

Publication 15-B (2009), Employer's Tax Guide to Fringe Benefits

SECTION 1. Fringe Benefit Overview

A fringe benefit is a form of pay for the performance of services. For example, you provide an employee with a fringe benefit when you allow the employee to use a business vehicle to commute to and from work.

Performance of services. A person who performs services for you does not have to be your employee. A person may perform services for you as an independent contractor, partner, or director. Also, for fringe benefit purposes, treat a person who agrees not to perform services (such as under a covenant not to compete) as performing services.

Provider of benefit. You are the provider of a fringe benefit if it is provided for services performed for you. You may be the provider of the benefit even if it was actually furnished by another person. You are the provider of a fringe benefit your client or customer provides to your employee for services the employee performs for you.

Recipient of benefit. The person who performs services for you is the recipient of a fringe benefit provided for those services. That person may be the recipient even if the benefit is provided to someone who did not perform services for you. For example, your employee may be the recipient of a fringe benefit you provide to a member of the employee's family.

Are Fringe Benefits Taxable?

Any fringe benefit you provide is taxable and must be included in the recipient's pay unless the law specifically excludes it. Section 2 discusses the exclusions that apply to certain fringe benefits. Any benefit not excluded under the rules discussed in section 2 is taxable.

Including taxable benefits in pay. You must include in a recipient's pay the amount by which the value of a fringe benefit is more than the sum of the following amounts.

- Any amount the law excludes from pay.
- Any amount the recipient paid for the benefit.

The rules used to determine the value of a fringe benefit are discussed in section 3.

If the recipient of a taxable fringe benefit is your employee, the benefit is subject to employment taxes and must be reported on Form W-2, Wage and Tax Statement. However, you can use special rules to withhold, deposit, and report the employment taxes. These rules are discussed in section 4.

SECTION 2. Fringe Benefit Exclusion Rules

This section discusses the exclusion rules that apply to fringe benefits. These rules exclude all or part of the value of certain benefits from the recipient's pay.

The excluded benefits are not subject to federal income tax withholding. Also, in most cases, they are not subject to social security, Medicare, or federal unemployment (FUTA) tax and are not reported on Form W-2.

This section discusses the exclusion rules for the following fringe benefits.

- Accident and health benefits.
- Achievement awards.
- Adoption assistance.
- Athletic facilities.
- De minimis (minimal) benefits.
- Dependent care assistance.
- Educational assistance.
- Employee discounts.
- Employee stock options.
- Group-term life insurance coverage.
- Health savings accounts (HSAs).
- Lodging on your business premises.
- Meals.
- Moving expense reimbursements.
- No-additional-cost services.
- Retirement planning services.
- Transportation (commuting) benefits.
- Tuition reduction.
- Volunteer firefighter and emergency medical responder benefits.
- Working condition benefits.

See Table 2-1 on page 5 for an overview of the employment tax treatment of these benefits.

Table 2-1. Special Rules for Various Types of Fringe Benefits (For more information, see the full discussion in this section.)

Treatment Under Employment Taxes

| Type of Fringe Benefit | Income Tax Withholding | Social Security and Medicare | Federal Unemployment (FUTA) |
|------------------------------------|---|--|-----------------------------|
| Accident and health benefits | Exempt ^{1,2} , except for long-term care benefits provided through a flexible spending or similar arrangement. | Exempt, except for certain payments to S corporation employees who are 2% shareholders. | Exempt |
| Achievement awards | Exempt ¹ up to \$1,600 for qualified plan awards (\$400 for nonqualified awards). | | |
| Adoption assistance | Exempt ^{1,3} | Taxable | Taxable |
| Athletic facilities | Exempt if substantially all use during the calendar year is by employees, their spouses, and their dependent children and the facility is operated by the employer on premises owned or leased by the employer. | | |
| De minimis (minimal) benefits | Exempt | Exempt | Exempt |
| Dependent care assistance | Exempt ³ up to certain limits, \$5,000 (\$2,500 for married employee filing separate return). | | |
| Educational assistance | Exempt up to \$5,250 of benefits each year. (See <i>Educational Assistance</i> , later.) | | |
| Employee discounts | Exempt ³ up to certain limits. (See <i>Employee Discounts</i> , later.) | | |
| Employee stock options | See <i>Employee Stock Options</i> , later. | | |
| Group-term life insurance coverage | Exempt | Exempt ^{1,4} up to cost of \$50,000 of coverage. (Special rules apply to former employees.) | Exempt |
| Health savings accounts (HSAs) | Exempt for qualified individuals up to the HSA contribution limits. (See <i>Health Savings Accounts</i> , later.) | | |
| Lodging on | Exempt ¹ if furnished for your convenience | | |

