Internal Audit Report

DEPARTMENT OF COUNTY ADMINISTRATION
FOLLOW-UP
TAKE-HOME VEHICLE USE AUDIT
JULY 2013

Office of the County Auditor

OFFICE OF THE COUNTY AUDITOR

Craig Glendenning, CPA
County Auditor

July 2013

The County Council and County Executive
of Howard County, Maryland

Pursuant to Section 212 of the Howard County Charter and Council Resolution 22-1985, we have conducted a follow-up review of selected activities of the

DEPARTMENT OF COUNTY ADMINISTRATION
TAKE-HOME VEHICLE USE

and our report is submitted herewith. The scope of our examination related specifically to a follow-up review of policies and procedures relating to the use of county vehicles by employees assigned take-home vehicles. The body of our report presents our findings and recommendations.

The contents of this report have been reviewed with the Chief Administrative Officer and we have included the Administration's responses. We wish to express our gratitude to the Department of County Administration for the cooperation and assistance extended to us during the course of this engagement.

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SUMMARY

In 2008, we performed a review of the policies and procedures relating to the use of county vehicles by employees assigned take-home vehicles. Our report was issued in September 2008 and contained nine recommendations: (1) that policies and procedures related to vehicle use be updated, (2) that vehicle utilization logs be completed and submitted monthly, (3) that no exemption to the reporting requirements be granted, (4) that the vehicle use policy be revised to include written justification before take-home vehicles are assigned, (5) that the assignment of take-home vehicles be limited to employees who live within the County, (6) that the value of non-business use be added to employees' paychecks monthly, (7) that procedures be developed to document assignment of take-home vehicles, (8) that monthly logs be completed by all employees assigned a take-home vehicle, and (9) that the valuation method used to calculate the fringe benefit be documented.

We requested information from the Department of County Administration on the status of audit recommendations included in our report. We found that although five of the recommendations had been satisfactorily implemented by the department, four of recommendations have not been fully implemented. During our review, we also noted the following four additional areas of concern:

(1) We found that taxable fringe benefits were calculated incorrectly for several employees. The calculations should be reviewed before taxable fringe benefits are included in affected employees' paychecks.

(2) We found that the taxable fringe benefit for one employee who left the County during 2012 was not reported on his paycheck, nor were applicable taxes withheld or remitted to the IRS. Appropriate action should be taken to report the taxable fringe benefit for the employee who left the County during 2012, including remittance of applicable taxes.

(3) We found that 33 additional employees who have take-home vehicles do not report taxable fringe benefits for the use of those vehicles. The Administration should review the IRS regulations regarding the definition of qualified nonpersonal use vehicles, and document why those employees assigned take-home vehicles who are not taxed for personal use are exempt from taxation.

(4) We found that 11 supervisors take home vehicles during the winter months. The Administration should review the necessity of providing seasonal take-home vehicles to employees.

INTRODUCTION AND SCOPE

Our audit focused on the take-home use of County owned vehicles by employees. We did not review the use of take-home vehicles by public safety employees with one exception. We did review take-home vehicles assigned to employees at the Department of Fire and Rescue Services who are currently including their personal use as a fringe benefit. We included a review of record keeping and reporting requirements by employees assigned take-home vehicles. We also reviewed applicable IRS regulations requiring the inclusion of the benefit in taxable income of the employees assigned vehicles.

The objective of our audit was to review the County's take-home vehicle practices to determine whether take-home vehicle assignments were consistent with relevant County policies and procedures and to ensure that vehicles are only allocated to and utilized by authorized staff for defined purposes. We performed tests to determine if records were consistent with policies and procedures. We reviewed the list of those employees who were assigned take-home vehicles along with the associated calculation of taxable benefit. In addition, management of take-home vehicle assignments and ongoing monitoring and reporting practices were reviewed. We also reviewed the County's compliance with federal tax requirements applicable to reporting taxable fringe benefits.

