

IRS Safe Harbor

Elaine Vatakis
Irvine Campus Housing Authority

Andy Lachman
University of Hawaii at Manoa



Safe Harbor Definition

A safe harbor is a provision in a law or regulation that affords protection from liability or penalty under specific situations or if certain conditions are met.

(Business Dictionary.com)

Today

- Campus Lodging
- Tax-Exempt Bond-Financed Facilities

Qualified Campus Lodging

- Lodging furnished to the employee by an educational institution for use as a home
- The lodging must be located on or near a campus of the educational institution or an academic health center

Campus Lodging Tax Law

The value of qualified campus lodging furnished to an employee of an educational institution is not taxable to the employee if the rent is adequate.

IRC §119(d)

Significance

To prevent residents from imputed
tax consequences

Adequate Rent

The amount of rent the employee pays for the year is considered “adequate” if it is at least equal to the lesser of:

1. The gross aggregate rental rates must be 5% or greater of the appraised value of the qualified campus lodging
2. The average of rentals paid by individuals (other than employees or students) for comparable lodging held for rent by the educational institution

Example

Professor T rents a house from a university. The house is appraised at \$180,000. Similar properties rent for \$1,400 per month. Rent per month for the professor is \$600.

Example

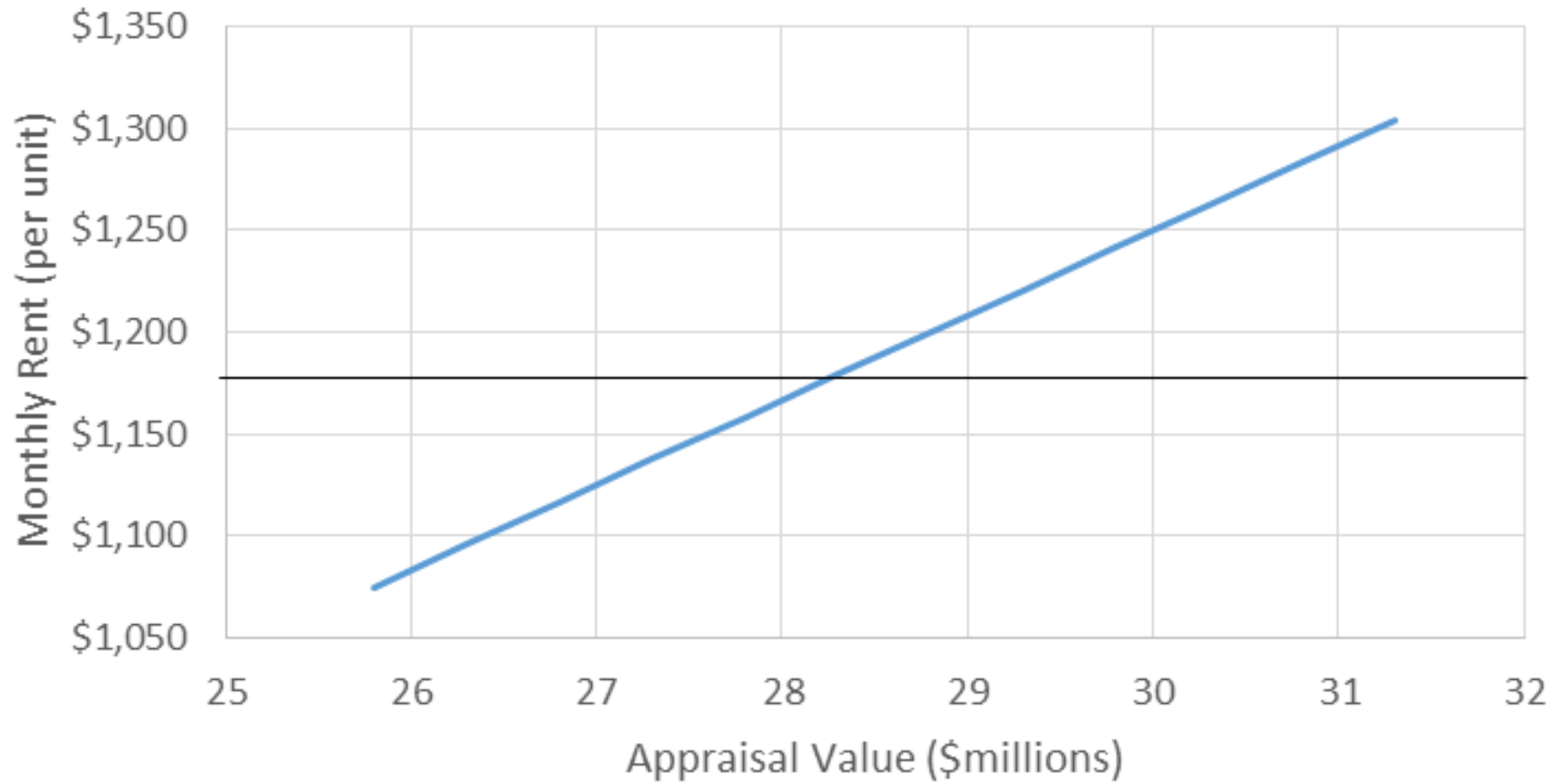
- (1) 5% of \$180,000 /12 = \$750 per month
- (2) AVG comp rent is \$1,400 per month

- \$750 - \$600 = \$150 per month
- Professor T must include \$1,800 per year in gross income

