

Parking Fringe Benefits and Unrelated Business Income

The IRS has provided guidance and examples for calculating the nondeductible portion of parking expenses. In addition, the IRS has provided guidance to tax-exempt organizations to help such organizations determine how unrelated business taxable income (UBTI) will be increased by the nondeductible amount of such fringe benefit expenses paid or incurred.

The IRS also has also provided transitional estimated tax penalty relief to tax-exempt organizations that offer qualified transportation fringe benefit expenses and were not required to file a Form 990-T, Exempt Organization Business Income Tax Return, last filing season.

Background

The Tax Cuts and Jobs Act added Code Sec. 274(a)(4) to preclude for profit employers from deducting qualified transportation fringe benefits expenses paid or incurred on behalf of employees beginning January 1, 2018. Qualified transportation fringe benefits include; van pools, transit passes, bicycle commuting, and qualified parking.

TCJA also added Code Sec. 512(a)(7), which requires exempt organizations to increase unrelated business taxable income (UBTI) by any amount for which a deduction is not allowable under Code Sec. 274 and which is paid or incurred from January 1, 2018 onward for any qualified transportation fringes and any parking facility used in connection with qualified parking.

Under the old law, provided certain requirements were met, if an employer paid for an employee's parking, the employee would not have to report any income for the benefit, and the for-profit employer would get a deduction for the amount paid.

Under the new law, employers can still exclude from the employee's income the value of "qualified transportation benefits," but employers can no longer take a deduction and nonprofits who provide onsite or off-site parking for employee may create a ubi issue.

Determining if Unrelated Business Income Exists

The IRS has provided two types of calculations to help entities determine if UBI exists. The first is for cases where the employer pays a third party for the use of its parking lot for the employer's employees. The second is for cases where the employer owns or leases the parking lot.

Employer contracts with third party for parking.

When an employer contracts with a third party for the use of the parking lot, the disallowance under Code Sec. 274(a)(4) is generally the amount that the employer pays to the third party. However, if that monthly amount exceeds \$260 an employee, the employer must treat the excess as additional compensation. Thus, the monthly amount in excess of \$260 is excluded from the disallowance amount.

For example, if Employer A pays \$300 per month for each of the employer's ten employees to park, \$31,200 ($(\$260 \times 10) \times 12$) is disallowed under Code Sec. 274(a)(4). The remaining \$4,800 ($(\$40 \times 10) \times 12$) is not subject to the Code Sec. 274(a)(4) and remains deductible.

Employer owns or leases the parking lot.

According to the IRS, until it issues further guidance, *employers may use any reasonable method to calculate the Code Sec. 274(a)(4) disallowance* in cases where the employer owns or leases the parking lot.

Nevertheless, the IRS has provided a four-step reasonable method:

1. Calculate the disallowance for reserved employee spots.
2. Determine the primary use of the remaining spots (for the general public (over 50 percent) or for employees).
3. Calculate the allowance for reserved nonemployee spots.
4. Determine the remaining use and allocable expenses.

For example, an Employer E, owns a surface parking lot adjacent to its plant. E incurs \$10,000 of total parking expenses¹. E's parking lot has 500 spots that are used by its visitors and employees. E has 50 spots reserved for management and has approximately 400 employees parking in the lot in non-reserved spots during normal business hours on a typical business day. Additionally, E has 10 reserved nonemployee spots for visitors.

- **Step 1.** Because E has 50 reserved spots for management, $\$1,000 ((50/500) \times \$10,000)$ is the amount of total parking expenses that is nondeductible for reserved employee spots.
- **Step 2.** The primary use of the remainder of E's parking lot is not to provide parking to the general public because 89% ($400/450 = 89$ percent) of the remaining parking spots in the lot are used by its employees.
- Therefore, expenses allocable to these spots are not excluded from the Code Sec. 274(a)(4)
- **Step 3.** Because 2 percent ($10/450$) of E's remaining parking lot spots are reserved nonemployee spots, the \$200 allocable to those spots ($\$10,000 \times 2$ percent)) is not subject to the Code Sec. 274(a)(4) disallowance. That amount continues to be deductible.
- **Step 4.** E must reasonably determine the employee use of the remaining parking spots during normal business hours on a typical business day and the expenses allocable to employee parking spots.

Four General Rules of Thumb

Generally, what this all boils down to is this:

1. Nonprofits that provide onsite parking to employees on property owned by them will not create ubi, provided a majority of the parking spots on campus are not restricted in any way and are available to the general public.
2. If more than 50% of the parking slots are used for employee parking ...ubi exists.

3. If you have onsite parking spaces specifically restricted for employee parking, no matter how many ... they are subject to ubi.
4. If you pay a third party to provide parking for employees that becomes subject to ubi.

In these cases, the basic premise of the IRS position in their analysis is to determine if most of the parking spaces are utilized for employees or for the "general public." (Spaces at a church that are not used during the week may be considered as available for the "general public" unless they are specifically designated for employee use only). If the majority of the spaces are utilized or available for the general public, then the church does not have unrelated business income.

On the other hand, if more than 50 percent of the parking spaces are used for employee parking, then the church would be subject to the ubi rules, and where required, pay tax on the "qualifying expenses" associated with the parking lot.

Estimated Tax Penalty Relief

If you find that your parking situation has created gross unrelated business income of more than \$1,000, for one reason or another, then your exempt organization may be subject to the unrelated business income tax under Code Sec. 511 at corporate rates and you will need to report the activity on *Form 990-T, Exempt Organization Business Income Tax Return*.

Further, you may find yourself halving to make quarterly estimated tax installment payments under Code Sec. 6655 if your estimated tax is expected to be \$500 or more. (Note: Code Sec. 6655 imposes an addition to tax for failure to make a sufficient and timely estimated income tax payment).

To avoid the underpayment penalty, each installment generally must equal at least 25 percent of the lesser of:

- 100 percent of the tax shown on the current year's tax return or of the actual tax if no return is filed (current-year safe harbor); or
- 100 percent of the tax shown on the corporation's return for the preceding tax year, provided a positive tax liability was shown and the preceding tax year consisted of 12 months (preceding-year safe harbor).

The IRS has recognized that Code Sec. 512(a)(7) may cause some exempt organizations to owe unrelated business income tax and have to pay estimated income tax for the first time. These organizations would have been able to use the preceding-year safe harbor and may need more time to develop knowledge and processes to comply with estimated tax payment requirements.

So, the IRS is waiving the addition to tax for failure to make estimated income tax payments for an exempt organization that:

1. provides qualified transportation fringes to an employee for which estimated income tax payments, affected by changes made by TCJA to Code Sec. 274 and Code Sec. 512, would otherwise be required to be made on or before December 17, 2018;

2. was not required to file a Form 990-T, Exempt Organization Business Income Tax Return, for the tax year preceding the organization's first tax year ending after December 31, 2017; and
3. timely pays the amount reported for the tax year for which relief is granted.

Taxpayers that do not qualify for this relief can avoid an addition to tax for underpayment of estimated income tax if they meet one of the statutory safe harbor or exception provisions under Code Sec. 6654 or Code Sec. 6655. To claim the waiver, the exempt organization must write "Notice 2018-100" on the top of its Form 990-T.

¹ Qualifying expenses that create unrelated business income are expenses associated with the parking lot, including: repairs, maintenance, utility costs, insurance, property taxes, interest, snow and ice removal, leaf removal, trash removal, cleaning, landscaping costs, parking lot attendant expenses, security, and rent or lease payments or a portion of a rent or lease payment (if not broken out separately). Qualifying expenses do not include depreciation or cost recovery.

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