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CLAIMING MOTOR VEHICLE DEDUCTIONS

— by Neil E. Harl*

A taxpayer may, on a yearly basis, deduct an amount equal to either (1) the business standard mileage rate (at 28 cents per mile for all business miles for 1992) times the number of business miles traveled or (2) the actual costs (both operating and fixed) paid or incurred by the taxpayer allocable to business miles.¹

Standard Mileage Allowance. A taxpayer using the standard mileage method of computing deductions for business use of a motor vehicle makes an automatic election to exclude the vehicle from the Modified Accelerated Cost Recovery System (MACRS).² Moreover, there is no provision for motor vehicles once removed from MACRS (or ACRS) to again become recovery property. If the taxpayer shifts to the actual cost method in a later year, which is permissible, depreciation may be claimed over the estimated useful life of the vehicle but only at the straight line rate.³

For motor vehicles under the standard mileage allowance, depreciation is considered to have been allowed at the rate of seven cents per mile for 1980 and 1981, seven and one-half cents per mile in 1982, eight cents per mile in 1983, 1984 and 1985, nine cents per mile for 1986, 10 cents for 1987, 10.5 cents for 1988, 11 cents for 1989, 1990 and 1991 and 11.5 cents per mile for 1992.⁴ These depreciation rates do not apply to years in which the "actual cost" method was used.⁵

The deduction under the standard mileage allowance for business miles is in lieu of a deduction for operating and fixed costs of the motor vehicle allocable to business use. Such items as depreciation, maintenance and repairs, tires, fuel (including taxes), oil, insurance and registration fees are included in operating and fixed costs.⁶ However, even though the standard mileage rate deduction is claimed, a separate deduction may be taken for parking fees and tolls, interest related to the purchase of the vehicle (to the extent the vehicle is a business asset) and state and local taxes (other than on motor fuel).⁷ Interest is nondeductible personal interest if paid or accrued on indebtedness allocable

to the trade or business of performing services as an employee.⁸ State and local taxes paid or accrued by a taxpayer in connection with an acquisition or disposition of property is treated as part of the cost of the acquired property or as a reduction in the amount realized on the disposition of such property.⁹

The business standard mileage rate may not be used to compute the deductible expenses of — (1) vehicles used for hire, such as taxicabs, (2) two or more vehicles used simultaneously (such as in fleet operations) or (3) any vehicle that is leased, rather than owned, by the taxpayer.¹⁰ Also, the business standard mileage rate may not be used if — (1) the vehicle has previously been depreciated using a method other than straight line depreciation over its estimated useful life, (2) additional first year or expense method depreciation has been claimed or (3) the taxpayer has used ACRS depreciation.¹¹

Employee reimbursement

Payments to employees equal to or less than the standard mileage rate need not be reported into income.¹² Payments in excess of the standard mileage allowance are reportable as income and are subject to withholding and employment taxes.¹³ If employees substantiate a greater amount than the standard mileage allowance, an itemized deduction may be claimed subject to the two percent floor for the excess with the deemed substantiated portion of the payment reported on Form 2106 and the amount (if any) in excess of the deemed substantiated rate included in gross income.

Although not mentioned in *Rev. Proc. 89-66*,¹⁴ the temporary regulations and *Rev. Proc. 92-17*¹⁵ specify that employees related to the employer (within the meaning of I.R.C. § 267(b)) are not relieved from the substantiation requirements merely because of an accounting to the employer.¹⁶

FAVR Method

IRS has approved another method for substantiating motor vehicle expenses.¹⁷ To use the method, the employer must provide a mileage allowance under a reimbursement or other expense allowance arrangement to pay for such expenses and the projected business mileage may not be less than 6,250 miles for the year.

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An employer's mileage allowance may be paid at a flat rate or stated schedule combining fixed and variable rate (FAVR) payments, both of which must be paid quarterly. Periodic fixed payments cover projected fixed costs of driving a standard automobile in connection with the employee's performance of services in a base locality. Periodic variable payments cover projected operating costs under the same assumptions.

A fixed and variable rate allowance may not be paid if the employee has claimed other than straight line

depreciation on the motor vehicle or claimed expense method depreciation.

