

## FRINGE BENEFITS for School Districts

When Is a Gift Not a Gift?

### RULES and BEST PRACTICES on TAXABLE COMPENSATION

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#### Overview

- Business Expenses
- Fringe Benefits
- Trends and Tips

#### Business Expenses – Employer IRC §162

- Business expense is an ordinary and necessary expense incurred or paid by the employer during the tax year for the purpose of carrying on the trade or business.
- Example – employer-sponsored attendance at employee training conference.
- The employer can deduct a qualified business expense from its income. IRC §162

Business expense deductions **do not** apply to school districts or other government employers because they are not subject to federal income tax.

#### Business Expenses – Employee §162

- Reimbursement by the employer for costs incurred by an employee for the employer's ordinary and necessary business expenses are excluded from the employee's income if they are made under an **accountable plan**.
- An accountable plan is not a benefit plan and does not require a written plan document.
- An accountable plan requires
  - A business connection – the expense must qualify as a business expense to the employer and qualify as an unreimbursed business expense deduction for the employee, if not paid by the employer.
  - Substantiation – amount, date, time, place and business purpose.
  - Excess returned in a reasonable period of time.
- Per diems must be administered under an accountable plan.
- Examples are work clothes, safety equipment, mileage allowance.

#### Fringe Benefits

- A **fringe benefit** is a form of compensation for the performance of services -- including property, services, cash or cash equivalent -- in addition to stated wages.
- All income is taxable, unless a **specific exclusion** applies. IRC § 61

## Fringe Benefits – Levels of Taxation

- The Internal Revenue Code (IRC) may provide that a fringe benefit is
  - Taxable – value is includable in the employee’s gross income, i.e., not excluded from taxation under any IRC section.
  - Nontaxable – value is excluded from wages by a specific IRC section. For example, the value of qualified health plan benefits.
  - Partially taxable – value is excluded up to certain limits as with an educational assistance program.
  - Tax-deferred – value of the benefit is not taxable when it is received but is subject to tax later as with 403(b) plan contributions.

## Fringe Benefit Overview

- Health Insurance IRC § 105 and 106
- Meals and Lodging IRC § 119
- Cafeteria Plans IRC § 125
- Educational Assistance Program IRC § 127
- Dependent Care Assistance IRC § 129
- No additional cost service IRC § 132(b)
- Qualified employee discount IRC § 132(c)
- Working Condition Fringe Benefits IRC § 132(d)
- De Minimis Benefits IRC § 132(e)
- Qualified transportation fringe IRC § 132(f)
- Awards Treasury Regulation § 1.274-8
- On-premises athletic facilities IRC § 132(j)(4)
- Qualified retirement planning services IRC § 132(m)
- Adoption assistance programs IRC § 137

## Trends

- Gift and Value Cards
- “Millennial” Benefits
- Retirement Benefits

## De minimis fringe benefits – IRC § 132(e)

- A de minimis fringe benefit is a property or service provided by the employer that has so little value it would be impractical to account for it.
- Items are generally de minimis by specific exclusion, everything else is taxable income to the employee. Not a catch-all.
- There is no minimum value for a de minimis benefit.
- Cash or cash equivalent is never a de minimis benefit.

## De minimis fringe benefits – IRC §132(e)

- Examples of de minimis benefits
  - Personal use of employer-provided cell phone
  - Occasional use of the employer copy machine
  - Holiday or birthday gifts that are not cash with a low value
  - Flowers provided for a specific occasion
  - Occasional parties for employees
  - Occasional tickets to theater or sports events
  - Low value snacks
- Examples of items that are not de minimis
  - Gift cards of any amount
  - Season tickets
  - YMCA membership
  - Regular snacks
  - Meals

## Examples – characterize these examples as taxable or not taxable

- Holiday “Chamber Bucks” cards.
- Staples gift card from the Band Boosters to the jazz band director at year end.
- Coffee and donuts in the break room when the Superintendent has time to stop at Dunkin Donuts.
- Sub sandwiches in the staff lunchroom before every Board of Education meeting.
- \$15 “cash back” from Scholastic Books to teachers who complete an on-line survey.
- \$15 stipend from the University of Pennsylvania to teachers who complete a survey on curriculum.
- Reimbursement to Special Ed teachers for cost of lunch at “Students with Exceptional Needs” update at UW-Whitewater.
- Nike athletic gear provided by Nike at no cost to athletic department staff.
- Massages at the school campus as a Christmas gift from the District

## Is a Gift Card Taxable?

- Gift Card as a reward for Wellness Program?
- Is there a minimum gift card value to be taxable?
- What if the Gift card comes for a business and is awarded to a District employee?

