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Tax, Benefits, and Private Client

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Treasury Department Issues Guidance on Tax Treatment of Qualified Transportation Fringe Benefits

The Treasury Department recently published guidance on determining the amount of qualified transportation fringe benefit expenses that are nondeductible and, for tax-exempt organizations, the amount that should be treated as an increase in unrelated business taxable income ("UBTI"). Both for-profit businesses and tax-exempt organizations should be aware of this interim guidance and its method for calculating disallowance, as summarized in the client alert that follows.

OVERVIEW

On December 10, 2018, the Treasury Department released Notice 2018-99, which provides interim guidance to taxpayers to determine the amount of parking expenses for qualified transportation fringe benefits ("QTFs") that are now nondeductible under Section 274(a)(4) of the Internal Revenue Code (the "Code"). Under Section 512(a)(7) of the Code, a tax-exempt organization's UBTI is increased by the amount of QTF that would be nondeductible if the exempt organization were taxable. The Tax Cuts and Jobs Act amended Section 274(a)(4) of the Code to disallow a deduction for expenses related to QTFs provided by a taxpayer to its employees and added Section 512(a)(7), which requires a tax-exempt organization to increase its UBTI by the amount of the nondeductible QTF expense, including expenses related to any parking facility used in connection with qualified parking (as explained below) and any on-premises athletic facility as defined in Section 132(j)(4)(B).

Effective January 1, 2018, no deduction is allowable for any employer-provided QTF expense incurred on or after January 1, 2018.[1] The amount disallowed is the employer's cost of providing the QTF, not the QTF's value to the employee. QTFs include transportation in a commuter highway vehicle, transit passes, and "qualified parking," *i.e.,* parking provided to an employee on or near the employee's place of employment. An employee is any individual currently employed by the employer, but does not include partners, two-percent shareholders of a S Corporation, sole proprietors, and independent contractors.

CALCULATING THE DISALLOWANCE

Taxpayer Provides Parking Spots at Third Party Lot/Garage

If an employer pays a third-party lot or garage to provide parking spots for its employees, no deduction is allowed for such amount paid to the third party.[2]

Taxpayer Owns or Leases All or a Portion of a Parking Facility
If an employer owns or leases part or all of a parking facility where its employees park, the amount disallowed may be calculated using any reasonable method until the Treasury Department issues additional guidance.

Example of Reasonable Method for Calculation Disallowance Amount
Under the Notice, the amount of QTF expense that is disallowed under Section 274(a)(4) of the Code when the employer owns or leases all or a portion of a parking facility may be calculated as follows:

1. *Calculate the Disallowance for Reserved Spot Employees*

First, the employer must calculate the number of spots reserved for employees ("Reserved Employee Spots"), *i.e.,* exclusively reserved for employees by an "Employee Parking Only" sign or in a separate facility or portion of a facility accessible only to employees, and determine the percentage of Reserved Employee Spots in relation to the total number of spots.[3] This percentage is then multiplied by the employer's total parking expenses for the parking facility.

$$\frac{\text{Reserved Employee Spots}}{\text{Total Parking Spots}} = \text{\% Reserved Employee Spots}$$

% Reserved Employee Spots x Parking Expense = Disallowance Amount

2. *Determine the Primary Use of Remaining Spots*

Next, the employer must identify the primary use of the non-Reserved Employee Spots during normal business hours on a typical business day. The employer may deduct the expense of providing such non-Reserved Employee Spots if the primary use of the non-Reserved Employee Spots is to provide parking to the general public, including customers, clients, visitors, and delivery vehicles.

3. *Calculate the Allowance for Reserved Nonemployee Spots*

If the primary use of the non-Reserved Employee Spots is other than parking for the general public, the employer may identify the spots reserved for nonemployees ("Reserved Nonemployee Spots"), such as spots for visitors, customers, partners, sole proprietors, and two-percent shareholders of S Corporations. Reserved Nonemployee Spots may be marked "Customer Parking Only" or be in a separate facility or portion of a facility accessible only to nonemployees and determine the percentage of Reserved Nonemployee Spots in relation to the total number of spots.

$$\frac{\text{Reserved Nonemployee Spots}}{\text{Total Parking Spots}} = \text{\% Reserved Nonemployee Spots}$$

% Reserved Nonemployee Spots x Parking Expense = Deduction Amount

The amount an employer spends to provide Reserved Nonemployee Spots may be deductible.

4. *Determine the Remaining Use and Allocable Expenses*

If, after completing these steps, the employer has any uncategorized parking spots, it must determine the extent of employee use of the remaining spots and the related expenses allocable to those spots. An employer may use any reasonable method to make this calculation, such as identifying specific spots actually used by employees or estimating such usage.

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EXEMPT ORGANIZATION

An exempt organization calculates the amount it pays to provide its employees with parking using the same methods as a for-profit employer. However, Section 512(a)(7) requires the organization to increase its UBTI by any amount for which a deduction would be disallowed if the employer was not a tax-exempt organization, even though the provision of parking or a commuter/transportation benefit itself is not considered an unrelated trade or business.[4] If the amount paid to provide employees with parking or a commuter/transportation benefit exceeds $1,000, the organization will be required to file a Form 990-T, Exempt Organization Business Income Tax Return.

1. It is important to note that for taxpayers that have a tax year other than a calendar year, some of the QTF expenses incurred may be deductible. Similarly, a tax-exempt organization that is not on a calendar year may not be required to increase its UBTI by the full amount of the QTF expenses incurred in its 2017-18 tax year.
2. The maximum tax-free QTF permissible for 2018 is $260 per month. If an employer provides a QTF that is more than $260 per month, the excess is taxable to the employee as compensation.
3. Until March 31, 2019, employers may change their parking arrangement, i.e., change signage, access, etc., to decrease or eliminate the number of Reserved Employee Spots so that it may treat those parking spots as non-Reserved Employee Spots. Such changes may be made retroactive to January 1, 2018.
4. *See* Notice 2018-67, 2018-36 I.R.B. 409.

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