



BEST

Workplaces
for CommutersSM



Commuter Tax Benefits:

Implementing Commuter Benefits
as One of the Nation's
Best Workplaces for CommutersSM

United States Environmental Protection Agency
Office of Air and Radiation
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Commuter Tax Benefits

Implementing Commuter Benefits as One of the Nation's Best Workplaces for CommutersSM

- ▶ The Federal tax code allows tax-free transportation fringe benefits of up to \$100 per month per employee for transit or vanpool expenses and up to \$195 per month for parking.
- ▶ The employer can cover the cost of the tax-free transportation fringe benefit, allow employees to reserve income on a pre-tax basis to cover the cost, or share the cost.
- ▶ Providing commuter tax benefits to employees can save payroll taxes for employers. The value of the benefit paid to employees is considered a tax-free transportation fringe benefit and not wage or salary compensation, therefore, payroll taxes do not apply. Giving an employee \$100 in transit/vanpool benefits is thus less expensive for an employer than raising the employee's salary by \$100. Allowing employees to reserve income on a pre-tax basis also saves the employer payroll taxes.
- ▶ Employees receive more from tax-free transportation fringe benefits than from a comparable salary increase since they do not pay federal income or payroll taxes on the value of the fringe benefit. Employees who reserve income on a pre-tax basis for a qualified transportation fringe benefit also save money since they do not pay federal income or payroll taxes on the income reserved.
- ▶ Several states provide employers with tax credits for offering commuter benefit programs.
- ▶ Providing transit/vanpool benefits is one of the primary benefits employers participating in Best Workplaces for CommutersSM can offer their employees. Employers must offer at least one of three primary benefits to their employees to be recognized as one of the Best Workplace for CommutersSM (the other two are parking cash out and telecommuting). Under this option, the employer agrees to provide at least \$30 per month in transit/vanpool benefits for any employee whose actual commuting costs are \$30 or more.

Best Workplaces for CommutersSM **The National Standard of Excellence for Commuter Benefits**

This document is one in a series of briefing papers designed to help employers participating in Best Workplaces for CommutersSM implement commuter benefits.

The U.S. Environmental Protection Agency (EPA) and the U.S. Department of Transportation (DOT) have established a voluntary National Standard of Excellence for employer-provided commuter benefits. Commuter benefits help American workers get to and from work in ways that cut air and global warming pollution, improve public health, increase worker productivity, and reduce expenses and taxes for employers and employees. Employers that agree to meet the National Standard of Excellence are recognized as Best Workplaces for CommutersSM and agree to:

- ▶ Centralize commute options information so that it is easy for employees to access and use
 - ▶ Promote the availability of commuter benefits to employees
 - ▶ Provide access to an emergency ride home (ERH) program
 - ▶ Provide one or more of the following primary commuter benefits:
 - ✓ Vanpool or transit benefits of at least \$30 per month;
 - ✓ Parking cash out of at least \$30 per month;
 - ✓ Telecommuting program that reduced commute trips by 6 percent;
 - ✓ Other option proposed by employer and agreed to by EPA. These services must reduce the rate at which employees drive to work alone and be perceived by employees as a significant workplace benefit. Options may include things like vacation time for carpoolers and comprehensive shuttle services.
 - ▶ Provide three or more of the following additional commuter benefits:
 - ✓ Active membership in a Transportation Management Association (TMA) or similar organization; participation in a regional air quality initiative
 - ✓ Membership in a local ozone awareness program
 - ✓ Ridesharing or carpool matching, either in-house or through a local or regional agency
 - ✓ Pre-tax transit or vanpool benefits
 - ✓ Parking cash out less than \$30 per month or less than 75% of the actual parking benefit
 - ✓ Shuttles from transit stations, either employer-provided or through a local agency
 - ✓ Parking at park-and-ride lots or vanpool staging areas
 - ✓ Preferred parking for carpools and vanpools
 - ✓ Employer-run vanpools or bus programs
 - ✓ Employer-assisted vanpools
 - ✓ Secured bicycle parking, showers, and lockers
 - ✓ Electric bicycle recharging stations
 - ✓ Employee commuting awards programs
 - ✓ Discounts/coupons for bicycles and walking shoes
 - ✓ Compressed work schedules
 - ✓ Telecommuting
 - ✓ Lunchtime shuttle
 - ✓ Proximate commute (working closer to home)
 - ✓ Incentives to encourage employees to live closer to work
 - ✓ On-site amenities (dry cleaning, etc.)
 - ✓ Concierge services
 - ✓ Participation/membership in a carsharing program
 - ✓ Other options proposed by employer
- ▶ In addition, employers commit to ensuring that within 18 months of applying at least 14 percent of their employees are not driving alone to work.

Best Workplaces for CommutersSM **The National Standard of Excellence for Commuter Benefits**

Disclaimer

EPA provides this briefing as a service to employers participating in the Best Workplaces for CommutersSM. Information about private service providers is intended for informational purposes and does not imply endorsement by EPA or the federal government.

The information presented here does not constitute official tax guidance or a ruling by the U.S. Government. Taxpayers are urged to consult with the Internal Revenue Service of the U.S. Department of Treasury or a tax professional for specific guidance related to the Federal tax law.

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Commuter Tax Benefits: A Summary

The Federal tax code allows employers to provide tax-free transit, vanpool, and parking benefits to their employees. Called “qualified transportation fringe” benefits, these commuter benefits can be deducted from corporate gross income for purposes of taxation when paid for by an employer. The employer and employee save on taxes since neither pays federal income or payroll taxes on these benefits.

