TCJA for Nonprofits – One Year Later

The webinar will begin in a few moments

NOTE: Participants will receive an email within 48 hours with a link to the slide deck and recording.

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To qualify for CPE, you must:

- Use a personal computer (no smartphones) and log in with your own information and unique URL
- Be logged into our online software for at least 50 consecutive minutes within the scheduled time frame of the webinar
- Actively respond to at least 75% of the polling questions
- Complete evaluation survey at the end of the webinar

Based on the Board of Accountancy Requirements, Armanino is not a NASBA certified provider

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Learning Objectives

- **Review** the impact of the TCJA on nonprofit organizations
- **Discuss** examples specific to parking and transportation benefits for nonprofit employees
- **Evaluate** next steps for organizations in 2019

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Today’s Presenters

Any questions regarding Armanino or the content of this presentation should be directed to:

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TCJA’s impact on nonprofit organizations

Several changes to the code that affect nonprofits and that generate new filing requirements

- New filing requirements for “taxable expenditures”
- Changes to Form 990-T
- State impact – which states conform to which portions?

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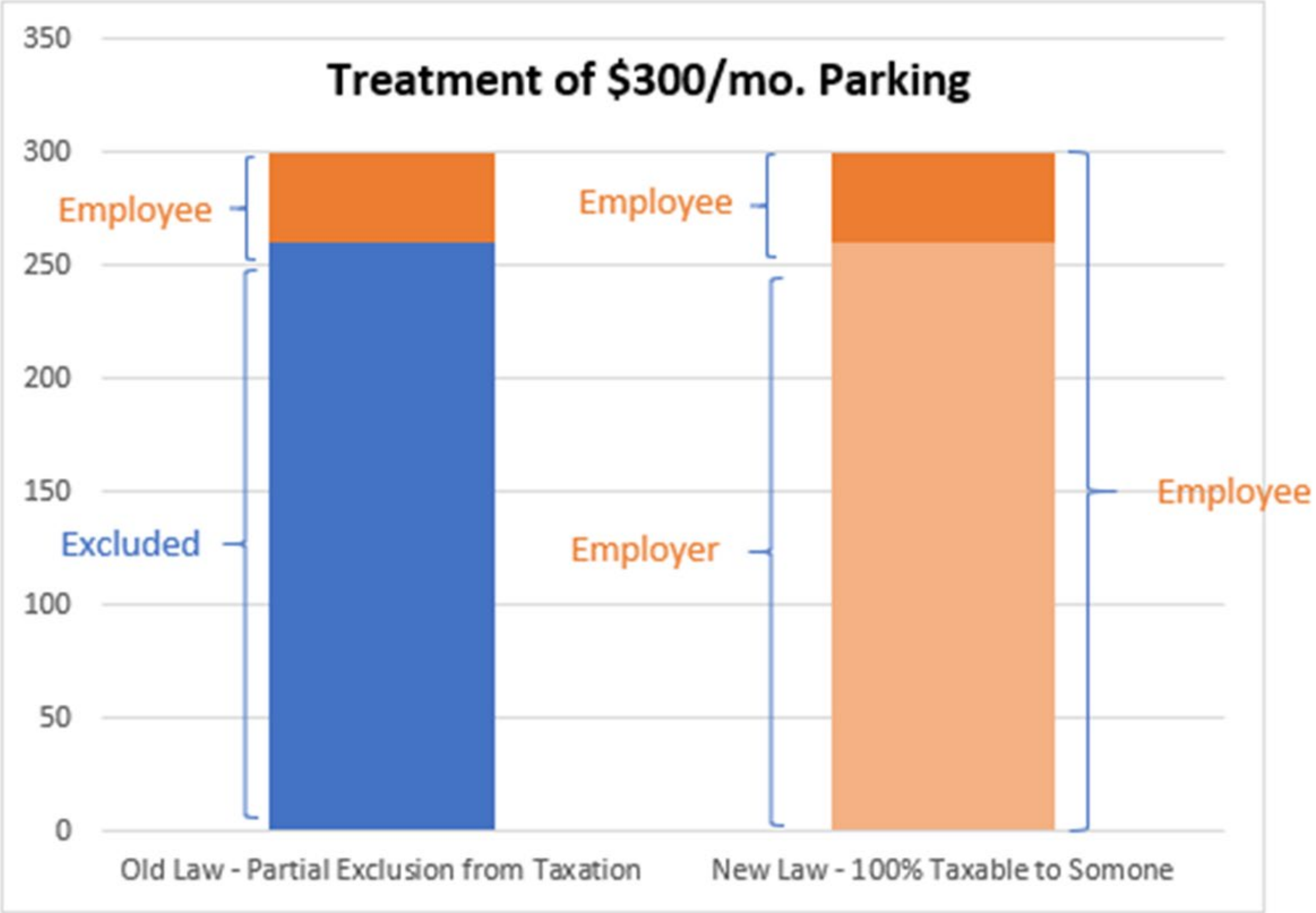
Major Changes to Nonprofit Reporting Due to TCJA