BACKGROUND

The Office of Central Services provides and maintains a fleet of vehicles to meet the needs of the County. Take-home vehicles are provided to a number of employees. Any non-business use, including commuting, is a taxable fringe benefit and subject to the substantiation requirements of the Internal Revenue Service. Qualified nonpersonal use vehicles are exempt from the substantiation requirements. The term qualified nonpersonal use vehicle is any vehicle which, by reason of its nature, is not likely to be used more than a de minimis amount for personal purposes. Vehicles which are qualified nonpersonal use vehicles include clearly marked police and fire vehicles, vehicles designed to carry cargo with a loaded gross vehicle weight over 14,000 pounds, delivery trucks with seating only for the driver, specialized utility repair trucks, school buses, tractors, and unmarked vehicles used by law enforcement officers.

CURRENT STATUS OF PRIOR RECOMMENDATIONS

Policies and Procedures

(1) Initial Findings

At the time of our initial review, Howard County Policy and Procedure 200.2 Vehicle Use was the County policy which governed the use of all vehicles including take-home vehicles. This policy had last been revised in 2002. We found that this policy was out of date and incomplete in regards to the assignment and reporting requirements for take-home vehicles.

Initial Recommendations and Administration's Responses

We recommended that Howard County Policy and Procedure 200.2 Vehicle Use be updated to reflect changes made since 2002. The Administration concurred with our 2008 recommendation.

Follow-up Findings

The Howard County Central Fleet Manual was issued in September 2008 to reflect changes made since the 2002 policy. However, the Administration stated that additional revisions are in order and will be forthcoming, and as part of these revisions, the Take-Home Vehicle Use Policy would be removed from the manual and would be a stand-alone policy.

We found that Howard County Policy and Procedure 200.2 Vehicle Use is still in place on the County's intranet, and there is no indication that it has been superseded.

Follow-up Recommendations

1. ***We recommend that the Administration update Howard County Policy and Procedure for Vehicle Use to reflect current procedures or policies on the County's intranet. We also recommend that the Administration follow through on its commitment to revise the Take-Home Vehicle Use Policy, including updating the policy to reflect current procedures.***

Administration's Response

The Administration concurs with this recommendation. Howard County Policy and Procedure Vehicle Use (200.2) and Disposition of Surplus Property (300.3) have been replaced by the Howard County Central Fleet Manual. Both of these polices have been deleted from the Howard County Policy and Procedure Manual on the Intranet. The Howard County Central Fleet Manual will be revoked and replaced by three polices:

1. Vehicle Use (Ninety percent completed)
2. Vehicle Equipment and Maintenance (Ninety-five percent completed)
3. Take-Home Vehicle Use (Forty percent completed)

The Administration anticipates completion of the three policies within the next six months. The Vehicle Utilization Log will be included in the Vehicle Use Policy and the Take-Home Vehicle Use Policy. The Vehicle Utilization Log will be made available as an electronic version and a printable version. Both polices will include instructions for completing and filing the log on a monthly basis.

Reporting Requirements

(2) Initial Findings

At the time of our review, the vehicle use policy required the use of a Uniform Vehicle Utilization Log. This form was required to be completed on a monthly basis. We found that the form was not being completed monthly as required by the policy.

Initial Recommendations and Administration's Responses

We recommended that the Uniform Vehicle Utilization Log be completed and submitted monthly as required by Howard County Policy and Procedure 200.2. Only those employees assigned qualified nonpersonal use vehicles should be exempt from completing the log. The Administration concurred with our recommendation and reported that the 2008 revised Howard County Central Fleet Manual requires that the Vehicle Utilization Log be maintained on a monthly basis.

Follow-up Findings

According to the Central Fleet Manual, a copy of the Vehicle Utilization Log should be forwarded to Central Fleet for all employees that have an on-call or assigned take-home vehicle

no later than the 10th day of the month following the reporting period.

We found that the Vehicle Utilization Mileage Log is completed on a monthly basis. It is forwarded to the Payroll Division where it is filed and used to compute the employee fringe benefit to be added to the employee paychecks annually. Only vehicle utilization logs for employees assigned qualified nonpersonal use vehicles are prepared and submitted to Payroll. The manual requires that the logs be forwarded to Central Fleet. The Administration reports that the logs are currently forwarded to the Payroll Division. We agree that this is appropriate. The Administration has indicated that the new policies and procedures will reflect current practice.

Exemptions from the Reporting Requirements

(3) Initial Findings

At the time of our initial review, the policy included a section covering employees who were exempted by the Chief Administrative Officer from the record keeping requirements of the policy. We found that no employees were completing the reporting requirements.

