January 9, 2015

Retroactive Transit Parity Guidance

At the end of 2014, Congress increased the tax break for employer-provided transit benefits from $130/month to $250/month to match the tax break provided for parking. The catch was that the increase applied retroactively to 2014 (and does not extend to 2015, at least not yet), but employees would have already been taxed on benefits in excess of $130/month. This week the IRS published guidance for employers in Notice 2015-2 that is similar to the guidance issued in early 2013 after a similar end-of-year change to taxable transit benefits. As can be expected whenever a retroactive change affects an employee's taxable income, the employer bears the administrative burden if its employees were provided transit passes in excess of $130 on an after-tax basis. The IRS Notice provides a process for adjusting or correcting Form 941 and explains the employer's obligation to issue a correct Form W-2.

Form 941: The IRS has provided a special administrative process for employers who have not yet filed their fourth quarter Form 941 (in lieu of filing Form 941-X and Forms W-2c). To take advantage of this procedure, the employer must repay or reimburse employees for the over-collected FICA tax, and any additional Medicare tax, for all four quarters of 2014 before filing the fourth quarter Form 941. When completing this fourth quarter Form, the employer can reduce the reported wages on Lines 2, 5c and 5d by the excess transit benefits for all four quarters of 2014. If the employer has already filed a fourth quarter Form 941 or has not repaid employees for the over-collected taxes, it instead must follow the normal procedures for correction, including filing Form 941-X.

Forms W-2: If an employer has not yet furnished Forms W-2 to its employees, it must take into account the retroactive increase in completing boxes 1, 3 and 5. Boxes 4 and 6 must be reduced if the employer has repaid or reimbursed the employee for over-collected taxes. Box 2 must reflect the actual amount of federal income tax that was withheld. Special rules are provided for employers that repay the over-collected amounts after furnishing Forms W-2 to the employees but before filing them with the SSA. Forms W-2c must be filed if the W-2s have already been provided to the SSA.