## Meals and Snacks IRC §119

- The value of any meal furnished by an employer to the employee is excluded from income if the meal is furnished on the employer premises for the convenience of the employer.
  - Meals furnished to allow employees to be available to respond to emergencies (e.g., certain hospital staff)
  - Employee’s meal period is restricted to 30-45 minutes due to work requirements and the employee cannot obtain a proper meal during that time period.

- Inadequate eating facilities and restaurants within a reasonable distance from the employee's work location. However, the IRS will evaluate meal delivery options. See, IRS Technical Advice Memorandum 201903017, 01/18/2019.

#### Meals

- IRS Technical Advice Memorandum 201903017, 01/18/2019
- Facts – Employer furnished all meals to all employees without substantiation of the business reason for the meals.

#### IRS Findings:

- 1) Cannot substantiate after the fact (during the audit).
- 2) Protecting the employer's confidential information was not an adequate reason when some employees did leave the campus for meals, the employer did not have a policy defining confidential information.
- 3) Enhancing innovation was not an adequate reason when the employer did not have a policy regarding innovation that would have required employer-provided meals on site.

#### Meals

#### IRS Findings (cont.)

- 4) Improving employee wellness with employer-provided healthy meals was not supported by any policy describing a business reason related to the employer's business.
- 5) Ensuring employees are available for emergencies must be demonstrated with examples of actual emergencies for which the employee had to be available and not the expectation of a possible emergency.

#### Meals

- Examples – would these meals have to be included in income:
  - Teachers assigned to playground/cafeteria duty during student lunch periods with no teacher lunch period.
  - School Resource Officer who walks the cafeteria during every student lunch period.
  - Principal is "on call" to intervene during every student lunch period.
  - District makes sub sandwiches available in the break room for staff required to attend evening Board of Education meetings.
  - Meals for Board members?

#### Snacks – IRC 119 and 132

- Snacks that are provided continuously in small, low value portions (e.g., candy bowl) are excludable from employee income as a *de minimis* fringe benefit.
- The value of snacks, even when combined, cannot be excluded from employee income as a meal provided for the convenience of the employer.

- Substantial snacks provided regularly to employees unrelated to a specific business purpose are not excludable from employee income.

#### Cafeteria Plans – IRC §125

- Non-cafeteria benefit plans are generally provided and paid for by the employer. Employers cannot offer a cash payment in lieu of participation. Ex. 403(b) plan is ‘cash’ and not eligible as Section 125 option.
- Participation in certain benefit plans can be optional without jeopardizing the tax-exempt status of the benefit to the employee. Choice between health benefits or cash.
- Optional benefits are provided in a Section 125/cafeteria plan. Employees can participate in one or more of the cafeteria plan benefits by paying the cost of the benefit through a *salary reduction agreement*.
- Employees who choose not to participate will not experience the salary reduction. The related income is taxable.

#### Cafeteria Plans – IRC §125

- Benefits allowed in a cafeteria plan
  - Accident and health
  - Adoption assistance
  - Dependent care assistance
  - Group term life insurance
  - Flexible Spending Account
  - Health Savings Accounts (HSA)
- Not allowed in a cafeteria plan
  - De minimis benefits
  - Educational assistance
  - Transportation (commuting) benefits
  - Tuition reduction
  - Working condition benefits
- Redirected dollars are considered Employer dollars

#### Educational Reimbursement – IRC §§132(d) and 127

- Educational expenses can be paid by the employer directly or reimbursed to the employee as
  - a working condition fringe benefit (132(d) or
  - through a Qualified Educational Assistance Program (127).