Initial Recommendations and Administration's Responses

We recommended that no exemption from the reporting requirements be granted to any employee except employees assigned nonpersonal use vehicles. The Administration concurred with this recommendation.

Follow-up Findings

Our previous recommendation has been implemented.

Granting of Take-Home Vehicles

(4) Initial Findings

During our initial review, we found that the policy did not address the issue of vehicle assignment or specify the requirements necessary to be assigned a take-home vehicle.

Initial Recommendations and Administration's Responses

We recommended that the Vehicle Use policy be revised to include specific requirements for granting take-home vehicles to employees who will report taxable income from the fringe benefit. Written justification should be prepared and approved before take-home vehicles are assigned. The Administration agreed and, according to the manual, a Take-Home Vehicle Assignment Authorization Request form must be submitted and approved by the County Administrative Officer for all assignments. It requires that justification and support be attached as required. Once approved or disapproved, this form should be sent to Central Fleet.

Follow-up Findings

We found that the Take-Home Vehicle Assignment Authorization Request form is not currently being used.

Follow-up Recommendations

2. ***We recommend that the Take-Home Vehicle Assignment Authorization Request form be completed for all new assignments and that written justification be prepared and approved before take-home vehicles are assigned.***

Administration's Response

> The Administration concurs with this recommendation**.** The Take-Home Vehicle Assignment Authorization Requests are being reviewed and updated. Copies of the Take-Home Vehicle Assignment Authorization Requests will be maintained by the Office of Central Fleet. The requirement to complete the Take-Home Vehicle Assignment Authorization Request to include written justification will be included as part of the Take-Home Vehicle Use Policy.

Out-of-County Take-Home Vehicles

(5) Initial Findings

During our initial review, we found that many employees assigned take-home vehicles resided outside the County. This results in increased expense to the County for fuel and maintenance of the vehicles.

Initial Recommendations and Administration's Responses

We recommended that the Vehicle Use policy be revised to limit assignment of take-home vehicles to employees who live within the County. The Administration stated that an exception exists to allow on call take-home vehicles to be taken out of the County in certain cases. Employees who live outside the County may be assigned a take-home vehicle if the County Administrative Officer determines that it is in the best interest of the County.

Follow-up Findings

A significant number of employees assigned take-home vehicles reside outside the County. Of the 36 employees with take-home vehicles who report a taxable fringe benefit, 21 do not live in the County. Of 33 additional employees with take-home vehicles who do not report a taxable fringe benefit, 24 live outside the County. There is no documentation to support the need for these out-of-county employees to be assigned take-home vehicles.

Follow-up Recommendations

3. ***We continue to recommend that the assignment of take-home vehicles be restricted to employees who live within the County. We understand that exceptions may be made in unusual circumstances. We recommend that written explanation and documentation be included on the Take-Home Vehicle Assignment Authorization Request for all instances in which a take-home vehicle will be issued to an employee who resides outside the County.***

Administration's Response

> The Administration will take this recommendation under advisement. In some circumstances, the cost benefit may not be the overriding factor in determining whether a vehicle is assigned. When it is determined by the CAO that it is in the best interest of the County, an employee who lives outside of Howard County may be assigned a take-home vehicle as provided in the Howard County Central Fleet Vehicle Manual.

Recording of Taxable Benefit

(6) Initial Findings

During our initial review, we found that the value of the non-business use of a County vehicle was included in the employees' income as a taxable fringe benefit in the first pay check

in December for the period from November 1st of the previous year to October 31st. We found several instances in which mistakes were made which had to be corrected.

Initial Recommendations and Administration's Responses

We recommended that the value of non-business use be calculated monthly and added to the second paycheck of the following month. This would ensure timelier reporting of personal use. In addition, the possibility of mistakes would be reduced. The Administration agreed and included this requirement in the manual.

Follow-up Findings

The manual states that estimated personal use will be charged through payroll each pay period and adjusted each month following the receipt of the monthly Vehicle Utilization Mileage Log.

However, the value of non-business use is calculated annually. The fringe benefit is usually reported on the first payroll in December for the previous twelve months. This is acceptable according to the Internal Revenue Service Pub. 15-B. The Administration reported that the record keeping section of the manual will be revised to reflect that the fringe benefit allocated to each employee with a take-home vehicle is reported annually through payroll. The Administration has indicated that the new policies and procedures will reflect current practice.