The scope of tax-free commuter benefits was expanded greatly in 1998 with passage of the Transportation Equity Act for the 21st Century (TEA-21). This act amended Section 132(f) of the Internal Revenue Code as it relates to employer-provided commuter benefits. Under the revised tax code, qualified transportation fringe benefits may be offered by employers in three ways:

- ▶ The employer can cover the full cost of the qualified transportation fringe benefit;
- ▶ The employer can allow employees to reserve income on a pre-tax basis to cover the costs of a qualified transportation fringe benefit; or,
- ▶ The employer and employee can share the costs of the benefit. Under current law, transit and vanpool expenses up to \$100 per month (\$1,200 per year) and qualified parking expenses up to \$195 per month (\$2,340 per year) are tax-free.

These tax-free qualified transportation fringe benefits are often referred to as “commuter benefit” programs. Please note that for the purposes of this brief, we refer to “qualified transportation fringe benefits” as “qualified commuter benefits”. Through these programs, employers and employees can receive substantial tax savings in their payroll and federal income taxes. Also, some states, including Maryland, Georgia, and Minnesota, provide state tax credits for employers that implement commuter benefit programs.

Types of Qualified Commuter Benefits

According to the Internal Revenue Code Section 132(f) qualified commuter benefits are excludable from income for purposes of taxation. Qualified commuter benefits include:

Transit Passes -

Transit passes include any vouchers, passes, farecards, tokens, or related items that employees can use to pay for transportation on mass transit facilities or transportation provided by a person in the business of transporting persons for compensation or hire if such transportation has a seating capacity of at least six adults (not including the driver).

Transportation in a Commuter Highway Vehicle -

Better known as a vanpool, the tax code defines a “commuter highway vehicle” as a vehicle that has a seating capacity of at least six adults, not including the driver; at least 80 percent of the vehicle’s mileage results from trips between work and employees’ homes; and during these trips, at least one half of the vehicle’s capacity must be filled (not including the driver).

Qualified Parking -

The term “qualified parking” is defined as parking near or at the employers’ place of business or parking located near or at a place where employees commute to work by mass transit, commuter highway vehicles, or carpools (for example, parking at a transit station, park-and-ride lot, or vanpool staging area).

Qualified commuter benefits include cash reimbursement by an employer to an employee for any of the three benefits described above. However, cash reimbursement is allowed for transit/vanpool benefits only in certain circumstances—when the transaction fees associated with purchasing vouchers are greater than one percent of the vouchers’ face value (described further below).

Tax-Free Limits and Adjustments

Under current tax law, transit and vanpool expenses up to \$100 per month (\$1,200 per year) and qualified parking expenses up to \$195 per month (\$2,340 per year) are tax-free. For future years, annual inflation adjustments may be made on all three benefits.

Three Ways to Provide Tax-Free Qualified Commuter Benefits

Qualified commuter benefits may be offered by employers in three ways:

- 1) **Company covers full cost of the benefit**—Up to \$100 per month for transit and vanpool expenses and \$195 per month for qualified parking expenses is offered tax-free to employees and does not incur payroll taxes for the employer or employee.
- 2) **Company offers a “pre-tax” benefit**—Employees may have up to \$100 per month taken out of their current monthly pay towards the cost of commuting on transit or in vanpools, and up to \$195 per month taken out for qualified parking expenses, before taxes are applied. Employees save federal income and payroll taxes. Many employers prefer this option because the employee pays the cost, and the employer saves money because FICA, Federal Insurance Contributions Act payments to Social Security and Medicare, and unemployment taxes do not apply.
- 3) **Employer and employee share costs**—Under this option, the employer and employee each pay a share. The

employer, for example, might offer \$40 per month in transit/vanpool benefits and allow the employee to reserve up to \$60 per month as a pre-tax benefit. The employer could also offer subsidized parking, paying \$40 per month for a \$100 space, and allowing the employee to pay for the other \$60 through a pre-tax salary deduction.

Tax Savings for Employers and Employees

By offering tax-free qualified fringe benefits, both employers and employees can save taxes.

The tax savings depends on the way the benefits are provided to employees—employer-paid, paid by employees through a pre-tax salary deduction, or a combination of both. This section describes how employers and employees save under each of these options. Sample calculations of tax savings follow in the Sample Tax Savings section.

Option	Employer Tax Benefit	Employee Tax Benefit
Employer-Paid: Employers provide their employees with up to \$100/month to commute via transit or vanpools (typically in the form of passes or vouchers) and/or up to \$195/month in qualified parking.	Compared to providing a salary increase, the employer saves on payroll taxes. No payroll taxes are paid on the value of the benefit.	Employee receives up to \$100/month tax-free to commute via transit or vanpools (and/or \$190/month tax-free for qualified parking). The employee does not pay any taxes on the value of the benefit.
Employee Pre-Tax Deduction: Employers allow employees to reserve up to \$100/month in pretax income to pay for transit or vanpools and/or up to \$195/month to pay for parking.	Employer saves on payroll taxes (7.65% savings if the employee’s salary is below the FICA wage base). No payroll taxes are paid on the income that is reserved by the employee.	Employee saves on income tax and payroll taxes. The amount of the benefit is no longer treated as taxable salary.
Employee, Employer Share Costs: Employers pay transit, vanpool, or qualified parking costs up to a certain limit and the employee pays for the remainder of the costs through a pre-tax deduction. Total employer and employee paid costs cannot exceed the monthly limits of \$100/month for transit and vanpool and \$195 for qualified parking.	Employer saves on payroll taxes (7.65% savings if the employee’s salary is below the FICA wage base) on the portion of the subsidy paid by the employee through a pre-tax deduction, and on the value of the benefit provided to the employee compared to providing a salary increase.	Employee does not have to pay any taxes on the portion of the benefit provided by the employer. Additionally, the employee saves on income tax and payroll taxes by taking a pre-tax deduction to pay for the remainder of his/her commuting costs.

The employer can also deduct the cost of the benefit as a business expense for purposes of calculating corporate income taxes, in the same manner that salary payments to employees can be deducted.