| Type of Fringe Benefit | Treatment Under Employment Taxes | | |
|--|---|------------------------------|-----------------------------|
| | Income Tax Withholding | Social Security and Medicare | Federal Unemployment (FUTA) |
| your business premises | as a condition of employment. | | |
| Meals | Exempt if furnished on your business premises for your convenience. | | |
| | Exempt if de minimis. | | |
| Moving expense reimbursements | Exempt ¹ if expenses would be deductible if the employee had paid them. | | |
| No-additional-cost services | Exempt ³ | Exempt ³ | Exempt ³ |
| Retirement planning services | Exempt ⁵ | Exempt ⁵ | Exempt ⁵ |
| Transportation (commuting) benefits | Exempt ¹ up to certain limits if for rides in a commuter highway vehicle and/or transit passes (\$120), qualified parking (\$230), or qualified bicycle commuting reimbursement ⁶ (\$20). (See <i>Transportation (Commuting) Benefits</i> , later.) | | |
| | Exempt if de minimis. | | |
| Tuition reduction | Exempt ³ if for undergraduate education (or graduate education if the employee performs teaching or research activities). | | |
| Volunteer firefighter and emergency medical responder benefits | Exempt | Exempt | Exempt |
| Working condition benefits | Exempt | Exempt | Exempt |

¹ Exemption does not apply to S corporation employees who are 2% shareholders.

² Exemption does not apply to certain highly compensated employees under a self-insured plan that favors those employees.

³ Exemption does not apply to certain highly compensated employees under a program that favors those employees.

⁴ Exemption does not apply to certain key employees under a plan that favors those employees.

| Type of Fringe Benefit | Treatment Under Employment Taxes | | |
|------------------------|----------------------------------|------------------------------|-----------------------------|
| | Income Tax Withholding | Social Security and Medicare | Federal Unemployment (FUTA) |

⁵ Exemption does not apply to services for tax preparation, accounting, legal, or brokerage services.

⁶ If the employee receives a qualified bicycle commuting reimbursement in a qualified bicycle commuting month, the employee cannot receive commuter highway vehicle, transit pass, or qualified parking benefits in that same month.

Transportation (Commuting) Benefits

This section discusses exclusion rules that apply to benefits you provide to your employees for their personal transportation, such as commuting to and from work. These rules apply to the following transportation benefits.

- De minimis transportation benefits.
- Qualified transportation benefits.

Special rules that apply to demonstrator cars and qualified nonpersonal-use vehicles are discussed under *Working Condition Benefits*, later.

Working Condition Benefits

This exclusion applies to property and services you provide to an employee so that the employee can perform his or her job. It applies to the extent the employee could deduct the cost of the property or services as a business expense or depreciation expense if he or she had paid for it. The employee must meet any substantiation requirements that apply to the deduction. Examples of working condition benefits include an employee's use of a company car for business and job-related education provided to an employee.

This exclusion also applies to a cash payment you provide for an employee's expenses for a specific or prearranged business activity for which a deduction is otherwise allowable to the employee. You must require the employee to verify that the payment is actually used for those expenses and to return any unused part of the payment.

For information on deductible employee business expenses, see *Unreimbursed Employee Expenses* in Publication 529, Miscellaneous Deductions.

The exclusion does not apply to the following items.