AGENDA

- Excess compensation
- Excess parachute payments
- No more advance refunding of tax-exempt bonds
- Section 529 plan funds may be used for K-12 tuition expenses
- Siloing of UBTI activities (Section 512(a)(6))
- Changes to NOL rules
- **Parking & Commute benefits tax** (Section 512(a)(7))

Employee Can Still Be Exempt from $260 per month, but Employer Must Now Pay



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Tax on Employee Parking & Commute Expenses

Exempt orgs must add to their UBTI the amounts spent on qualified transportation fringe (QTF) benefits and qualified parking

- IRC Section 512(a)(7) (with reference to Section 274)
- QTF is excludable from employee income up to $260/mo (2018) - $265/mo for 2019
  - Any amount in excess must be included in employee wages
  - Any amount the employee doesn't pay tax on, the employer must pay tax on
- Qualified parking is also excludable from employee income up to the same limits
  - We originally thought owned parking lots would not be subject to this, because it is not generally considered an employee benefit
  - Notice 2018-99 indicates that maintenance costs for owned parking lots are also subject to the tax
- Qualified bicycle commute reimbursements ($20/mo) are now taxable

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Notice 2018-99 Parking Tax Calculation

Depends on the parking lot arrangement

- Scope – any parking provided to employees at work
  - Employer-owned parking lots
  - Parking included in lease & not separately stated
  - Leased parking lots and spaces
  - Beginning Jan 1, 2018 for all tax years

- General principles –
  - Focus on normal business hours (not 24 hours per day)
  - Spots that are typically empty = non-employee
  - May remove signage or barriers by Mar 31, 2019 it will be retroactive back to 1/1/18 when the change became effective

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IRS' Suggested Four-Step Process (Notice 2018-99)

- Step 1 – Calculate the disallowance for reserved employee parking (taxable)
- Step 2 – Calculate the primary use of remaining area: employee or non-employee
  - 50%+ actually used by non-employees, entire area is non-taxable
  - 50%+ actually used by employees, allocate between emp/non-emp use
    - Number of spots, number of employees, hours of use, etc.
  - If usage varies, estimate using any "reasonable" method - documentation
- Step 3 – Calculate the exclusion for reserved non-employee parking
- Step 4 – Determine remaining use & allocable expenses

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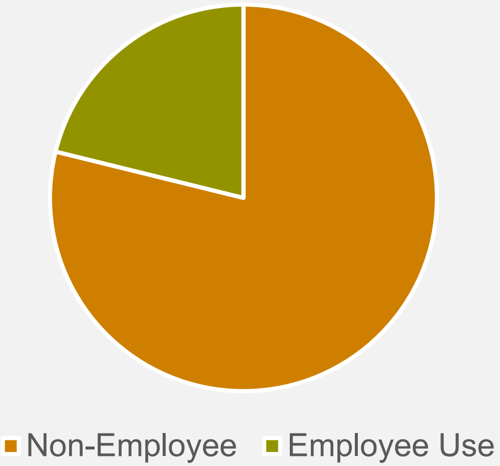
Example 1: Museum Leases – No Specific Rate for Parking

- $20,000 in CAM allocated to organization each year; estimated $10,000 related to parking
- 500 spots
- 50 reserved for management
- ~100 employees in non-reserved spots

1. Reserved spots: 50/500 x $10,000 = $1,000
2. Primary use of others: 350/450 = 78%

No need for remaining steps. If no other UBTI; should still file because total =$1,000, but no tax due



When no employee reserved parking and non-employee use is >50%, entire cost is deductible.