Tax Benefits of Employer-Paid Benefits

If the employer pays for the benefit, the value of the benefit is

- ▶ Tax-free to the employee, and
- ▶ Free of employer payroll (FICA) taxes.

As a result, employer-paid transportation benefits are cheaper to provide than an increase in taxable salary.

For example, as shown in Figure 2, by providing a \$100 per month (\$1,200 per year) transit/vanpool benefit rather than an increase in salary to an employee with an annual salary less than the FICA wage base, the employer saves \$91.80 per year in payroll taxes (\$1,200 times 7.65% FICA).

Meanwhile, the employee saves about \$464 in taxes compared to receiving taxable income (based on a 25% federal income tax, 6% state income tax, and 7.65% FICA). With taxable salary, the employee does not see more than 38 percent of the salary increase. In contrast, the employee receives the full \$1,200 per year (\$100 per month) in transit/vanpool benefits paid by the employer.

Both the commuter benefit and the salary increase may be deducted by the employer as a business expense for purposes of calculating corporate income taxes.

Note that some transit-voucher providers charge an administrative fee for ordering the vouchers, which would slightly increase the cost to the employer. On the other hand, some transit agencies offer discounts for purchasing transit passes in bulk, which would lower the cost. Some states and localities also offer employer tax credits, further lowering the cost to the employer. The employee takes home the full \$1,200 benefit, tax-free. To net an increase in after-tax income of \$1,200 would require a salary increase of over \$1,950.¹

Under Federal tax law, an employee who pays to park at a qualified parking area (such as a transit station) and then takes mass transit or a commuter highway vehicle to work can receive a combination of transit/vanpool and qualified parking benefits, up to a combined benefit of \$295 per month (\$100 for the transit/vanpool benefit and \$195 per month for parking) or a maximum of \$3,540 per year.

Tax Benefits of Employee Pre-Tax Deductions

If the employer does not pay for the fringe benefit, but deducts the pass and/or parking cost from an employee's pre-tax income:

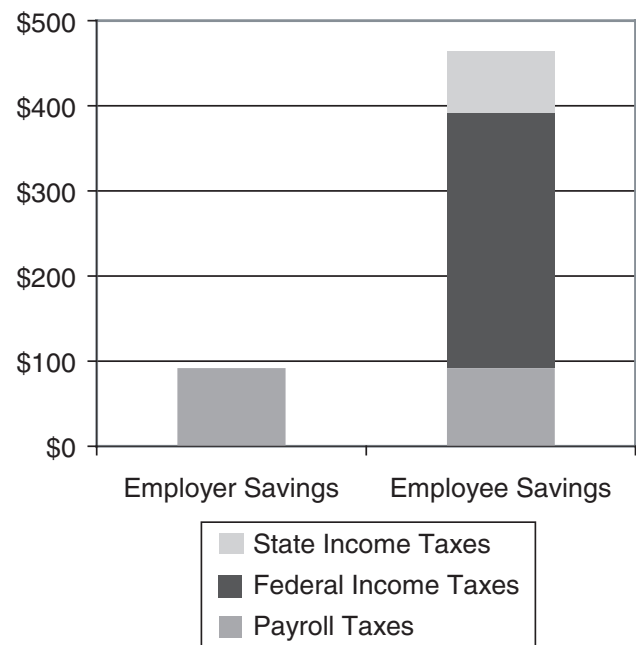


Figure 2: Tax Savings from offering \$1,200 commuter benefit rather than salary (to an employee with an annual salary less than the FICA wage base)

- ▶ the employer sees a reduction in payroll taxes, and
- ▶ the employee does not pay federal income, payroll, and possibly state income taxes on the deducted amount.

Employers do not pay any payroll (FICA) taxes on the amount of income that is reserved by the employee from taxable income. FICA consists of Social Security and Medicare taxes paid on wages. For tax year 2004, employers and employees pay equal amounts: 6.2 percent of wages up to \$87,900 per year per employee for Social Security and 1.45 percent of all wages for Medicare (no salary limit). As a result, for every dollar that an employee reserves for a pre-tax transportation fringe benefit, the employer saves about 7.65 cents (for employees making less than \$87,900 per year).² An employee who reserves \$100 per month for transit or vanpools will save over \$91 per year for the employer in reduced FICA taxes. If an employee reserves the full \$195 per month for qualified parking, employer tax savings would be \$179 per year.

Employees also receive substantial tax savings. An employee in the 25% federal tax bracket who reduces his or her pre-tax income by \$100 per month to pay for transit or vanpooling

¹ Some transit systems add value when fares are purchased in larger increments, resulting in a larger employee benefit.

² Because Social Security taxes do not apply on income above \$87,900 per year (in 2004), employer and employee tax savings from commuter benefit programs would be less for an employer with many higher paid employees than one with more lower paid employees.

expenses could save \$300 per year in federal income taxes and an additional \$91.80 in payroll taxes. Employees could also save on state income taxes that piggyback on the federal tax definitions of compensations. For example, in a state with a 6% income tax, employees could save another \$72 in taxes. In total, an employee could be saving over \$463 each year. This brings the real transit cost to the employee down from \$100 per month to \$61.35 per month, a savings of almost 40%.

Employer/Employee Cost Sharing

Both employers and employees benefit when an employer shares the cost of commuting with employees by paying a portion of commute expenses as an additional benefit and allowing employees to deduct the rest of their expenses (up to the monthly limit) from their pre-tax income. For example, if an employer decides to provide up to \$30 per month (\$360 per year) for transit and allows the employee to take the additional \$70 (\$840 per year) from pre-tax income, the employer would save \$64.26 in payroll taxes on the \$840 in pre-tax income. The employer also would save \$27.54 in payroll taxes compared to offering the \$30 as salary, for a combined savings of \$91.80 per year per participating employee. Regardless of whether the employer provides \$1,200 to the employee as a qualified commuter benefit or as additional salary, the employer saves on corporate income taxes as both are tax deductible.