#### Education as a Working Condition Fringe Benefit – IRC §132(d)

- Education must be job-related.
  - Maintain or improve job skills
  - Be expressly required by the employer or by law.
  - Ex. Work toward an advanced degree necessary to retain the job or pay level.
- Employer is not required to have a written plan.
- There is no dollar limit.

- The employer can discriminate in favor of highly-compensated employees.
- The course must not
  - Be needed to meet the minimum job requirements
  - Qualify the employee for a new trade or business
- Employer must substantiate cash reimbursements
  - The expense qualifies as a working condition fringe benefit
  - The payment was actually used for the educational expense.
  - Excess payment was repaid.

#### Qualified Educational Assistance Program – IRC §127

- Employer may exclude up to \$5,250 from employee wages for costs associated with undergraduate or graduate education.
- Requires a written plan.
- Cannot be offered as a cafeteria plan benefit.
- Cannot discriminate in favor of highly compensated employees.
- The education is not required to be job-related, but it can be job-related.

#### Educational Expenses

- Examples – Characterize these educational expenses as taxable or not taxable
  - Karen is the school secretary. She wants to take an undergraduate psychology course at UW-Oshkosh.
  - Adam is a middle school social studies teacher. He wants to get a license as an athletic trainer to work with the high school soccer team.
  - D’Nai teaches high school math. She wants to get her Ed.D. with the goal of working in administration.
  - Maria is working as a special education teacher on a temporary license while completing her undergraduate degree in special education. She has a job offer waiting at her school.
  - The School District of Central Wisconsin reimburses Joseph for the cost of classes he took to get a maintenance technician certificate but did not require substantiation of the tuition payment.

#### Dependent Care Assistance – IRC §129

- Up to \$5,000 in employee dependent care expense can be excluded from annual income.
- Expense is paid through a salary reduction agreement.
- Can be offered as a pretax benefit via the Section 125/cafeteria plan.
- Requires a written plan and substantiation.

#### On site daycare

- Example - Set up an on-site daycare facility that District staff can use.
- District provides 0-3 year daycare for families with children enrolled in the District.
- District allows staff to use the daycare on a drop-in basis at no cost to the employee.

- District provides a \$5,000 Dependent Care FSA.
- Mark, a District employee, has \$4,000 deducted from his salary for his Dependent Care FSA. He also uses the District daycare once/week when his wife works an early shift. The fair market value of the daycare use annually is \$1,750.
  - For use of the employer's daycare, the employer includes which amount on the employee's W-2?
    - \$1750
    - \$0
    - \$1000

#### Working Condition Fringe Benefits – IRC §132(d)

- Property and services provided by the employer to the employee so the employee can perform her/his job are not taxable to the employee.
- Ex. Use of District vehicle, District-provided cell phone, job-related education and licensing costs.
- Also includes cash reimbursements by the employer for pre-arranged business activities made under an accountable plan.
- Ex. Travel per diems, mileage reimbursement, lodging for job-related travel.
- Conditions for a working condition fringe benefit
  - Benefit must relate to the employer's business.
  - Employee would have been able to take a tax deduction if the employee paid the expense.
  - Business use is substantiated with records.
- Catch-all - Any expense can qualify if it meets the working condition fringe benefit criteria.

#### Transportation Benefit

- Employers may reimburse the employee's expenses for use of a personal vehicle for work purposes on a tax-exempt basis if the reimbursement is consistent with the accountable plan rules.
- Use of an employer-provided vehicle exclusively for business purposes is a working condition fringe benefit with no tax consequences to the employee.
- Mixed personal and business use of an employer-provided vehicle requires reporting the personal use as taxable income to the employee.
- De minimis exception applies to small personal detours (e.g., driving to lunch while out on business) and infrequent commuting of no more than one day per month.

Value the personal use of this company car

Use of the District jet

- Working condition fringe?
- De minimis?
- Transportation fringe?

Alaska bush plane

- Working condition fringe?
- De minimis?
- Transportation fringe

Thank you!

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