Safe harbor

It is important to remember that a vehicle used during most of a normal business day directly in connection with the business of farming may be treated as 75 percent used in the business plus whatever percentage, if any, is included in an employee's gross income.¹⁸

FOOTNOTES

- ¹ Rev. Proc. 91-67, 1991-2 C.B. 887. See generally 4 Harl, **Agricultural Law** § 28.02[4][a] (1992).
- ² Rev. Proc. 91-67, 1991-2 C.B. 887.
- ³ *Id.*
- ⁴ *Id.* See Rev. Proc. 90-59, 1990-2 C.B. 644; Rev. Proc. 89-62, 1989-2 C.B. 782.
- ⁵ Rev. Proc. 83-74, 1983-2 C.B. 593; Rev. Proc. 85-49, 1985-2 C.B. 716.
- ⁶ Rev. Proc. 91-67, 1991-2 C.B. 887.
- ⁷ *Id.*
- ⁸ I.R.C. § 163(h)(2)(A).
- ⁹ I.R.C. § 164.
- ¹⁰ Rev. Proc. 91-67, 1991-2 C.B. 887.

- ¹¹ *Id.*
- ¹² Rev. Proc. 92-17, I.R.B. 1992-8, 16; Rev. Proc. 89-66, 1989-2 C.B. 792.
- ¹³ See Rev. Proc. 92-17, I.R.B. 1992-8, 16.
- ¹⁴ 1989-2 C.B. 792.
- ¹⁵ I.R.B. 1992-8, 16.
- ¹⁶ Temp. Treas. Reg. § 1.274-5T(f)(5)(ii) (including individuals owning more than 10 percent of stock of corporation).
- ¹⁷ Rev. Proc. 90-34, 1990-1 C.B. 552; Rev. Proc. 91-67, 1991-2 C.B. 887. See Ltr. Rul. 9117052, Jan. 30, 1991 (plan set up as FAVR but requirements not met).
- ¹⁸ Temp. Treas. Reg. § 1.274-6T(b).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

BANKRUPTCY

GENERAL

ADMINISTRATIVE EXPENSES. During the debtor's long bankruptcy case, the debtor's former wife, before divorcing the debtor, assisted the estate in post-petition financing and operating the farm business. The former spouse filed administrative claims for wages and rent of machinery to the estate but the claims were denied because the claims were not presented prior to the estate's filing of the plan. The former spouse's claims for the costs of other labor were denied because of insufficient records of the labor provided. Other claims for machinery rent were denied because the former spouse failed to demonstrate how the machinery use benefited the estate or other creditors or that the former spouse even owned the machinery leased. *In re Bellman Farms, Inc.*, 140 B.R. 986 (Bankr. D. S.D. 1991).

DISCHARGE. The debtor entered into a joint venture with a creditor to operate a cattle breeding ranch. The creditor provided the equipment, working capital and real property. The debtor was to provide personal services in operating the ranch and the parties were to split all profits and losses. After the creditor terminated the joint venture, several pieces of equipment were found to be missing, the proceeds of the sale of two steers were missing from the business account, and the proceeds of the sale of a prize steer were not deposited in the business account. The court held

that the joint venture placed the debtor in a fiduciary capacity and that the failure of the debtor to account for all joint venture property was defalcation; thus, the value of the missing equipment and one-half (the creditor's share) of the missing proceeds from the cattle sales were nondischargeable debts. *In re Shane*, 140 B.R. 964 (Bankr. N.D. Ohio 1992).

ESTATE PROPERTY. The debtors purchased a farm with another couple with each couple owning an equal portion as tenants in common. A portion of the purchase price was secured by a mortgage. The other couple later prepaid their portion of the mortgage balance and the parties entered into an agreement which provided that if the debtors defaulted on their remaining portion of the mortgage, the other couple could make the payments, with a corresponding increase in their ownership share of the farm. If the entire balance of the mortgage was paid by the other couple, the debtors would be required to assign their entire beneficial ownership interest in the farm to the other couple. After this agreement was entered into, the debtors assigned their beneficial interest in the farm to a bank as security for loans. The bank was also a trustee holding the debtor's interest in the farm under a land trust. The farm was leased to a corporation owned by the son of the other couple with the rent to be divided according to the parties' beneficial interests in the farm. After the debtors defaulted on their portion of the real estate taxes and mortgage, the debtors transferred their beneficial interest in the farm to the other