Employee tax savings are also substantial under this approach. By taking \$360 per year as a tax-free commuter benefit, rather than as a salary increase, the employee takes home an additional \$139.14 (assuming a 25% Federal income tax rate, a 6% state income tax rate, and a 7.65 percent rate for FICA). Also, by paying for the remainder of transit expenses (\$840 per year) with pre-tax income, an employee can save up to \$324.66 in taxes (once again assum-

ing a 25% Federal income tax rate, a 6% state income tax rate, and a 7.65% rate for FICA taxes), for a combined savings of \$463.80 per year.

As a salary substitute, an additional benefit, or a combination of the two, transportation benefits provide more value for less money than cash. For more examples, see the following section.

Sample Tax Savings

This section contains sample calculations for tax savings associated with different types of commuter benefit programs. For all examples, it is assumed that the employee is single with no dependants, pays at a federal income tax rate of 25 percent, and makes less than the taxable wage base. Corporate income taxes are assumed to be 34 percent.

Example 1: Employee Pays with Pre-Tax Income³

Craig is an employee at Acme Corporation, making \$3,600 per month. Acme Corporation offers its employees commuter benefits, including allowing employees to pay for transit and vanpool passes using pre-tax income, up to the monthly limit of \$100. Craig elects to do this and uses pre-tax income to purchase his monthly transit pass, which costs \$90 per month. By electing to use pre-tax income to pay for his transit pass, \$90 is taken out of Craig's monthly, pre-tax income, thereby saving him the FICA and federal income taxes that would normally be applied to that \$90 had he purchased his tickets using the money from his paycheck.

Both Craig and Acme pay less in taxes with the pre-tax deduction option. The transit pass costs Craig one-third less (\$90 minus \$29.39, or \$60.61) than if he had paid for it through taxable income, with a net tax savings to the employer.

Employer (per Employee)			Employee		
	Pre-Tax Income	Regular Salary		Pre-Tax Income	Regular Salary
Direct Cost	\$0	\$0	Direct Cost	\$90	\$90
FICA Cost	—	\$6.89	FICA Cost	—	\$6.89
Corporate Income Tax	—	—	Income Tax	—	\$22.50
Savings per Month	\$6.89	—	Savings per Month	\$29.39	—
Savings per Year	\$82.62	—	Savings per Year	\$352.62	—

³ This example was modified from an example given in a publication entitled "Tax Laws and Commute Related Expenses," which was developed by Charlene Fleming, MPAcc, President, K.E. & Associates, Seattle, Washington, in November 1999 for King County Metro.

Example 2: Employer Pays

Acme Corporation has decided to provide employees with a tax-free transit/vanpool voucher of up to \$90 per month (\$1,080 per year) to help pay commute expenses. Craig elects to accept an employer-paid monthly transit pass worth \$90 per month. Over the course of a year, he will receive \$1,080 worth of transit passes. For both Craig and Acme Corporation, this arrangement is better than giving him a \$1,080 raise since Craig actually receives more money and

Acme pays less. If Acme Corporation had raised Craig's annual salary by \$1,080, he would only receive \$727.38 in post-tax income. Because transit benefits are tax-free, he receives the full \$1,080 benefit. The transit pass is free to Craig, providing him with a no-cost commute. In total, Craig saves about \$352.62 in taxes when his employer provides him with a tax-free transit benefit rather than the same benefit in salary.

Employer (per Employee)			Employee		
	Pre-Tax Income	Regular Salary		Pre-Tax Income	Regular Salary
Direct Cost	\$90.00	\$90.00	Direct Cost	\$90.00	\$90.00
FICA Cost	—	\$6.89	FICA Cost	—	\$6.89
Corporate Income Tax	(\$30.60)	(\$30.60)	Income Tax	—	—
Net Cost	\$59.40	\$66.29	Net Benefit	\$90.00	\$60.62
Savings per Month	\$6.89	—	Savings per Month	\$29.39	—
Savings per Year	\$82.62	—	Savings per Year	\$352.62	—

Note: Craig's take home pay through a salary increase would be even lower if he was subject to state and/or local income taxes, since this calculation does not include state or local income taxes.

Example 3: Shared Costs

Acme Corporation has decided to provide a tax-free fringe benefit of \$65 per month. Employees whose commute expenses exceed this will be allowed to pay the remainder of their expenses using pre-tax income. For Craig, this means

that he will take the \$65 tax-free fringe benefit and then use pre-tax income to pay for the remaining \$25 of his transit pass expenses.

Impact on Employer (per Employee) for Employer's Contributions			Impact on Employee for Employer's Contributions		
	Transit Benefit	Salary Increase		Transit Benefit	Salary Increase
Direct Cost	\$65.00	\$65.00	Direct Cost	\$65.00	\$65.00
FICA Cost	—	\$4.97	FICA Cost	—	\$4.97
Corporate Income Tax	(\$22.10)	(\$22.10)	Income Tax	—	\$16.25
Net Cost	\$42.90	\$47.87	Net Benefit	\$65.00	\$43.78
Savings per Month	\$4.97	—	Savings per Month	\$21.22	—
Savings per Year	\$59.67	—	Savings per Year	\$254.67	—

Impact on Employer (per Employee) for Employee's Contributions		Impact on Employee for Employee's Contributions	
	Transit Benefit		Transit Benefit
Direct Cost	\$0	Direct Cost	\$25.00
FICA Cost	\$1.91	FICA Cost	\$1.91
Corporate Income Tax	—	Income Tax	\$6.25
Savings per Month	\$1.91	Savings per Month	\$8.16
Savings per Year	\$22.92	Savings per Year	\$97.95
Total Impact		Total Impact	
Total Monthly Cost	\$40.99	Total Monthly Cost	\$16.84
Total Annual Cost	\$1.91	Total Annual Cost	\$1.91

Acme's total cost per month for the benefit is \$40.99, which consists of \$42.90 net cost for the \$65 benefit and \$1.91 FICA savings from the employee's pre-tax income. As a

result, the company pays \$491.85 per year. As shown above, Craig only pays \$16.84 per month for the transit benefit with a \$90 value.

