

Deducting Automobile expenses

By Peter Mar EA, LTC
Northwest Tax Associates

Did you know that certain expenses for driving could be tax deductible? Business trips, employee trips for an employer, charitable organization mileage, trips for medical care, and even round trip moving may count as a deduction. Those who use their personal vehicle in this manner could be entitled to a deduction on their respective income tax return.

Tracking mileage

A written record of both business and total mileage must be kept by the taxpayer to substantiate business use. A mileage log showing date, purpose of trip, and miles driven will usually be adequate for recordkeeping. Mileage logs can be purchased at an office supply store or recorded using any number of available Apps on your smart phone. A daily event planner or other written record containing the above information may also be sufficient.

Actual expenses vs. the standard mileage rate

There are two methods for deducting automobile expenses. The actual expense method allows a deduction for the business portion of actual expenses. Fuel, oil, repairs, insurance, tires, and depreciation are typical expenses. The sum total of actual expenses must be prorated against the business percentage of mileage driven. For example, business miles divided by total mileage for the year will yield the business use percentage. That percentage must be multiplied against the sum total of automobile expenses to arrive at the actual expense deduction.

The optional method is the standard mileage rate, which is taken in lieu of actual expenses. This method uses the business and total mileage log. However, the applicable standard mileage rate is multiplied against business miles driven to arrive at the standard mileage rate deduction. No tracking of automobile expenses is required.

Taxpayers may also be entitled to deduct the business portion of interest paid on an automobile loan as well as parking tolls and fees. However, penalties for violation of law, such as citations for traffic or parking infractions, are not deductible.

What are the pros and cons of each method?

Both methods have an acceptable tax purpose. The standard mileage rate method can prove superior when many miles are driven. This method can also be used as long as the taxpayer owns the vehicle. The taxpayer also has the option to convert to the actual expense method in future years.

One advantage to the actual expense method can be when the business portion of automobile expense is high and the vehicle is not driven very much. However, this election is irrevocable, meaning the taxpayer cannot later convert to the standard mileage rate method for that specific vehicle. Also, depreciation will eventually be used up under the actual expense method, causing a lower deduction in future years.

Many taxpayers prefer to use the standard mileage rate because expense tracking is not required. Conversely, some taxpayers use their vehicle 100% for business and have difficulty keeping a mileage log. In some cases, taxpayers may be required to use the actual expense method if they use their vehicle for hire or maintain multiple vehicles, such as in fleet operations.

Standard mileage rates*

*Current and prior-year IRS standard mileage rates can be found under "Resources"- "Tax Center"- "Tax Rates" menu link on our website.

NOTE: The standard mileage rate is adjusted by the US government and can be changed more than once during the same tax year! Rates adjust annually based upon the inflation index. However, the charitable mileage rate is set by congress and is not adjusted for inflation.

Where do auto expenses get deducted?

Most business owners will deduct automobile expenses on their business-related form. For Sole Proprietors, Schedule C and/or Form 4562 will apply. Corporate employees and owners will generally use Form 2106 for unreimbursed business mileage, but may also have other options.

Mileage driven for charitable organizations, medical treatment, or moves due to change in employment may be deductible. Those amounts are deducted on Schedule A or Form 3903.

Which method is right for me?

We like to review each tax situation individually to determine the best overall method to deduct auto expenses. The auto expense deduction can be huge for obvious reasons. Therefore, make sure to ask us about it if you are unsure whether you qualify to take an auto expense deduction on your income tax return.

Last, but certainly not least, KEEP YOUR MILEAGE LOG! You need to track mileage regardless of which method you choose. A mileage log will also help support your auto deduction in the event of an IRS examination ("audit") of your income tax return.