Oversight of Take-Home Vehicle Use

(7) Initial Findings

During our initial review, we noted that the list of take-home vehicles assigned to employees included employees who no longer work for the County, and omitted some employees who did have an assigned take-home vehicle.

Initial Recommendations and Administration's Responses

We recommended that procedures be developed to ensure that the assignment of take-home vehicles is closely documented and updated as changes occur. The Administration

concurred with this recommendation and stated that it is reflected in the record keeping section of the manual.

Follow-up Findings

According to the manual, "On a monthly basis, each department shall submit an updated list of all take home vehicles to the Central Fleet Administrator. The list shall include the vehicle FAICS# and name of employee assigned to the vehicle. On a semi-annual basis, Central Fleet shall re-evaluate the information for assigned vehicles and provide a recommendation to the CAO for adjustments to the program." This procedure is not being followed. Changes made in employees and vehicles assigned are not being communicated to Central Fleet and the Payroll Division as they occur, and therefore they were unaware of the full extent of the take-home vehicle program, including the number of vehicles and the employees assigned to them.

Follow-up Recommendations

4. ***We recommend that the policy requiring tracking of take-home vehicles be revised to ensure that the Central Fleet Administrator, the Payroll Chief, and the County Administrative Officer are aware of all take-home vehicles and the employees assigned to those vehicles. On a semi-annual basis, the Central Fleet Administrator should re-evaluate the information and provide recommendations for changes to the program to the County Administrative Officer.***

Administration's Response

> The Administration concurs with this recommendation. The Central Fleet Administrator will re-evaluate on a <u>semi-annual</u> basis the tracking of take-home vehicles. The Take-Home Vehicle Use Policy and Procedure will reflect this change.

Record Keeping

(8) Initial Findings

Treasury Regulations require substantiation of the business use of county owned vehicles. Employees must keep logs of their usage of take-home vehicles and submit the logs monthly, reporting daily working mileage and mileage driven between work and residence. During our initial review, we found that monthly logs were not being submitted.

Initial Recommendations and Administration's Responses

We recommended that monthly logs be completed by all employees assigned a take-home vehicle. The only exception to this requirement would be for employees assigned qualified nonpersonal use vehicles. The Administration concurred with this recommendation.

Follow-up Findings

As reflected in the record keeping section of the manual, drivers of assigned take-home vehicles must maintain adequate records to support mileage activity. These employees must submit their mileage activity on a monthly basis to Central Fleet by the 10th of the following month.

This is currently the process followed by employees with one exception. They submit the mileage activity to the Payroll Division because it is responsible for reporting this fringe benefit for tax purposes. The Administration has indicated that the new policies and procedures will reflect current practice.

Documentation

(9) Initial Findings

During our initial review, we found that the County calculated employees' fringe benefit for personal use of take-home vehicles using three different methods, the lease value rule, the cents-per-mile rule, and the commuting rule. Calculations for some employees were determined using more than one rule. No documentation existed as to how the appropriate valuation method was determined.

Initial Recommendations and Administration's Responses

We recommended that documentation be prepared to substantiate the valuation method used to determine the calculation of taxable fringe benefits for the use of each take-home vehicle subject to taxation as a fringe benefit. The Administration concurred with this recommendation.

Follow-up Findings

The Administration implemented our recommendation adding a statement to the manual

under the heading tax consequences. The statement reads as follows, “Any vehicle that has been assigned that does not meet the requirements of a qualified nonpersonal use vehicle will be considered a taxable fringe benefit. The Payroll Department will determine the value of the personal use by using the rules established by the Internal Revenue Service to decide which one of the three valuation methods (Commuter Valuation, Cents per Mile or Annual Lease Value) to use.”

We found that the Payroll Division determined the proper valuation method, and properly (with some exceptions) included the appropriate amount on the employees’ paychecks annually. The exceptions are discussed more fully below.

ADDITIONAL FINDINGS AND RECOMMENDATIONS

(1) We determined that there were 36 employees with take-home vehicles who reported taxable fringe benefits in 2012. Of the total, taxable fringe benefits were reported under the lease value rule for 11 employees. The remaining 25 employees reporting their taxable fringe benefit using the commuting rule. Total taxable fringe benefits amounted to $44,171 for 2012. We reviewed the monthly utilization logs and the calculations of taxable fringe benefits for all 36 employees. We also traced the taxable fringe benefits to the employees' paychecks.