State Tax Credits

State Tax Credits for Employer-Provided Transit/Vanpool Benefits

A number of states have implemented tax incentive programs to encourage employers to provide transit/vanpool benefits to their employees. These programs increase the cost savings for businesses:

Maryland—The Maryland Commuter Tax Credit provides a 50% tax credit, up to \$30 per employee per month, for provision of transit passes, vanpool benefits, and reimbursement for carpooling expenses. Employers can elect to which tax they wish to apply the credit, such as the state income tax, the financial institution franchise tax, or the insurance premium tax. The tax credit essentially subsidizes the implementation of commuter benefits, although it is broader because the tax credits can also be used to offset monthly, employee carpooling costs. Under Federal law, any carpool expense reimbursements are taxable, as they are not considered qualified transportation fringes under Section 132 (f) of the Internal Revenue Code. The Maryland Commuter Benefits Act of 2000 allows a credit against specified state taxes for employers who provide employees a parking cash out or an emergency ride home program. It also allows specified tax-exempt organizations to apply tax credits allowed for employer-provided commuter benefits as a credit against the payment of employee withholding taxes and required to be paid to the Comptroller. Finally, the Act also established reporting requirements to help assess the success of the program.

Georgia—Employers providing employees with designated commuter benefits, including transit passes, transportation in a commuter highway vehicle, and qualified parking, are eligible to receive an annual \$25 tax credit for each employee receiving a commuter benefit. The credit cannot exceed the expense to the employer in providing the benefit and the alternative method of transportation must be used at least 10 days per month.

Minnesota—In Minnesota, tax credits can be received by employers who provide employees with transit passes (for use in Minnesota only) for transportation via either a public or privately owned mass transit facility or by a person in the business of transporting people for compensation or hire. Vehicles hired to transport employees must seat at least six people (not including the driver). The credit is equal to 30 percent of the difference between what the employer pays for the passes and what employees are charged for the passes. The

credit is nonrefundable and can only be used in the current tax year. The types of organizations eligible for the tax credit include C corporations, S corporations, sole proprietors, insurance companies, fiduciaries, and nonprofit organizations.

Delaware—Employers with approved Travelink plans/programs can receive either a 10% tax credit based on the direct cost of developing, implementing, and maintaining a program, a credit based on the ratio of commuter trip reductions versus commuter trips generated, or a credit of \$250 per commute trip reduced (whichever results in the smaller amount).

Connecticut—Employers in Connecticut with 100 or more employees are eligible for a tax credit for any taxable year after January 1, 1997 equal to 50% of the employer's direct costs for implementing a traffic reduction program, up to a limit of \$250 per participating employee. Eligible programs must have been implemented after January 1, 1995. The total amount of credits available each year to corporations under this program is \$1.5 million.

Oregon—Under the Oregon Business Energy Tax Credit Program, employers can receive a tax credit equal to 35% of project costs for projects involving commute reduction, investments in cleaner-fuel vehicles; participation in various conservation and renewable energy projects and recycled materials markets; and involvement in the research and development of new, energy-efficient technologies. Eligible commute reduction programs must decrease work-related travel and eligible costs include those from telework programs, providing transit passes, commuter pool vehicle arrangements, financial incentive programs, bicycle projects, and transportation management association membership dues. The credit is taken over five years, with 10% taken the first and second year and 5% taken in each subsequent year.

New Jersey—The Smart Moves for Business Tax Credit Program provides a tax credit to eligible corporations equal to either 10% of the costs attributed to implementing an authorized commuter transportation benefits plan/report or up to \$124 per participating employee. For partnerships or limited liability corporations, the program provides a tax credit of either 157% of the costs attributed to implementing an authorized commuter transportation benefits plan/report or up to \$1,947 per participating employee. For each type of employer, the tax credit is taken for the smaller amount of the two calculations and the employer decides to which tax the credit applies.

Sample Calculation of Tax Savings with a State Tax Credit⁴

The following calculations illustrate the savings of an employer in Maryland who provides its employees with up to \$60 per month for transit passes. State tax credits may reduce the amount of federal tax savings, due to smaller federal deductions for state taxes.

Monthly Cost of Transit Pass (per participating employee)	\$60.00
Maryland State Tax Credit (50% of transit pass cost)	(\$30.00)
Total Business Expense	\$30.00
Federal Corporate Income Tax Savings (at 34% of \$30 Business Expense)	(\$10.20)
Monthly Cost of Transit Pass to Employer	\$19.80

Employers should discuss state tax credit implications with a qualified tax advisor.

State Tax Credits for Employer Commute Programs

Several states have implemented other types of tax incentives to encourage employers to adopt programs to encourage employees to commute to work without using a single occupancy vehicle. Many of these programs were passed prior to the passage of TEA-21 and address a broad range of transportation alternatives.

Employer Questions and Answers⁵

Are all employees eligible for qualified commuter benefits?

Yes. Any employee or group of employees can be offered a qualified commuter benefit. The employer has the discretion to choose which employees are offered the benefit and the amount of the benefit can vary from employee to employee. There are only two restrictions on who can receive the qualified commuter benefits. First, it must be given only to employees who will use it for their daily commute to and from work, and not for personal travel. Second, individuals who are employed as partners in a company, who are self-employed, or who are more than two percent shareholders of a subchapter S corporation are not eligible.

