## Section 132.—Certain Fringe Benefits

*26 CFR 1.132–9(b): Qualified transportation fringes.*

**Parking reimbursements.** This ruling holds that certain amounts paid to an employee as "reimbursements" for a parking expense that the employee supposedly "paid" through a salary reduction are wages for purposes of the Federal Insurance Contributions Act (FICA), the Federal Unemployment Tax Act (FUTA), and the collection of income tax at source on wages (federal income tax withholding).

## Rev. Rul. 2004–98

ISSUE(S)

Whether, under the facts described below, the exclusion from gross income under § 132(a)(5) applies to payments from an employer to employees characterized as "reimbursements" by the employer.

FACTS

Employer X decides to provide parking for its employees. The parking will be on or near X's business premises.

Before X implements the arrangement for parking, as described below, X pays Employee A monthly wages of $1,500. After withholding for employee FICA tax of $114.75 and withholding for federal income tax of $83.80, A's net pay is $1,301.45.

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| Monthly wages | $1,500.00 |
| FICA tax withholding | (114.75) |
| Federal income tax withholding | (83.80) |
| Net monthly payment | $1,301.45 |

X implements a payroll arrangement under which the amount of its employees' cash compensation is reduced in return for X providing parking. In addition, X makes "reimbursement" payments to employees with respect to parking expenses in amounts that cause employees' net after-tax pay from X to be the same amount as it would have been if there was no compensation reduction. X takes the position that both the compensation reduction amounts and the "reimbursement" payments are excluded from gross income of employees and are not subject to Federal Insurance Contributions Act (FICA) tax, Federal Unemployment Tax Act (FUTA) tax, or federal income tax withholding.

X can make the compensation reduction used to pay for parking under X's payroll arrangement mandatory or elective. For example, X could unilaterally reduce all employees' salaries and provide parking to all employees. Alternatively, X could offer employees the choice, as permitted under section 132(f)(4), between cash compensation and parking, and provide parking to the employees electing to reduce their cash compensation.

After X implements the arrangement, Employee A's monthly wages of $1,500 are reduced by $100 in exchange for the parking. From the remaining $1,400, X withholds employee FICA tax of $105 and federal income tax of $73.30. X then pays A an additional $79.75 as a purported reimbursement of parking expenses, with the result that A's net pay remains at $1,301.45.

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| Monthly wages | $1,400.00 |
| FICA tax withholding | (105.00) |
| Federal income tax withholding | (73.30) |
| Subtotal | $1,221.70 |
| Additional payment | 79.75 |
| Net monthly payment | $1,301.45 |

LAW AND ANALYSIS

Section 132(a)(5) provides that any employer-provided fringe benefit that qualifies as a "qualified transportation fringe" is excluded from gross income. Section 132(f)(1) provides that the term "qualified transportation fringe" means (1) transportation between home and work in a commuter highway vehicle, (2) any transit pass, and (3) qualified parking. Under § 132(f)(5)(C), the term "qualified parking" means parking provided by an employer to an employee on or near the employer's business premises.

Section 132(f)(4) provides that 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 that would otherwise be includible in the gross income of such employee.

Section 132(f)(3) provides that a qualified transportation fringe includes a cash reimbursement by an employer to an employee for qualified parking expenses. Section 1.132–9(b) Q/A–16(a) of the regulations provides that a reimbursement must be made under a *bona fide* reimbursement arrangement within the meaning of § 1.132–9(b) Q/A–16(c) in order to be excluded from gross income. Section 1.132–9(b) Q&A–16(c) provides that employers that make cash reimbursements must establish a *bona fide* reimbursement arrangement to establish that their employees have, in fact, incurred expenses for qualified parking. The employer must implement reasonable procedures to ensure that an amount equal to the reimbursement was incurred by the employee for qualified parking.

Sections 3121(a) and 3306(b) define the term "wages" for FICA and FUTA purposes, respectively, as all remuneration for employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash, with certain specified exceptions. Section 3401(a) contains a similar definition for purposes of federal income tax withholding. Sections 3121(a)(20), 3306(b)(16), and 3401(a)(19) provide for purposes of FICA, FUTA, and federal income tax with-

holding, respectively, that the definition of "wages" does not include any benefit provided to or on behalf of an employee if, at the time such benefit is provided, it is reasonable to believe that the employee will be able to exclude such benefit from income under § 132.

X's position with respect to the transaction described in this ruling is meritless. An employee may exclude from gross income employer reimbursements for qualified parking expenses, but only if those expenses were actually incurred by the employee. If an employee is given a choice between cash compensation or an employer-provided benefit under a statutory exception to the constructive receipt rules, such as § 132(f)(4), or if an employer unilaterally reduces an employee's cash compensation for the purpose of providing a non-taxable benefit, the benefit is treated as provided directly by the employer rather than purchased by the employee with the amount of the compensation reduction. Otherwise, the value of the benefit would not be excluded from the employee's gross income. The cost of providing the parking is incurred by Employer X, not Employee A, and the value of the benefit is excludable from A's gross income under § 132(a)(5) because the parking is on or near X's business premises, and the parking benefit is provided by X. Although the § 132(a)(5) exclusion applies to the qualified parking benefits provided by X, there is no expense incurred by Employee A for X to reimburse, and therefore the "reimbursement" payments that X makes to A are not excluded from gross income under § 132(a)(5). The conclusion would be the same whether the compensation reduction was mandatory or elective. The conclusion would also be the same if the employer originally provided free parking to employees and then upon implementing the payroll arrangement purported to impose a charge on employees for parking. *See also*, Rev. Rul. 2002–3, 2002–1 C.B. 316, which holds that a purported reimbursement of health insurance premiums paid by the employer, and not by employees, is not excludable from the gross income of employees under §§ 106(a) and 105(b).

Because the "reimbursement" payments were not reimbursements of expenses incurred by A for parking, it was unreasonable for X to believe at the time the "reimbursements" were paid to A that A would be able to exclude the payments from gross income under § 132(a)(5). Thus, the "reimbursement" payments are not excluded from wages for FICA, FUTA, or federal income tax withholding purposes under §§ 3121(a)(20), 3306(b)(16), or 3401(a)(19), respectively.

## HOLDING

The exclusion from gross income under § 132(a)(5) does not apply to the payments characterized by the employer as "reimbursements." Employee A has not incurred an expense for parking for which there can be a reimbursement. Accordingly, amounts that Employer X pays to Employee A purportedly as reimbursements are included in Employee A's gross income and are wages subject to employment taxes under §§ 3121(a), 3306(b), and 3401(a). This is the outcome whether or not the amounts of Employer X's payments are calculated to provide Employee A with the same net pay A received prior to the implementation of the payroll arrangement.

In addition, this ruling applies to arrangements with respect to benefits other than parking where: (1) an employee's salary (and gross income) is reduced in return for a non-taxable benefit, and (2) the employer "reimburses" the employee for some or all of the cost of the non-taxable benefit and excludes the reimbursement from the employee's salary (and gross income) even though that cost was paid by the employer and not the employee.

## DRAFTING INFORMATION

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