

Guidance on Parking and Unrelated Business Taxable Income

With the passage of the Tax Cuts and Jobs Act (TCJA), significant changes were made regarding the deductibility of employee parking expenses. The TCJA amended Sec. 274(a)(4) to provide that no deduction is allowed for the expense of any qualified transportation fringe (QTF) benefit that taxpayers provide to their employees. Recent IRS guidance on the issue indicates that providing parking to employees may be considered a nondeductible QTF benefit.

The nondeductibility of QTF's applies to both for profit and not for profit entities. The impact to a not for profit entity is seen through an increase in the nonprofits' unrelated business taxable income (UBTI) by the amount of the nondeductible QTF expense and is set forth via IRC section 512(a)(7). In some instances, a not for profit entity may have a Form 990T filing requirement for the first time.

The TCJA does not outline how to determine the QTF expense that is nondeductible and, therefore, treated as an increase to UBTI. To provide interim guidance to tax-exempt organizations, the IRS published Notice 2018-99 in December 2018. This guidance helps determine the corresponding increase in the amount of unrelated business taxable income under IRC Section 512 (a)(7) attributable to the nondeductible parking expenses. The increase in UBTI is applicable for expenses paid or incurred after December 31, 2017.

Qualified parking is defined in IRC Section 132(f)(5)(c) as parking provided to an employee on or near the business premises of the employer or on or near a location from which the employee commutes to work. It should be noted that although the value of the QTF is relevant in determining the exclusion and whether the exception applies, the disallowed deduction relates to the expense of providing a QTF, not to its value. It should also be noted that expenses for parking made available to the public are exempted from disallowance.

The following sets forth several calculations to determine the disallowed deduction. The most important aspects stated in the recently released Notice for determining the nondeductible amount depend on two key factors - (1) Whether the nonprofit employer pays a third party to provide reserved parking for its employees or (2) If the nonprofit employer owns or leases a parking facility, or a portion of a facility, where its employees park.

1. The Nonprofit Employer Pays a Third Party to Provide Employee Parking

Under this scenario, if the employer pays a third party an amount so that its employees may park at the third party's garage, the disallowance is generally calculated simply as the employer's total annual cost of the employee parking paid to the third party. An issue occurs if the amount exceeds the monthly limitation on exclusion which is \$260 for 2018. In that case, Section 274 states that the excess must be treated by the employer as compensation and wages to the employee and is exempted from the employer's disallowance amount.

2. The Nonprofit Employer Owns or Leases All or a Portion of a Parking Facility

Under these circumstances, if the employer owns or leases all or a portion of one or more parking facilities (indoor or outdoor garages, lots and other structures) where employees park on or near the premises of their employment or on or near a location from which they commute, the disallowance should be calculated using the four basic steps approved by the IRS as a "reasonable" method for calculations.

For purposes of Notice 2018-99, “total parking expenses” include, but are not limited to; repairs, maintenance, utility costs, insurance, property taxes, interest, snow and ice removal, leaf removal, trash removal, cleaning, landscape costs, parking lot attendant, security, and rent or lease payments or a portion of a rent or lease payment.

The IRS Notice sets forth 4 steps in calculating the disallowed expense as explained below.

Step 1. Calculate the disallowance for reserved employee spots

A taxpayer that owns or leases all or a portion of one or more parking facilities must identify the number of spots in the parking facility, or the taxpayer’s portion thereof, exclusively reserved for the taxpayer’s employees (“reserved employee spots”). Employee spots in the parking facility, or portion thereof, may be exclusively reserved for employees by a variety of methods. These methods include but are not limited to; specific signage (for example, “Employee Parking Only”) or a separate facility or portion of a facility segregated by a barrier to entry or limited by terms of access.

The taxpayer must then determine the percentage of reserved employee spots in relation to total parking spots and multiply that percentage by the taxpayer’s total parking expenses for the parking facility. The product is the amount of the deduction for total parking expenses that is disallowed under § 274(a)(4) for reserved employee spots. Until March 31, 2019, taxpayers that have reserved employee spots as defined in this notice may change their parking arrangements (changing signage, access, etc.) to decrease or eliminate their reserved employee spots. This would then treat those parking spots as not reserved employee spots for purposes of this notice retroactively to January 1, 2018.

Step 2. Determine the primary use of remaining spots (the “primary use test”)

The taxpayer may identify the remaining parking spots in the parking facility and determine whether their primary use is to provide parking to the general public. If the primary use of the remaining parking spots in the parking facility is to provide parking to the general public, then the remaining total parking expenses for the parking facility are excepted from the § 274(a) disallowance by the general public exception under § 274(e)(7). For purposes of § 274(a)(4) and this notice, “primary use” means greater than 50 percent of the actual or estimated usage of the parking spots in the parking facility. Primary use of the parking spots is tested during normal business hours on a typical business day, or in the case of an exempt organization, during the normal hours of the exempt organization’s activities on a typical day. Non-reserved parking spots that are available to the general public but empty during normal business hours on a typical business day, or in the case of an exempt organization, during the normal hours of the exempt organization’s activities on a typical day, are treated as provided to the general public. In addition, if the actual or estimated usage of the parking spots varies significantly between days of the week or times of the year, the taxpayer may use any reasonable method to determine the average actual or estimated usage.

For purposes of § 274(a)(4) and this notice, the “general public” includes, but is not limited to, customers, clients, visitors, individuals delivering goods or services to the taxpayer, patients of a health care facility, students of an educational institution, and congregants of a religious organization. The general public does not include employees, partners or independent contractors of the taxpayer.

Step 3. Calculate the allowance for reserved nonemployee spots

If the primary use of a taxpayer’s remaining parking spots is not to provide parking to the general public, the taxpayer may identify the number of spots in the parking facility, or the taxpayer’s portion thereof,

exclusively reserved for nonemployees (“reserved nonemployee spots”). For example, reserved nonemployee spots include spots reserved for visitors and customers.

If the taxpayer has reserved nonemployee spots, it may determine the percentage of reserved nonemployee spots in relation to the remaining total parking spots and multiply that percentage by the taxpayer’s remaining total parking expenses. The product is the amount of the deduction for remaining total parking expense that is not disallowed under § 274(a)(4).

Step 4. Determine remaining use and allocable expenses

If the taxpayer completes Steps 1-3 in the methodology above and has any remaining parking expenses not specifically categorized as deductible or nondeductible, the taxpayer must reasonably determine the employee use of the remaining parking spots. To do so, they should consider the use during normal business hours on a typical business day (or, in the case of an exempt organization, during the normal hours of the exempt organization’s activities on a typical day) and the related expenses allocable to employee parking spots. Methods to determine employee use of the remaining parking spots may include specifically identifying the number of employee spots based on actual or estimated usage. Actual or estimated usage may be based on the number of spots, the number of employees, the hours of use, or other data.

As you can see, the enactment of the IRC Section 512(a)(7) may have a critical impact on nonprofits. It may be where your entity is experiencing a Form 990T filing requirement and the payment of quarterly estimated tax payments for the first time.

Both the U.S. Treasury and the IRS have sought comments for future guidance as they continue to clarify the treatments of QTF as outlined under the TCJA.

If you feel the disallowance of employee parking expense will impact your entity, we encourage you to contact your WK advisor for assistance. We can provide you with resources to assist with the calculation of the disallowed expenses. Please do not hesitate to email your WK advisor or call (573) 635-6196 or (573) 442-6171.