- A service or property provided under a flexible spending account in which you agree to provide the employee, over a time period, a certain level of unspecified noncash benefits with a predetermined cash value.
- A physical examination program you provide, even if mandatory.

- Any item to the extent the employee could deduct its cost as an expense for a trade or business other than your trade or business.

Employee. For this exclusion, treat the following individuals as employees.

- A current employee.
- A partner who performs services for a partnership.
- A director of your company.
- An independent contractor who performs services for you.

Vehicle allocation rules. If you provide a car for an employee's use, the amount you can exclude as a working condition benefit is the amount that would be allowable as a deductible business expense if the employee paid for its use. If the employee uses the car for both business and personal use, the value of the working condition benefit is the part determined to be for business use of the vehicle. See *Business use of your car* under *Personal versus Business Expenses* in chapter 1 of Publication 535. Also, see the special rules for certain demonstrator cars and qualified nonpersonal-use vehicles discussed below.

However, instead of excluding the value of the working condition benefit, you can include the entire annual lease value of the car in the employee's wages. The employee can then claim any deductible business expense for the car as an itemized deduction on his or her personal income tax return. This option is available only if you use the lease value rule (discussed in section 3) to value the benefit.

Demonstrator cars. Generally, all of the use of a demonstrator car by your full-time auto salesperson qualifies as a working condition benefit if the use is primarily to facilitate the services the salesperson provides for you and there are substantial restrictions on personal use. For more information and the definition of "full-time auto salesperson," see Regulations section 1.132-5(o). For optional, simplified methods used to determine if full, partial, or no exclusion of income to the employee for personal use of a demonstrator car applies, see Revenue Procedure 2001-56. You can find Revenue Procedure 2001-56 on page 590 of Internal Revenue Bulletin 2001-51 at www.irs.gov/pub/irs-irbs/irb01-51.pdf.

Qualified nonpersonal-use vehicles. All of an employee's use of a qualified nonpersonal-use vehicle is a working condition benefit. A qualified nonpersonal-use vehicle is any vehicle the employee is not likely to use more than minimally for personal purposes because of its design. Qualified nonpersonal-use vehicles generally include all of the following vehicles.

- Clearly marked, through painted insignia or words, police and fire vehicles.
- Unmarked vehicles used by law enforcement officers if the use is officially authorized.
- An ambulance or hearse used for its specific purpose.

- Any vehicle designed to carry cargo with a loaded gross vehicle weight over 14,000 pounds.
- Delivery trucks with seating for the driver only, or the driver plus a folding jump seat.
- A passenger bus with a capacity of at least 20 passengers used for its specific purpose.
- School buses.
- Tractors and other special-purpose farm vehicles.

Pickup trucks. A pickup truck with a loaded gross vehicle weight of 14,000 pounds or less is a qualified nonpersonal-use vehicle if it has been specially modified so it is not likely to be used more than minimally for personal purposes. For example, a pickup truck qualifies if it is clearly marked with permanently affixed decals, special painting, or other advertising associated with your trade, business, or function and meets either of the following requirements.

1. It is equipped with at least one of the following items.
 - a. A hydraulic lift gate.
 - b. Permanent tanks or drums.
 - c. Permanent side boards or panels that materially raise the level of the sides of the truck bed.
 - d. Other heavy equipment (such as an electric generator, welder, boom, or crane used to tow automobiles and other vehicles).
2. It is used primarily to transport a particular type of load (other than over the public highways) in a construction, manufacturing, processing, farming, mining, drilling, timbering, or other similar operation for which it was specially designed or significantly modified.

Vans. A van with a loaded gross vehicle weight of 14,000 pounds or less is a qualified nonpersonal-use vehicle if it has been specially modified so it is not likely to be used more than minimally for personal purposes. For example, a van qualifies if it is clearly marked with permanently affixed decals, special painting, or other advertising associated with your trade, business, or function and has a seat for the driver only (or the driver and one other person) and either of the following items.

- Permanent shelving that fills most of the cargo area.
- An open cargo area and the van always carries merchandise, material, or equipment used in your trade, business, or function.