DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF THE CHIEF COUNSEL

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CONEX-135462-09

The Honorable Carolyn McCarthy
Member, U.S. House of Representatives
300 Garden City Plaza, Suite 200
Garden City, NY 11530

Attention:

Dear Congresswoman McCarthy:

This letter responds to your inquiry dated July 30, 2009, on behalf of your constituent, . asked why employees who terminate employment cannot receive any of the balance remaining on their transit reimbursement accounts as taxable compensation.

The law excludes qualified transportation fringes from gross income (section 132(a)(5) of the Internal Revenue code (the Code)). The term "qualified transportation fringe" refers to any of the following that an employer provides to an employee:

- Transportation in a commuter highway vehicle in connection with travel between the employee's residence and place of employment
- Any transit pass
- Qualified parking

Qualified transportation fringe also includes cash reimbursement for any of the above mentioned benefits (section 132(f)(3) of the Code).

The Income Tax Regulations (the Regulations) allow an employer to provide qualified transportation fringes to employees either as a benefit provided in addition to an employee's regular compensation or under a compensation reduction agreement (section 1.132-9(b) Q/A-11). In these agreements, an employee agrees to contribute pre-tax earnings into an account that he or she can use to pay for qualified transportation fringes. Once the employee elects to convert a portion of pre-tax earnings into a tax-free qualified transportation fringe benefit, the treatment is not reversible (section 1.132-9(b) Q/A-14(d)).

Participation in a compensation reduction agreement for the provision of qualified transportation fringe benefits is completely voluntary. However, once the employee has agreed to reduce his or her compensation to pay for commuting expenses, the employee is no longer entitled to receive that compensation. Instead, the employee is entitled to receive nontaxable qualified transportation fringe benefits.

If an employee has a choice between cash compensation or an employer-provided benefit, the law treats the benefit as provided directly by the employer rather than purchased by the employee with the amount of the compensation reduction. This treatment allows the employee to exclude the value of the benefit from income for tax purposes. If the employee could choose to receive the benefits at any time in the form of cash rather than qualified transportation fringe benefits, then the law would treat the employee as constructively receiving the benefits as compensation and tax the employee on the full value.

I hope this information is helpful. If I can assist you further, please contact me at ( ) .

Sincerely,

Lynne Camillo
Branch Chief, Employment Tax Branch 2
(Exempt Organizations/Employment Tax/Government Entities)
(Tax Exempt & Government Entities)