If I implement a transit/vanpool benefit program, am I required to offer the full value of the benefits to my employee (e.g., \$100 for transit/vanpool programs and \$195 for qualified parking)?

No. An employer may provide benefits of any amount, or provide no assistance, in the purchase of vouchers.

If a monthly transit pass costs \$125 per month, am I limited to providing a \$100 benefit per month?

No. An employer may provide transit/vanpool benefits of any amount. The tax-free benefit for transit/vanpool benefits, however, is currently limited to \$100 per month. As a result, the employee and employer must pay taxes on the value of the benefit that exceeds the \$100 statutory limit. For example, if the employer provides the employee with a monthly pass valued at \$125 per month, \$100 is a tax-free fringe benefit, and the excess—\$25—must be included in the employee's wages for income and employment tax purposes. Similarly, if the employer offers a pre-tax salary deduction option, the employee may be allowed to purchase a pass with a value of more than \$100 per month. Then, \$100 per month will be deducted from the employee's wages for income and employment tax purposes. The remaining cost will be included in taxable salary but be used by the employer to purchase the pass.

How are benefits treated if an employee terminates employment and the transit pass covers multiple months?

In general, the value of transit passes provided in advance to an employee for a month in which the individual is not an employee must be included in the employee's wages for income tax purposes. Transit passes distributed in advance to an employee are excludable from wages for income and employment tax withholding purposes if the employer distributes transit passes to the employee in advance for not more than 3 months. At the time the passes are distributed, there cannot be an established date that the employee's employment will terminate (for example, if the employee has given notice of retirement) occurring before the beginning of the last month of the period for which the transit passes are provided. Assume the employer distributes transit passes quarterly, and the employee elects to have \$300 deducted from salary to cover transit vouchers for April, May, and June. If employment terminates on May 31, and there was not an established date of termination at the time the transit passes were distributed, then the value of the transit passes

⁴ This example is based on an example and information found in a brochure by the Maryland Department of Transportation and Maryland Department of the Environment called "Maryland's New Commuter Tax Credit."

⁵ Questions and answers were based on information found at the following Web sites: www.bwc.gov, www.fta.dot.gov/library/policy/tvbp.html, and tmi.cob.fsu.edu/act/f_tool.htm

provided for June (\$100) is excludable from the employee's wages for employment tax purposes.

However, the value of the transit passes distributed for June (\$100) is not excludable from wages for income tax purposes. If the employee's termination date was established at the time the transit passes were provided, then the \$100 is included in the employee's wages for both income and employment tax purposes.

Question: Under what circumstances can an employer offer benefits in the form of cash payments rather than using transit vouchers or passes?

The tax code states that transportation reimbursements must be made through transit vouchers or passes, rather than cash payments, unless the employer can show that the voucher provider charges a fee in excess of one percent of the average annual value of the voucher. Internal administrative costs that cannot be considered in determining voucher availability include expenses incurred by the employer to distribute the vouchers (i.e., if the employer chooses to mail vouchers to employees, the postal fee cannot be considered); any additional security measures that must be taken to safeguard the vouchers; expenses incurred to advertise the provision of transit vouchers; etc.

Example: Acme Corporation would like to provide a transit benefit up to \$100 per month to all employees who commute to work via subway. The local transportation management association (TMA) charges a 0.5% fee for providing passes to employers. Because Acme does not have a central location where passes can be picked up, it will have to distribute the passes by sending them to employees via regular mail on a monthly basis. This will cost the company approximately \$1,000 per year in postal fees in addition to the cost of having a Human Resources employee prepare the envelopes, bring them to the post office, etc. To save money, Acme would prefer to provide cash reimbursements to employees rather than distribute the passes each month. Due to the requirements of the federal regulations, Acme is not allowed to do this. The only cost that Acme can take into consideration when deciding how to distribute the passes is how much the TMA charges for the vouchers. In this case, the TMA charges less than one percent and therefore, Acme must purchase the vouchers instead of providing a cash payment. The personnel costs and costs of distributing the passes via mail cannot be considered because they are internal administrative costs.

What are the typical internal administrative (and other) costs faced by employers who implement commuter benefit programs?

The most common internal administrative costs faced by employers who implement commuter benefit programs include the cost of managing the program on a day-to-day basis, marketing the program to employees, distributing transit passes or vouchers, etc. Other internal costs depend on the type of program that the employer chooses to establish. For example, if an employer sets up a vanpool program, then typical costs could include the amount of money spent on purchasing or leasing a commuter highway vehicle, finding and/or training someone to drive the vehicle, and any additional insurance expenses.

Does a qualified commuter benefits plan have to be in writing?

No. The Internal Revenue Code does not require that a commuter benefits plan be in writing or that any form of written plan be submitted to the IRS. However, a company may wish to have certain written rules in order to answer employee questions and describe how the commuter benefit program operates. For example, an employer could write a plan that describes:

- ▶ Which employees are eligible to receive commuter benefits
- ▶ What benefits will be provided by the company
- ▶ How the company vanpool and emergency ride home programs operate, and
- ▶ The procedure for enrolling in and discontinuing participation in the benefits program

The company should not submit this plan to the IRS, but should make it available to all employees.

What are the payroll tax requirements for qualified commuter benefits?

Qualified commuter benefits that do not exceed the statutory monthly limit are not considered wages for purposes of FICA, the Federal Unemployment Tax Act (FUTA), and federal income tax withholding. Any amount by which an employee elects to reduce compensation under the limit is not subject to the FICA, the FUTA, and federal income tax withholding. Qualified commuter benefits exceeding the applicable statutory monthly limit are wages for purposes of the FICA, the FUTA, and federal income tax withholding and are reported on the employee's Form W-2, Wage and Tax Statement. Also, cash reimbursements to employees (for example, cash reimbursement for qualified parking) in excess

of the applicable statutory monthly limit are treated as paid for employment tax purposes when actually or constructively paid. Employers must report and deposit the amounts withheld in addition to reporting and depositing other employment taxes. To receive payroll tax savings, employees do not have any additional paperwork requirements beyond those normally performed when filing taxes.

