

# Federal Tax Alert

*Provided by the National Tax Office*

## IRS releases new guidance for tax exempt employers on the “parking tax”

[Special report on Notices 2018-99 and 2018-100](#)

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### IRS ISSUES NOTICES ON THE “PARKING TAX”

The IRS has released preliminary guidance on a provision of the 2017 Tax Cuts and Jobs Act that taxes exempt employers on the expenses incurred in providing qualified transportation fringe benefits to their employees. This provision, which pertains to benefits such as transit passes as well as the provision of parking facilities on or near the business premises of the employer or near a commuting location, is assessed by way of treating the applicable expenses as an addition to the organization’s unrelated business taxable income (UBTI). This result was intended to create parity with for-profit employers, who are precluded from deducting these expenses under the new law. Because the provision was effective for expenses incurred on or after Jan. 1, 2018, exempt organizations had been operating in the dark until the issuance of Notices 2018-99 and 2018-100 on Dec. 10, 2018.

#### **Notice 2018-99**

This notice provides interim guidance on determining the amount of parking expenses to be treated as nondeductible by for-profit employers, and as an addition to unrelated business income for tax-exempt employers. Our discussion of this notice will target the impacts on tax-exempt employers.

The amount of parking expenses required to be treated as UBTI is calculated differently depending on the nature of the parking arrangement:

- Payments to a third party for employees to park at the third-party's facility — payments are UBTI up to a cap of \$260 per employee per month
- Parking facilities owned or leased by employers — any reasonable method may be used to allocate costs to employee use, but a four-step method provided in the notice is deemed to be reasonable

**Payment to a third party:** The first scenario has the expected result, and is the least difficult situation to be addressed under these rules. The notice confirms that these benefits include those that are provided through a salary reduction agreement in addition to those provided in-kind or through a cash reimbursement arrangement. Also, payments that are treated as taxable wages to an employee, i.e., the amount exceeding the \$260 per month threshold for tax-free transportation benefits, won't be treated as UBTI.

**Facilities owned or leased by employers:** The more difficult analysis has been and continues to be under the new guidance, the treatment of parking expenses where the employer owns or leases all or part of a parking facility. The starting point for this analysis is to determine the pool of costs attributable to the organization's parking facilities. While some commentators had proposed that the value of a particular parking arrangement might be used to determine the cost of the parking, the notice confirms that this won't be considered a reasonable method. The notice provides an illustrative list of these expenses which includes items such as repairs, maintenance, utility costs, insurance, property taxes, interest, snow removal, trash removal, parking lot attendant costs, security, and rent or lease payments, but doesn't include depreciation. Guidance is also provided to allow taxpayers to aggregate multiple parking facilities for this purpose.

One significant, unanswered question is how to allocate lease costs to a parking facility when the organization's lease covers both building space and parking spaces, with no breakdown of the lease payment between the two. In many situations, there will be no easy way to determine that breakdown.

Once the pool of parking costs is accumulated, the four-step method is applied.

- **Step 1:** Costs attributable to reserved employee parking spots must be identified and treated as UBTI. For example, if the organization's employees have 10 reserved spots in a parking facility that has 100 total spots, 10 percent of the total costs of the parking facility will be included in UBTI. Reserved spots are those indicated by signage or by requiring a badge to access the spots. There is an opportunity to revise such reserved parking arrangements by March 31, 2019, to decrease or eliminate this issue retroactively to Jan. 1, 2018.
- **Step 2:** Next, the primary use of the remaining parking spots must be determined. For many organizations, this test may allow them to exclude most of their parking costs from UBTI. This step states that if the primary use of the remaining parking spots (i.e. greater than 50 percent) is to provide parking to the general public, the remaining total parking expenses are excluded from UBTI. The term "general public" includes customers, clients, visitors, vendors, patients, students, and religious congregants.
- **Step 3:** If the primary use test of step 2 isn't met, then the cost attributable to any spots reserved for nonemployees is calculated and removed from the pool of costs.

- **Step 4:** If all of the parking costs aren't allocated either to employees or the general public based on steps 1 through 3, then any reasonable method may be used to allocate the remaining costs.

