Tax Exempt & Government Entities

Tax Cuts and Jobs Act
EO Provision

Increased Unrelated Business Taxable Income for Nondeductible Fringes

IRC Section 512(a) - Provision 13703

Training based on TCJA guidance issued through September 30, 2018

New Law – TCJA Section 13703

- New IRC 512(a)(7)
- Unrelated business taxable income (UBTI) is increased by amounts paid or incurred for qualified transportation fringe benefits that are not deductible under IRC 274

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Section 13703 of the Tax Cuts and Jobs Act amends IRC 512(a) by adding new paragraph (7).

Under this paragraph, an organization's unrelated business taxable income is increased by amounts paid or incurred for any qualified transportation fringe, any parking facility used in connection with qualified parking that are not deductible under IRC 274. IRC 274 was modified by the TCJA to disallow most parking and transportation fringe benefit deductions.

IRS Nonqualified Fringe Benefits

- Fringe benefits not deductible under IRC 274
  - Qualified transportation fringe (defined in IRC 132(f))
  - Parking facility used in connection with qualified parking (defined in IRC 132(f)(5)(C))

3 IRC 512(a)(7) - Increased UBTI

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Under 512(a)(7), UBTI is increased only by amounts paid or incurred by an organization for any qualified transportation fringe as defined in IRC Section 132(f) or any parking facility used in connection with qualified parking as defined in IRC Section 132(f)(5)(C).

Qualified transportation benefits include:

- A ride in a commuter highway vehicle between the employee's home and work place.
- A transit pass.
- Qualified parking.

Qualified parking is parking provided to employees on or near the business work premises, or parking on or near a location from which employees commute to work by commuter highway vehicle mass transit, or van pool.

IRC Section 274 provides that no deduction is allowed for qualified transportation fringe benefits, as defined in IRC Section 132(f) (whether provided directly by the organization, or through a bona fide reimbursement arrangement, or through a compensation reduction agreement) incurred or paid after December 31, 2017. For example, under section 274, a for-profit business corporation would not be able to deduct qualified transportation fringe benefits paid after December 31, 2017.

Under section 512(a)(7), if an exempt hospital provides a qualified transportation fringe, say transit passes, for its employees, the amount paid or incurred by the hospital for the transit passes is added to the unrelated business taxable income of the hospital.

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Although IRC Section 512(a)(7) references on-premise athletic facilities fringe benefits as defined in IRC Section 132(j)(4)(B), the statute also states that UBTI is increased only by amounts for which a deduction is not allowable under IRC Section 274. IRC Section 274 does not disallow a deduction for the expense of on-premises athletic facilities as defined in IRC Section 132(j)(4)(B). Therefore, amounts paid or incurred for on-premise athletic facilities will not increase UBTI.

For example, if the exempt hospital makes it's on-site gym to available to its employees, that is not considered a nondeductible fringe benefit and there is no increase in the hospital's UBTI.

Nondeductible Expenses

- Unrelated trade or business expenses
  - Amounts directly connected with regularly carried on unrelated trade or business don’t increase UBTI
  - But, not deductible under IRC 274

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It is important to note that IRC 512(a)(7) specifies that amounts paid or incurred that are directly connected with an unrelated trade or business regularly carried on by the organization, are not included in UBTI. However, under IRC §274 those amounts are not allowed as a deduction when calculating UBTI.

For example, suppose the exempt hospital has a publication and 10 dedicated employees who solicit advertising for the publication. If the hospital provides transit passes for those employees, the amounts paid or incurred will not increase the hospital’s UBTI; however, under 274 those amounts are not deductible from unrelated business income generated from the advertising activity.

Effective Date

- Amounts paid or incurred after 12/31/2017
- Non-calendar year taxpayers may have Fringe Benefit UBTI inclusions under IRC 512(a)(7) for 2017 Tax Year

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The effective date of the amendment applies to amounts paid or incurred after December 31, 2017. This means that taxpayers whose tax year ends after December 31, 2017 will have to report amounts paid or incurred for qualified transportation fringe benefits in their 2017 tax year. Organizations with a fiscal tax year that begins in 2017 have been instructed to enter the amount of any increase in UBTI on line 12 of the 2017 Form 990-T.

For organizations reporting on a calendar year, the first reporting of amounts paid for disallowed fringe benefits would be on the 2018 Form 990-T, which will be due May 15, 2019.

Form/Instruction Changes

- Form 990-T
  - Line 34 – Amounts paid for disallowed fringe benefits included in calculation of UBTI

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IRC 512(a)(7) - Increased UBTI

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Form 990-T for 2018 has been revised to provide a separate line, Line 34, for reporting amounts paid or incurred for disallowed fringe benefits. Form 990-T Instructions direct filers to include amounts paid or incurred for qualified transportation benefits disallowed under IRC 274.

Audit Tips

- Review:
  - HR policy on employee fringe benefits
  - Form 990-T – was this already reported?
  - Form 990 – Part IX- line 9 Expenses – other benefits
  - From 990 Schedule J – Compensation Information
  - Payables – i.e.: payments to transit agencies?
- Interview appropriate parties- do you provide bus/train passes and or parking to employee's?
- Tour facilities- free Employee parking in paid lots

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Tour facilities – employee parking lots with free parking for the employees and where parking in the area is paid

Expected Guidance:

- FAQs
- Regulations

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FAQs will be posted on IRS.gov addressing some of the issues related to IRC 512(a)(7) and disallowed fringe benefits. Review the FAQs once they become available

Refer to Notice 2018-67 proposed regulations previously discussed under 512(a)(6).

Summary

- IRC 512(a)(7): UBTI is increased by amounts paid or incurred for disallowed fringe benefits
  - Qualified transportation fringe benefits
  - Parking facility used for qualified parking
- Some taxpayers may have disallowed fringe UBTI on 2017 Form 990-T

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In summary, according to IRC 512(a)(7), UBTI will increased by the following disallowed fringe benefits:

Qualified transportation and the use of the entity's parking facility for qualified parking. This tax change may impact taxpayer who files on a fiscal year. Therefore, the issue may be present on some taxpayer's 2017 tax return.