SEYFARTH SHAW

One Minute Memo®

Transit Benefit Adjustments for 2014

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Qualified transportation fringe benefits include (1) transportation in a commuter highway vehicle between home and work, (2) transit passes, and (3) qualified parking. The amount of the benefit excludible from an employee's gross income and wages for 2014 was originally limited to $130 per month for the aggregate of transportation in a commuter highway vehicle and transit passes ("transit benefits"), and $250 per month for qualified parking.

In late December 2014, however, the IRS increased the monthly amount of transit benefits excludible from income for 2014 from $130 per month to $250 per month, equaling the exclusion for qualified parking benefits. The increase was effective retroactively to January 1, 2014. Accordingly, any transit benefits provided by an employer (or by an employee pursuant to a compensation reduction arrangement) in excess of $130 up to $250 ("excess transit benefits") are excludible from the employee's gross income.

Notice 2015-2 clarifies how the increase applies for 2014 and provides a special procedure for employers to use in filing Form 941 for the fourth quarter of 2014 to reflect changes in the excludable amount for transit benefits and in filing Forms W-2.

Employer Instructions for W-2s

Employers that paid excess transit benefits must take into account the increased exclusion in calculating the amount of wages reported in box 1, Wages, tips, other compensation; box 3, social security wages; and box 5, Medicare wages.

In addition, employees are entitled to a refund or reimbursement of social security and Medicare taxes paid on the excess transit benefits.

- Employers that reimburse employees prior to furnishing Form W-2 must reduce the amounts of withheld tax reported in box 4, social security tax withheld, and in box 6, Medicare tax withhold, by the amount of the reimbursement. All employers must report in box 2, Federal income tax withhold, the actual amount of income taxes withheld during 2014.
- Employers that reimburse employees after furnishing Forms W-2, but before filing Forms W-2 with the Social Security Administration (SSA) must check the "Void" box at the top of each incorrect Form W-2 (Copy A). The employer must prepare new Forms W-2 and send them to the SSA. "Corrected" should be written on the new copies (B, C and 2) and furnished to employees.
- Employers that have already filed their 2014 Forms W-2 with SSA must file Corrected Wage and Tax Statements, Forms W-2c, to reflect the increased exclusion for transit benefits and to reflect any reimbursements of the FICA tax, and furnish the Forms W-2c to employees. Employees may recoup any Federal/State over-withholding with the filing of their personal income tax returns for 2014.

Recouping Employment Tax Overpayments - Special Procedure. An employer may obtain a refund of overpaid employment taxes on an employee's behalf. Employers who originally reported excess transit benefits as includible in gross income and withheld FICA taxes would normally be required to file Form 941-X for each quarter to make corrections. However, under a special rule, the adjustment can be made on the fourth quarter Form 941 without filing Form 941-X or obtaining employee statements if the employer has not yet filed its Form 941 for the fourth quarter of 2014. (The fourth quarter Form 941 is due ***January 31, 2015***, with 10 additional days permitted if the employers taxes are deposited on time).

Procedure for Employers Who Have Filed Fourth Quarter Form 941 or Have Not Reimbursed Employees Prior to Fourth Quarter Form 941. Employers that have already filed fourth quarter Form 941, or have not reimbursed their employees who received excess transit benefits prior to filing the fourth quarter Form 941, must file a Form 941-X for each quarter and obtain a statement from employees confirming that the employee has not and will not seek a refund of over-withheld amounts.

Guidance on Electronic Payment of Transit Benefits

The IRS also published *Revenue Ruling 2014-32* toward the end of 2014 expanding and in some circumstances clarifying the circumstances under which transit benefits may be purchased with electronic forms of payment. The Revenue Ruling sets forth eight fact situations using smart cards. Here are the highlights of the guidance.

- **Smart cards** contain a memory chip storing certain information that uniquely identifies the card and value stored on the card, and can be used either as fare media or to purchase fare media. Debit cards can be a smart card or a magnetic strip card.
- **Terminal-restricted debit cards** are debit cards that can be used only at terminals that exclusively sell fare media for local transit systems.
- **MCC-restricted debit cards** are debit cards that can be used only at merchants that sell fare media, whether or not they sell other merchandise.

Impact of Terminal-Restricted Debit Cards on Cash Reimbursement Programs. The Internal Revenue Code provides that cash reimbursements for transit passes are not permitted if vouchers (or similar items which can only be exchanged for transit passes) are readily available. The IRS previously announced that it would not challenge cash reimbursements for transit passes based on the availability of vouchers until additional guidance was issued. This Revenue Ruling provides that, after December 31, 2015, employers are no longer permitted to provide qualified transportation fringe benefits in the form of cash reimbursement in geographic areas where a terminal-restricted debit card is readily available.

MCC-Restricted Debit Cards. One fact situation highlights that use of MCC-restricted debit cards may qualify as transit passes if there are restrictions that prohibit the purchase of anything other than fare media for use on local transit systems.

Transit System Smartcards with Multiple Accounts. Another fact situation involves transfers from an employer-funded MCC-restricted debit card to a transit system's smartcard with multiple accounts. The transit system's smartcard includes separate accounts to separately track funds provided directly by an employer that are available only for transit use, funds provided directly by an employer that are only available for nontransit use (e.g., parking), and funds added by the cardholder/employee that are available for either use. Funds in each of the three accounts cannot be transferred between accounts. An employer provides its employees who use the transit system smartcard with an MCC-restricted debit card that can be used to load funds onto the transit system's smartcard. The funds are placed into the account holding funds that are available for either transit or nontransit use. The IRS concluded that this employer-funded MCC-restricted debit card would not qualify for pre-tax treatment because the funds could be used for non-transit purposes.

Further, if the smartcard's employer-funded transit account is readily available, a cash reimbursement program using the debit card would not qualify for pre-tax treatment (even with substantiation) because a voucher or similar item is readily available.

Delivery Charge for Vanpool Vouchers. If a vendor adds a reasonable delivery charge for vanpool vouchers purchased online, the delivery charge can be treated as part of the cost of the transit.

Joy Sellstrom and *Kelly Pointer* are members of the Employee Benefits and Executive Compensation Department. If you would like further information, please do not hesitate to contact your Seyfarth Shaw LLP attorney or any member of the Employee Benefits and Executive Compensation Department.

Seyfarth Shaw LLP One Minute Memo® | January 26, 2015