Information and Contacts

The Internal Revenue Code that governs employer provided commuter benefits is found at 26 USC Section 132(f), and is available on the Web at uscode.house.gov/usc.htm or tmi.cob.fsu.edu/act/f_benefit.htm.

For more information relating to qualified transportation fringes in Section 132(f), visit the Internal Revenue Service (IRS) Web site at www.irs.gov.

This site contains useful information for employers regarding the tax treatment of fringe benefits. Some publications available from the IRS that may be useful include:

- ▶ Publication 15a, Employer's Supplemental Tax Guide—Section 6. Employee Fringe Benefits www.irs.gov/pub/irs-pdf/p15b.pdf.
- ▶ Publication 15b, Employer's Tax Guide to Fringe Benefits—Transportation (Commuting) Benefits www.irs.gov/pub/irs-pdf/p15b.pdf.
- ▶ Final Regulation Concerning Qualified Transportation Fringe Benefits (Issued January 11, 2001) frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=2001_register&docid=01-294-filed.

For more information relating to qualified commuter benefits in Section 132(f), send a written request to:

Freedom of Information Reading Room

PO Box 795
Ben Franklin Station
Washington DC, 20044b

Or contact Patricia Holtzworth at the IRS at 202-622-6040.

Appendix A: Internal Revenue

Code Section 132(F)

(f) Qualified transportation fringe

(1) In general

For purposes of this section, the term “qualified transportation fringe” means any of the following provided by an employer to an employee:

(A) Transportation in a commuter highway vehicle if such transportation is in connection with travel between the employee’s residence and place of employment.

(B) Any transit pass.

(C) Qualified parking.

(2) Limitation on exclusion

The amount of the fringe benefits which are provided by an employer to any employee and which may be excluded from gross income under subsection

(a)(5) shall not exceed—

(A) \$100 per month in the case of the aggregate of the benefits described in subparagraphs (A) and

(B) of paragraph (1), and

(B) \$195 per month in the case of qualified parking.

(3) Cash reimbursements

For purposes of this subsection, the term “qualified transportation fringe” includes a cash reimbursement by an employer to an employee for a benefit described in paragraph

(1). The preceding sentence shall apply to a cash reimbursement for any transit pass only if a voucher or similar item which may be exchanged only for a transit pass is not readily available for direct distribution by the employer to the employee.

(4) No constructive receipt

No amount shall be included in the gross income of an employee solely because the employee may choose between any qualified transportation fringe and compensation which would otherwise be includible in gross income of such employee.

(5) Definitions

For purposes of this subsection—

(A) Transit pass. The term “transit pass” means any pass, token, farecard, voucher, or similar item entitling a person to transportation (or transportation at a reduced price) if such transportation is—

(i) on mass transit facilities (whether or not publicly owned), or

(ii) provided by any person in the business of transporting persons for compensation or hire if such transportation is provided in a vehicle meeting the requirements of subparagraph (B)(i).

(B) Commuter highway vehicle. The term “commuter highway vehicle” means any highway vehicle—

(i) the seating capacity of which is at least 6 adults (not including the driver), and

(ii) at least 80 percent of the mileage use of which can reasonably be expected to be—

(I) for purposes of transporting employees in connection with travel between their residences and their place of employment, and

(II) on trips during which the number of employees transported for such purposes is at least 1/2 of the adult seating capacity of such vehicle (not including the driver).

(C) Qualified parking. The term “qualified parking” means 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 by transportation described in subparagraph (A), in a commuter highway vehicle, or by carpool. Such term shall not include any parking on or near property used by the employee for residential purposes.

(D) Transportation provided by employer. Transportation referred to in paragraph (1)(A) shall be considered to be provided by an employer if such transportation is furnished in a commuter highway vehicle operated by or for the employer.

(E) Employee. For purposes of this subsection, the term “employee” does not include an individual who is an employee within the meaning of section 401(c)(1).

(6) Inflation adjustment

(A) In general

In the case of any taxable year beginning in a calendar year after 1999, the dollar amounts contained in subparagraphs

(A) and (B) of paragraph

- (2) shall be increased by an amount equal to—
- (i) such dollar amount, multiplied by
 - (ii) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting “calendar year 1998” for “calendar year 1992”.

(A) is not a multiple of \$5, such increase shall be rounded to the next lowest multiple of \$5.

(7) Coordination with other provisions

For purposes of this section, the terms “working condition fringe” and “de minimus fringe” shall not include any qualified transportation fringe (determined without regard to paragraph (2)).

(B) Rounding

If any increase determined under subparagraph

Source: IRS Tax Code (www.irs.gov).

Appendix B: Employer Tax Savings Worksheet

The following calculations can be used to estimate an employer’s tax savings from implementing a commuter benefit program.

Option 1: Tax-Free Transportation Fringe Benefit

This section calculates the tax savings for employers who offer commuter benefits as an employer-paid, transportation fringe benefit, compared to providing the same benefit as additional salary.

1. Yearly Cost of Benefit Per Employee
(i.e., the maximum amount the employer provides up to statutory limit) _____
2. FICA rate (for participants below FICA wage base) 0.0765
3. FICA Tax Savings per Participating Employee (*Line 1 x Line 2*) _____
4. Number of Participating Employees _____
5. Total FICA Tax Savings (*Line 3 x Line 4*) _____

Option 2: Pre-Tax Benefit

This section is for employers who allow employees to use pre-tax income to pay for qualified commute expenses.