Example 2: Social Services Organization Leases – Reserved & Unreserved

- 10 reserved spots at $100/month – 8 used by employees; two reserved for visitors
- Access to 90 spaces daily, for which visitors must pay
- Parking lot open to the public at nights and weekends; public pays
- $20,000 in CAM allocated to organization each year; estimated $10,000 related to parking

Number of spots		8
Rate per month	$	100
		12
Yearly cost	$	9,600
Less: exclusion amount		(1,000)
Taxable amount		8,600
Tax rate		21%
Tax due	$	1,806

No employee use of other spaces, so no calculation required

Will need to file 990-T and will incur tax of $1,806 if no other unrelated activities.

Example 3: Health Clinic Leases Full Building With Lot

- No reserved spots for employees
- Costs related to parking $15,000 annually
- 200 spots in lot
- ~120 employees daily
- 10 reserved accessible spots

Total spots			200	
Less: reserved for non-employees			(10)	
Total potentially-taxable spots			190	A
Average daily employee use			120	B
Percentage of costs taxable	B ÷ A		63.2%	C
Yearly cost		$	15,000	
Less: reserved for non-employees			(750)	
			14,250	D
Allocable to employees	C x D		9,000	
Less: exclusion amount			(1,000)	
Taxable amount			8,000	
Tax rate			21.0%	
Tax due		$	1,680	

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Office Leases Treat Parking in a lot of Different Ways

- Spaces paid directly to a third-party parking company
- Spaces with a per month rate
- Spaces included in leases but without a specific charge
- Common area maintenance (CAM) costs that include the cost of parking

What Documentation is Required?

- Any reasonable method is allowable
  - Guidance from IRS Notice 2018-99 will be considered reasonable
  - Not the only “reasonable” method
  - Document how the costs were allocated
  - Areas / items that are adjacent to parking lots may be allocated away
  - Maintain records for the length of the statute of limitations
    - Federal: 3 years from date of filing or original due date, whichever is earlier

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What Costs Are Taxable?

Once the total % of employee use is determined, apply it to the total of these costs:

- Utilities
- Insurance / interest
- Maintenance / repair
- Leaf, trash, snow removal
- Parking lot attendants / valet
- Security
- Property taxes
- Rent or lease payments for the parking spaces or parking lot
- **NOT DEPRECIATION**

Example 4: Affordable Housing Developer Leases Office Space That Comes With Parking


- 6 parking spots included in lease, all used by employees
- No specific rate set for the parking and no CAM
- Lease is $10,000 per month
- There are 500 spots in the lot, of which 200 are reserved for the various tenants and believed to be used by employees
- There are two lot attendants, because the lot has stacked parking and cars must be moved
- Lot is cleaned once a month

# of spaces in the lot		500	A
# reserved for all tenants' employees		180	B
B ÷ A		36%	
# of spots organization has		6	C
% of all employee use (C ÷ B)		3.3%	D
Parking attendant (2 @ $15/hr x 22 days)	$	5,280	
Monthly cleaning		400	
Estimated repairs		100	
		5,780	
Annual cost		69,360	
Percentage allocated to reserved spots		36%	
		24,970	
Percentage allocated to organization		3.3%	
	$	832	

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Are Expenses Allowed Against This Addition to UBTI?

Form 990-T does not allow for expenses against 512(a)(7) taxable expenditures

- Difference between for-profit and nonprofit entities
- Suggest providing comment to the IRS on this issue
- Suggest calling / writing your Congresspeople – there is some effort in Congress to repeal

Reporting Details

- Tax rates:
  - Blended rate for orgs with fiscal years beginning in 2017
  - Flat 21% rate for 2018 and later tax years for corporations
  - Trusts are still taxed at graduated rates
- Automatic relief from underpayment penalties for first-time filers (Notice 2018-100)
- What if a client chooses not to file? Impact on audit?