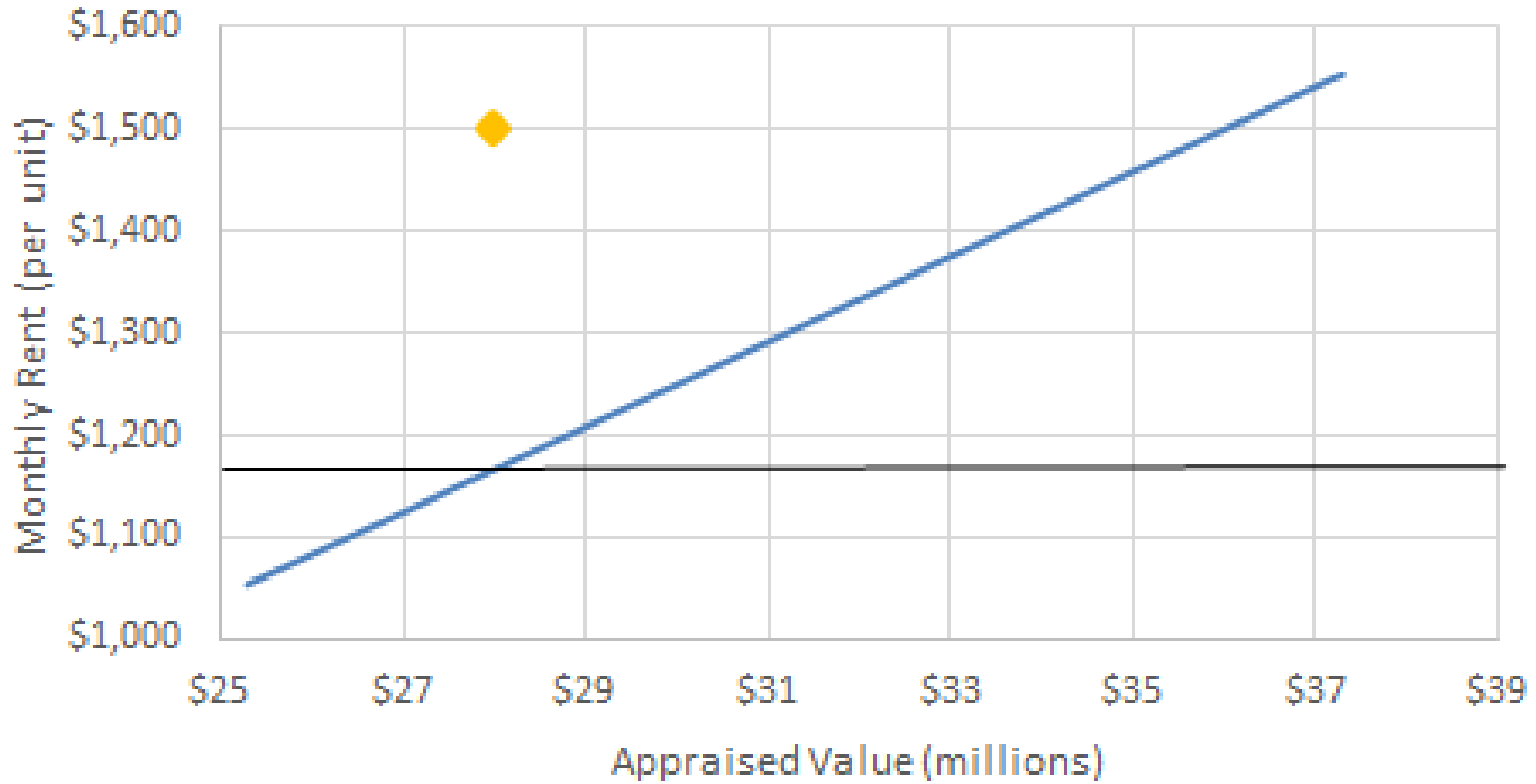
ICHA's Santiago Community

- Appraised Value: \$28,300,000 annually
- 5% * (Appraised Value) = \$1,415,000 annually
- \$14,150 per unit annually
- \$1,179 per unit monthly

Value vs Rent



Adequate Rent Threshold



UH's Waahila Apartments

- Appraised Value: \$16,250,000
- $5\% * (\text{Appraised Value}) = \$812,500$ annually
- \$12,310 per unit annually
- \$1,025 per unit monthly
- Actual avg monthly rent per unit = \$940.46

UH's Waahila Apartments

Taxable Benefit

- Avg taxable benefit per month = \$84.54
- This increase resident's Federal, State and FICA taxable income.
 - Reported on the employee's W-2 as wages-in-kind.
 - Withholdings for taxable income.

Appraisal Requirements/Best Practice

- To comply with the “1986 Act Conference Committee Report”, the appraisal must be made by a qualified appraiser.
- Consistent appraisals on an annual basis, preferably prior to the beginning of the next tax year, is ideal in maintaining safe harbor guidelines

Tax-Exempt Bond-Financed Facilities

One popular source of funding for capital improvements at institutions of higher education is tax-exempt bonds. These bonds have certain requirements established by the IRS to maintain their tax exempt status.

Significance

To adhere to IRS requirements for tax exempt bonds, Universities (and other entities) must only engage non-exempt providers (i.e. private businesses) under certain safe harbor conditions.

Impacts

These requirements have impacted:

- 1) How contracts are structured
- 2) Decisions on how to finance capital improvement projects

Best Practice

- Consider types of operations prior to the issuance of tax exempt bonds.
 - Management fee contracts versus percentage of revenue contracts or leases.
 - Self Operations.
- Annually review contracts in facilities that were built using tax exempt bond financing.
 - Ensure less than 5% of Square Feet is used for private use.

Questions?