***The following example provides an illustration of the four-step process:***

Taxpayer H, a tax-exempt organization, owns multiple parking lots and garages adjacent to its complex in the city of X. H owns parking lots and garages in other cities too. For the purposes of applying the methodology in this notice, H chooses to aggregate the parking spots in the lots and garages at its complex in city X. However, H may not aggregate the spots in parking lots and garages in other cities with its parking spots in city X. H incurs \$50,000 of total parking expenses related to the parking lots and garages at its complex in city X. H's parking lots and garages at its complex in city X have 1,000 spots in total that are used by its visitors and employees. H has 50 spots reserved for management and has approximately 500 employees parking in the garages and lots in nonreserved spots during normal business hours on a typical business day at H's complex in city X.

- Step 1. Because H has 50 reserved spots for management, \$2,500  $((50/1,000) \times \$50,000 = \$2,500)$  is the amount of total parking expenses that is treated as UBTI for reserved employee spots.
- Step 2. The primary use of the remainder of H's parking facility is not to provide parking to general public because 53 percent  $(500/950 = 53\%)$  of the remaining parking spots in the facility are used by its employees. Thus, expenses allocable to these spots aren't excepted from the inclusion in UBTI under the primary use test.
- Step 3. Because none of H's parking spots are exclusively reserved for nonemployees, there is no amount to be specifically allocated to reserved nonemployee spots.
- Step 4. H 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 at its complex in city X. Because 53 percent  $(500/950 = 53\%)$  of the remaining parking spots in the lot are used by its employees during normal business hours on a typical business day, H reasonably determines that \$25,175  $((\$50,000 - \$2,500) \times 53\% = \$25,175)$  of H's total parking expenses is included in UBTI.

A more typical result for many tax-exempt organizations will be that this analysis will stop at step 2, and the costs allocated to employee parking will be relatively small. Example 10 from the notice describes this result:

"Tax-Exempt Organization K is a hospital and owns a surface parking lot adjacent to its building. K incurs \$10,000 of total parking expenses. K's parking lot has 500 spots that are used by its patients, visitors, and employees. K has 50 spots reserved for management and has approximately 100 employees parking in the lot in non-reserved spots during the normal operating hours of the hospital.

- Step 1. Because K has 50 reserved spots for employees, \$1,000  $((50/500) \times \$10,000 = \$1,000)$  is the amount of total parking expenses that is nondeductible for reserved employee spots under § 274(a)(4). Thus, under § 512(a)(7), K must increase its UBTI by \$1,000, the amount of the deduction disallowed under § 274(a)(4). Step 2. The primary use of the remainder of K's parking lot is to provide parking to the general public because 78%  $(350/450 = 78\%)$  of the remaining spots in the lot are open to the public. Thus, expenses allocable to these spots are excepted from the § 274(a) disallowance by § 274(e)(7) under the primary use test, and only

\$1,000 is subject to the § 274(a)(4) disallowance. Therefore, only \$1,000 of the expenses for the provision of the QTF will result in an increase in UBTI under § 512(a)(7).

- K will need to add the \$1,000 increase of UBTI under § 512(a)(7) to its gross income from unrelated trades or businesses. K is required to file a Form 990-T because the \$1,000 increase to UBTI under § 512(a)(7) meets the filing threshold.”

Use of net operating losses (NOL): The notice provides that a current-year loss from unrelated business activities may be used to offset the deemed UBTI from parking benefits, as long as there is only one unrelated business activity creating the current-year loss. Otherwise, the guidance provided under Notice 2018-67, issued in August of 2018, will cause the losses to be “siloeed” and will eliminate the ability to offset the parking income with NOLs. However, NOLs created prior to tax years ending after Dec. 31, 2017, should be available to offset this income.

#### Notice 2018-100

Because this guidance was issued almost a year after the passage of these provisions, the IRS has provided penalty relief for exempt organizations that haven’t had a Form 990-T filing requirement prior to the imposition of tax on these qualified transportation fringe benefits. The relief applies to estimated tax payments that would’ve been due on or before Dec. 17, 2018, as long as the exempt organization timely files the Form 990-T for the first tax year ending after Dec. 31, 2017, and pays the amount reported for that tax year in a timely manner. The timing of this provision seems problematic for organizations with year ends earlier in 2018, such as June 30, 2018, year ends — some organizations may not have filed 990-Ts in the absence of guidance and so seem to be ineligible for penalty relief. Hopefully, the IRS will further clarify this matter.

We’ll continue to update you as more information on these rules becomes available. Please contact your Plante Moran team member if you have additional questions.

## If you have any questions, please contact:

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