1. Average amount of pre-tax income deducted from each participating employee (up to statutory limit) _____
2. FICA rate (for participants below FICA wage base) 0.0765
3. Average FICA Tax Savings per Participating Employee (*Line 1 x Line 2*) _____
4. Number of Participating Employees _____
5. Total FICA Tax Savings (*Line 3 x Line 4*) _____

Option 3: Cost Sharing

Employers who share commute costs with participating employees can calculate their tax savings using the two options above. First, calculate the payroll tax savings from offering employees the tax-free benefit rather than a salary increase. Second, calculate payroll tax savings from allowing employees to use pre-tax income to pay for the benefit.

Appendix C: Brief History

Since the early 1990s, federal legislation and actions have enabled and expanded the range of commuter benefits that employers can offer their employees. This section briefly describes the evolution of the qualified transportation fringe benefit program.

Pre-1992: Parking is Only Qualified Transportation Fringe Benefit.

Prior to 1993, parking was the only transportation fringe benefit specifically excluded under the federal tax code. Transit passes were considered *de minimus* fringe benefits. A *de minimus* benefit is a service or item of such small value or provided so infrequently as to make accounting for it impractical or impossible. As a result, transit benefits were allowed to be offered tax-free to employees as long as they were of small value. The initial *de minimus* value was defined at \$15 per month, which was later adjusted to \$21 per month. Vanpool benefits were considered neither transportation fringe benefits nor *de minimus* benefits.

1992: Energy Policy Act of 1992 Expands Qualified Transportation Fringe.

In 1992, Congress passed the Energy Policy Act of 1992 (Pub. L. No. 102-486). This Act was important in that it expanded the term *qualified transportation* fringe to include transit passes and transportation in commuter highway vehicles (i.e., vanpools) in addition to qualified parking. As a result, it allowed the employer, for the first time, to offer vanpool benefits tax-free. It also allowed transit passes to be provided to employees tax-free at a higher value than allowed for a *de minimus* fringe. The Act imposed a tax-free limit of \$60 per month on transit/vanpool benefits and \$155 per month for qualified parking. It provided an inflation adjustment to these limits based on changes in the consumer price index (CPI), with increases to rise in increments of \$5. In order to receive tax-free status, all benefits were required to be offered in addition to, and not in lieu of, salary. The Act applied to benefits provided after December 31, 1992.

1995: Tax-Free Limit on Transit/Vanpool Benefits Rises to \$65 per Month.

In accordance with the inflation adjustment provisions of the Energy Policy Act of 1992, the monthly tax-free limit for commuter highway vehicle and transit passes was raised from \$60 to \$65 for tax years beginning in 1996.

1997: Taxpayer Relief Act of 1997. The Taxpayer Relief Act of 1997 (Pub. L. No. 105-34) amended the Federal tax code to allow qualified parking to be provided to employees in lieu of salary beginning December 31, 1997. As noted above, the tax code previously stated that transportation fringe benefits could not be taken in lieu of salary. As a result, prior to 1998, the tax code created a major barrier for employers that wanted to offer their employees cash in lieu of parking (parking cash out): if they offered a choice of cash or parking, all employer-provided parking would become taxable. By allowing parking benefits to be taken in lieu of salary, the Taxpayer Relief Act of 1997 allowed employers to offer their employees the option of accepting taxable cash income in lieu of a parking space at work, while maintaining the tax-free status of the parking benefit. The employer would only have to pay taxes on the cash payment, not the parking benefit.

1998: Transportation Equity Act for the 21st Century (TEA-21). The Transportation Equity

Act for the 21st Century (Public Law 105-178), which was enacted on June 9, 1998, amended the Internal Revenue Code to allow any qualified transportation fringe to be provided in lieu of salary. Just as the Taxpayer Relief Act of 1997 allowed qualified parking benefits to be taken in lieu of income, TEA-21 expanded this to also allow transit pass and commuter highway vehicle benefits to be taken in lieu of other monetary compensation. The Act also raised the tax-free limit on transit pass and commuter highway vehicle benefits from \$65 to \$100 per month, starting in 2002.

1999: Commuter Choice Initiative launched.

In 1999, the federal government started the Commuter Choice Initiative. As part of this, FTA released the Commuter Choice Toolkit and the U.S. Environmental Protection Agency, in collaboration with the U.S. Department of Transportation, initiated the Commuter Choice Leadership Program to honor employers providing commuting benefits to their employees.

2001: Final Regulation: Qualified Transportation Fringe Benefits.

On January 11, 2001, the Internal Revenue Service issued final regulations concerning qualified transportation fringe benefits and their excludability from employees' gross income. The regulations provide rules to ensure that transportation benefits provided to employees are excludable from gross income. These regulations provide clarification regarding under what circumstances transportation fringes may be provided pursuant to a compensation reduction agreement, the ability to carry over excess amounts to subsequent peri-

ods, reporting requirements, and use of cash payments rather than transit vouchers or passes.

2002: Best Workplaces for CommutersSM unveiled.

In 2002, the U.S. Environmental Protection Agency and the U.S. Department of Transportation unveiled the Best Workplaces for CommutersSM list, a list to honor and to recognize employers who offer their employees outstanding commuting benefits. Participating companies earn the designation “Best Workplaces for CommutersSM”—a mark of excellence for environmentally and employee-friendly organizations. The program builds on the efforts of many top employers to help get employees to work safely, on time, and free of commute-related stress. It provides the tools, guidance, and promotion

necessary to help U.S. employers of any size incorporate commuter benefits into their standard benefits plan, reap financial benefits, and gain national recognition. The list replaces and builds upon the work begun by the Commuter Choice Leadership Initiative to recognize employers who offer their employees outstanding commuting benefits.

For More Information

This guidance document and other information about Best Workplaces for CommutersSM are available at <www.bwc.gov> or by calling the Best Workplaces for CommutersSM voicemail request line at 888 856-3131.

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Visit www.bwc.gov • Call 888 856-3131 • E-mail bwc@epa.gov