We found that employees were properly reporting their mileage monthly as required. However, we found minor discrepancies in the calculation of taxable fringe benefit for three employees who were required to report their take-home vehicle use using the lease value rule. Two of the employees were overcharged, one by $33.24 and one by $187.85. One employee was undercharged by $6.66.

> ***We recommend that an employee in the Department of Finance review the calculations before taxable fringe benefits are included in affected employees' paychecks.***

Administration's Response

> The Administration concurs with this recommendation. Finance/Payroll is currently establishing new procedures requiring a second review of all input calculations to the fringe value worksheets and sign off verification of batch totals loaded into the payroll process by a second staff member.

(2) According to Internal Revenue Service Publication 15-B, "if your employee leaves your employment and you have unpaid and uncollected taxes for noncash benefits, you are still liable for those taxes. You must add the uncollected employee share of social security and Medicare tax to the employee's wages." Two employees with take-home vehicles left the County during 2012. One of the employee's final paycheck did not include his taxable fringe benefit, which amounted to $477.

> ***We recommend that in accordance with IRS regulations, the taxable fringe benefit of $477 be included in the affected employee's W-2. If the County choses to pay the employee's social security and Medicare taxes on the taxable fringe benefits without deducting them from his pay, it must also include the amount of the payments in the employee's income. Required taxes must also be remitted to the IRS.***

We also recommend that when employees with take-home vehicles leave County employment, the Payroll Division be informed so that their final paychecks can be adjusted accordingly. This change should be communicated to the Payroll Division in written form.

Administration's Response

The Administration concurs with this recommendation and will consult with the County's outside tax attorney to determine the appropriate action.

Fleet will work closely with Human Resources and Payroll to make sure that the Payroll Division is notified whenever an employee leaves employment.

(3) During our review, we found that an additional 33 employees in the Department of Public Works and the Department of County Administration have take-home vehicles, and the employees do not report a taxable benefit for their use of the vehicles. The Central Fleet Vehicle Manual requires that requests to authorize take-home vehicles meet at least one of the following criteria, on-call, special equipment, assigned vehicle, or economic benefit. However, in order to be exempt from the reporting requirements, and to be exempt from taxation on their personal use, the vehicles must meet stringent requirements under IRS regulations under § 1.274-5. Qualified nonpersonal use vehicles such as trucks and vans must be specially modified with the result that it is not likely to be used more than a de minimis amount for personal purposes.

We recommend that the Administration review the IRS regulations regarding the definition of qualified nonpersonal use vehicles, and document why those employees assigned take-home vehicles who are not taxed for personal use are exempt from taxation. If any employees are found to be required to report a taxable fringe benefit, appropriate action should be taken to report the benefit.

Administration's Response

The Administration concurs with this recommendation and is taking corrective action. All vehicles that are used for commuting are being photographed and evaluated to determine if there is a reportable taxable fringe benefit. Once determined, the driver and the department will be notified and the benefit will be reported to the Payroll Division. Employees will be required to complete the Take-Home Vehicle Utilization Request and provide written justification.

(4) During our review, we noted that 11 supervisors in the Department of Public Works are assigned take-home vehicles during the winter months, from December 1st through April 15th.

Ten of these 11 employees do not report a taxable fringe benefit. Six of the employees live outside the County. These employees take their vehicles home regardless of the weather.

> ***We recommend that the Administration review the necessity of providing seasonal take-home vehicles to employees. If it is necessary for these employees to have take-home vehicles during storms, they should only take their vehicles home when inclement weather is predicted, not every day as is the current policy. We also recommend that if the Administration determines that it is necessary to provide the seasonal take-home vehicles, a determination of taxable benefit should also be made.***

Administration's Response

> The Administration will review with Central Fleet and the departments the necessity for employees to take-home vehicles during inclement weather. If the Administration decides to continue the program, it will be determined who is required to report taxable benefits based on Internal Service Revenue Publications.

We would like to thank the Administration for their assistance in our follow-up procedures, and the implementation of our audit recommendations. We will be conducting future audits to determine the status of our recommendations.