies and procedures relating to the uses of and accounting for take home vehicles. We also reviewed Attorney General opinions as appropriate.

K.S.A. 8-301, as noted above, precludes the use of publicly-owned vehicles for private uses.

Johnson County adopted policy 404-1 which regulates the incidental use of County equipment and 404-2 which regulates the operation of County owned and leased vehicles and the use of personal vehicles. Neither of these policies specifically describes the use or restriction of uses for take home vehicles.

Attorney General's Opinion 1993-077 indicates that the prohibition included in KSA 8-301 does not include the incidental personal use of a 24/7 publicly-owned take home vehicle.

IRS Publication 15B – *Employer's Tax Guide to Fringe Benefits* identifies the requirements for documenting use of take home vehicles and calculating the value to be used to determine the amount of tax liability for a fringe benefit.

### **Twelve departments allow some employees to take home County vehicles**

We asked all County department directors to declare the number and assignment of take home vehicles for their employees. Table 1.1 identifies the 12 departments reporting take home vehicles and the number of vehicles assigned as of January 1, 2007.

**Table 1: Distribution and Attributes of Take Home Vehicles**

Department or Agency	Take Home Vehicles	Exempt Vehicles <sup>2</sup>	Vehicles with Mileage Documented	Vehicles with Income Reporting
Med-Act	13	0	0	0
Parks & Recreation	11	1	5 <sup>a</sup>	5
Airport	10	3	0	0
Public Works	10	3	0	0
Sheriff	7 <sup>b</sup>	1	0	0
Emergency Management	4	0	0	0
Emergency Communications	3	1	0 <sup>c</sup>	0
Planning	3	0	0	0
Corrections	2 <sup>d</sup>	0	0	0
Development Supports	2 <sup>e</sup>	0	0	0
District Attorney	1 <sup>f</sup>	0	0	0
Risk Management	1	0	0	0
<b>Totals</b>	<b>67</b>	<b>9</b>	<b>5</b>	<b>5</b>

<sup>a</sup> Parks & Recreation recorded personal mileage rather than business mileage as required by the IRS.

<sup>b</sup> We did not include marked or unmarked police cars in the scope of our review.

<sup>c</sup> These vehicles were assigned to the Sheriff prior to January 1, 2007. Since that time, appropriate mileage logs have been maintained.

<sup>d</sup> These vehicles were assigned to employees who are no longer employed by Johnson County. Both vehicles were used for part of the period from 2004 to 2006.

<sup>e</sup> One of these vehicles was assigned for a short time to an employee until he left Johnson County employment.

<sup>f</sup> This vehicle is not currently assigned to an individual because that individual lives at a distance from Johnson County. The vehicle was assigned for most of the time from 2004 to 2006.

Source: The information in this Table was collected by interview and observation during the audit.

### County departments did not understand the tax implications of take home vehicles

The County does not have a policy or procedure which provides guidance to the departments and agencies on the handling of take home vehicles. As a result, department staffs did not prepare mileage logs documenting the business use of take home vehicles. Also, except for the Parks and Recreation Department, department staffs did not report the income resulting from the availability of the take home vehicles.

Our interviews with department directors and staff disclosed a general lack of knowledge regarding record keeping and reporting for business and personal use of these vehicles. Personal use is taxed as a fringe benefit.

<sup>2</sup> Exempt Vehicles – exempt from personal use designation by federal regulation. Mileage logs and tax reporting are not required.

We focused on the following IRS requirements which must be fulfilled to determine the proper tax amount for personal use and withholding amount for employee W-2s.:

- Were trip logs<sup>3</sup> kept for the business mileage for each vehicle?
- Were beginning and ending odometer readings recorded for each vehicle on an annual basis?
- Did any of the vehicles meet the IRS requirements for exclusion from the personal use category, for instance marked police cars, substantial permanent installation of equipment which reduced the personal use capacity of the vehicle?
- Did the County provide fuel for the vehicle?

The Department of Parks and Recreation maintained records and reported the fringe benefit aspect of personal use for inclusion on the employees' W-2 tax forms. They recorded personal use rather than business use. However, this approach was only applied to their administrative fleet not their operational fleet. None of the other departments maintained logs of vehicle use to identify business use and did not segregate business use from personal use.

Most of the departments designated the take home vehicles as needed for some emergency response on a 24/7 basis. Generally, the departments do not allow personal use of the vehicle and considered all mileage as business mileage. This does not comply with IRS tax code which explicitly states that commuting miles are taxable as fringe benefits. Commuting miles are generally categorized as the first trip from the residence to the first business location, and the last trip from a business location to the personal residence. Additionally, under the tax code, if the employee does not supply mileage logs to departments specifically addressing each trip, the full lease value of the vehicle must be included in the employee's income.

Commuting miles  
are taxable

### **Take home vehicle assignments may need re-evaluation**

We did not attempt to determine if the assignment of a take home vehicle was appropriate. We believe this is a management decision based on organization needs. Since the justifications for the take home vehicles were based on broad definitions of what does or does not constitute a business need, there was no criterion to measure the management decision. However, by observation there are instances that appear to be reviewable by management.

One employee has a full time take home vehicle and in 7 years has used the vehicle for 4,540 business miles or 649 miles per year. The vehicle is driven mainly for commuting purposes based on total mileage of 8,000 miles accumulated since 1999.

Several employees have vehicles for 24/7 emergency response needs but responded in the interviews that such response after normal work hours is rare – in one case once or twice a year.

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<sup>3</sup> Trip logs would include beginning and ending odometer reading, destination, and business purpose for each business use of the vehicle.

The justification for the assignment of a take home vehicle should be based on criteria that account for a variety of County needs and missions and also on the cost benefit to the County.

### **Conclusion**

Lack of county-wide guidance on the treatment of take home vehicles resulted in failure to properly document the use of the vehicles and to properly report the fringe benefit income associated with the vehicles. In most cases, the agencies and departments assigning take home vehicles were not aware of tax implications for the County or their employees. This has resulted in high risk for the County and potential monetary penalties for the employees.

## **OBJECTIVES, SCOPE AND METHODOLOGY**

### **Objectives**

The objectives of the audit were to:

- 1) Identify how many vehicles are assigned Johnson County employees
- 2) Determine if Johnson County take home vehicles meet the IRS fringe benefit exemption criteria and, if not, whether they are properly reported for tax purposes
- 3) Review and test compliance with Johnson County policies, procedures, and internal controls applicable to the take home vehicles

### **Scope and Methodology**

In order to accomplish these objectives we:

- (1) Reviewed applicable county-wide and departmental policies and procedures,
- (2) Interviewed agency and department officials and administration,
- (3) Reviewed applicable laws, rules and regulations applicable to take home vehicles,
- (4) Consulted with legal staff regarding the application of Kansas law, and
- (5) Determined whether the County and the department had properly handled the income reporting requirements for the assigned vehicles.

Verification steps included inquiries about vehicles, inquiries about W-2 reporting to verify that vehicles have been declared as income where necessary, and review of vehicle logs to determine business/non-business use.