GROOM LAW GROUP

MEMORANDUM TO CLIENTS

December 23, 2009

RE: **Qualified Transportation Plans: IRS Delays Effective Date Again for Mass Transit Electronic Payment Cards**

The Internal Revenue Service ("IRS") recently issued Notice 2009-95 once again delaying the effective date for its 2006 guidance (Revenue Ruling 2006-57) regarding the use of "smartcards" and other types of electronic payment cards for mass transit expenses under qualified transportation plans under Section 132 of the Internal Revenue Code ("Code"). The effective date for Revenue Ruling 2006-57 (originally effective January 1, 2008 and twice delayed previously) is now January 1, 2011. Employers can, however, rely on the Ruling in advance of the effective date. The IRS explained in Notice 2009-95 that the effective date has been pushed back again because certain transit systems need additional time to complete the process of adapting their technology to achieve compatibility with the requirements for vouchers.

The delayed effective date is good news for third party administrators ("TPAs") and employers offering qualified transportation plans with electronic payment cards. The delay gives the transit systems another year to come into compliance with the rules. Employers and TPAs should take this opportunity to review the rules regarding electronic payment cards for qualified transportation plans and determine whether their cards will be in compliance when the rules finally do become effective. The rules are discussed briefly below.

Revenue Ruling 2006-57 describes the situations in which an electronic payment card may be used to make tax free payments for eligible transportation expenses under a qualified transportation plan. The Ruling addresses payment of eligible transportation expenses with a "smartcard" (a card with an embedded information "chip"), a terminal-restricted debit card (a card that may be used at terminals that sell only fare media for a particular transit system), and a merchant category code ("MCC") restricted debit card (a card that may only be used at merchants with a MCC indicating that they sell fare media). The Ruling indicates that payments made with a smartcard and/or a terminal-restricted debit card are generally excluded from income and considered to be "vouchers", as described below. Because these cards are vouchers, there are **no substantiation requirements** for mass transit expenses if an employer provides smartcards or terminal-restricted debit cards to employees.

MCC-restricted debit cards, on the other hand, may constitute a cash reimbursement arrangement – but not a voucher – if certain requirements are met. As a result, MCC-restricted debit cards can be used only if a voucher is not "readily available", as defined in the regulations under Code Section 132. Additionally, the Ruling makes clear that the MCC filter coupled with an employee certification alone does not provide an adequate level of substantiation. Under IRS rules, there are only a few areas in the country in which a voucher is not "readily available". But, one notable area where vouchers are not readily available (thus permitting MCC-restricted debit cards) is the New York metropolitan area, which has several million people commuting via mass transit on a daily basis.

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Notably, the Ruling relates only to the use of electronic payment cards to purchase transit passes. The guidance does not specifically approve electronic payment cards used for parking expenses. Parking expenses may be reimbursable under a program similar to the MCC-restricted debit card arrangement, but there is no specific guidance on that issue. Finally, because the smartcard, terminal-restricted debit card and the MCC-restricted debit card each are limited to expenses for "fare media" (i.e., transit expenses), any parking expenses should either be loaded onto a separate "purse" on any card that is also used for transit expenses or onto a separate card.

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