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Reporting and Payment

<u>Report on Form 990-T</u>

- New schedules to allow for siloing rules
- Fringe benefits appears at the end
- $1,000 specific deduction

<u>Payment requirements</u>

- Once you must make a payment of $500+, EFTPS is required
- www.eftps.gov
- 10 business days from online sign-up to ability to schedule online payments (48 hours to schedule phone payments)
- Quarterly estimate payments required if total amount due is $1,000+

State Conformity

- California has not (yet?) conformed with any of the TCJA changes
  - No parking tax, no change to Form 109 filing requirements
  - Penalty on withdrawal of 529 plan funds to pay for K-12 tuition – 3%
- Texas – no tax on UBTI
- New York – decoupled from federal conformity on the parking tax

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"James Lankford (R-Okla.) and Chris Coons (D-Del.) introduced the legislation in the U.S. Senate. Mark Walker (R-N.C.) and Tom Suozzi (D-N.Y.) introduced the companion bill in the House of Representatives. U.S. Representatives Randy Weber (R-Texas), Doug Lamborn (R-Colo.), Jeff Duncan (R-S.C.), Matt Gaetz (R-Fla.), and Jody Hice (R-Ga.) are also co-sponsors on the House of Representatives version."

Article in last Thursday's *Nonprofit Times*

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FAQs


- We already filed our 2017 990-T back in November prior to the IRS guidance. Do we have to amend?
- Are volunteers “employees” for the purpose of the parking tax?
- If our signage says “for our company’s use only,” does that indicate employee or customer use?
- Do we have to make quarterly estimated payments?
- How do we pay this tax? Can we pay online?
- What other deductions can we find against our UBTI?
  - Consider charitable contributions – 10% limitation
  - Review expense allocations each year

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Siloing of UBTI Revenue Streams

Income/loss from different UBTI activities may not offset each other, including for NOL purposes

- Section 512(a)(6)
- Effective for tax years 2018 and later (beginning after Dec 31, 2017)
- Notice 2018-67
  - Suggests using NAICS codes or maybe the first three digits
  - States that we may group all partnership passthrough UBTI into one activity (passive investment activities may be treated as one trade or business)
    - De minimus = 2% or less ownership
    - Lack of control = 20% or less ownership, no actual control

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Other Common Sources of UBTI

- Advertising of any kind
- Passthrough UBTI on investment partnership K-1s
- Rental of debt-financed property (exception for schools)
- Private business use of tax-exempt bond financed property
- Rental of facilities that includes significant services
- Rental of property other than real estate (personal property)

Changes to NOL Rules

- Section 172(a) limits Net Operating Loss carryovers to 80% of taxable income
  - NOLs generated in one UBTI activity will only be applicable to that activity
  - Also subject to the 80% limitation
- Section 172(b) eliminates the two-year carryback provision
  - All NOLs will carry forward 20 years
- Effective for tax years beginning after Dec 31, 2017

Orgs will be paying tax on UBTI activities with net income in future years, even if they have net operating losses

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Net Operating Loss Rules


- NOL ordering rules –
  - Use 2018 & later specific NOLs first, subject to 80% limitation
  - Then use 2017 all-purpose NOLs
- 2017 and prior NOLs may be used against any activity, including Section 512(a)(7) parking and commute costs
  - No 80% limitation on 2017 and prior NOLs

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Excess Compensation

- IRC Section 4960 – excise tax imposed on nonprofit employer
- Effective for tax years <u>beginning</u> after December 31, 2017
- Compensation in excess of $1m paid to a "covered employee"
  - Wages, less Roth contributions, plus 457(f) amounts vested
  - Five highest compensated employees in any year after 2016
- Nonprofit corporations = 21% tax rate
- Exception for medical & veterinary employees

Excess Parachute Payments

- IRC Section 4960 – excise tax imposed on nonprofit employer
- Effective for tax years beginning after December 31, 2017
- Severance payments that exceed 3x the employee's average comp over the previous five years (the base amount)
- The entire amount in excess of the base amount is taxable
- Nonprofit corporations = 21% tax rate

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Tax-Exempt Bond Advance Refunding


- Changes to IRC Section 149(d) eliminate tax-exempt treatment of advance refunding bonds
  - Refunding = refinancing
  - Advance refunding vs. Current refunding
  - Eliminates an org's ability to receive refinancing funds in advance of paying off the original debt
  - In line with current strict enforcement of use of tax-exempt bond proceeds & facilities financed with tax-exempt bonds

Section 529 Plan Usage for K-12 Tuition


- IRC Section 529(c)(7) amended
  - Special tax-advantaged savings programs
  - Some states allow pre-tax contributions or other tax incentives (not CA)
  - Originally only usable for qualified higher education expenses
  - Amended code allows up to $10,000 per student per year to be withdrawn for K-12 tuition expenses
  - State conformity issues (CA did not conform)

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