

## FRINGE BENEFITS ARE TAXABLE

Unless the law specifically excludes it, any fringe benefit you provide is taxable and must be shown on the employee's Form W-2. Failure to report taxable earnings could expose you to severe penalties:

Event	Tax Liability or Penalty Amount
<b>A.</b> Failure to withhold income taxes on taxable fringe benefits	Taxed at prevailing wage rates. If income is supplemental to wages, then taxed at 25% (30% if supplemental income exceeds \$1,000,000 in a calendar year)
<b>B.</b> Failure to withhold employee's portion of FICA taxes due on taxable benefits	7.65% of unreported income, up to FICA base of \$106,800 (in 2010), and 1.45% on the excess
<b>C.</b> Failure to pay employer's portion of FICA taxes due on taxable benefits	
<b>D.</b> Failure to deposit withholding taxes in a timely manner	Up to 10% of underreported employer share of FICA taxes discussed above (i.e., 10% of 7.65%)
<b>E.</b> Failure to pay employment taxes required to be shown on payroll tax return within 10 days of notice and demand	0.5% per month of underreported taxes above in A, B, and C, up to 25%
<b>F.</b> Negligence or intentional disregard of IRS regulations	20% of total taxes under A, B, and C, above
<b>G.</b> Failure to furnish correct payee statements (i.e., W-2)	\$50 per failure, with a maximum penalty of \$100,000 per calendar year

## HOWEVER, MANY FRINGE BENEFITS ARE TAX-EXEMPT

IRS publication 15-B, *Employer's Tax Guide to Fringe Benefits*, lists dozens of fringe benefits that are not subject to taxation. This guide provides an overview of those exemptions. Many have exceptions or further qualification requirements. For a more detailed explanation, visit [www.irs.gov](http://www.irs.gov) and search "Publication 15-B." This information was current as of November 2009.

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### Automatic Data Processing, Inc.

One ADP Boulevard  
Roseland, NJ 07068-1728

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# Taxable or Nontaxable?

## A Concise Guide to the Tax Status of Employee Benefits

**NOTE: This guide is provided for informational purposes and covers federal tax laws only. It is not intended to offer specific legal advice from counsel and does not cover state and local tax laws, which may vary. If you require legal or other expert assistance, seek the services of a competent professional.**

## TAXABLE

The value of the benefits in the following examples is generally taxable.

- **Cash bonuses or gifts.** When you award employees with cash (or gift certificates, or similar items easily exchanged for cash) you must report the value of such gifts as extra salary or wages, regardless of the amount involved.
- **Prizes in the form of goods or services.** If you award prizes or bonuses in the form of goods or services (e.g., a vacation trip for meeting sales goals), you must report the fair market value of the goods or services in the employee's income.
- **Employer-provided professional services.** The value of employer-provided tax preparation, accounting, legal, or brokerage services should be reported as extra salary or wages. The value of employer-provided outplacement services (e.g., training in résumé writing and interview techniques) must be reported if the employee accepts these services in exchange for reduced severance pay.
- **Personal use of employer-provided vehicles.** If you provide a car (or other highway motor vehicle) to your employees, the personal use of that vehicle may be taxable as a noncash fringe benefit. See IRS Publication 525 for how to determine the value of that benefit.

## NONTAXABLE

The benefits in the following examples are typically not taxable and therefore exempt from the tax reporting requirement.

### Token gifts and awards

- **Gifts of *de minimis* (minimal) value.** If you provide employees with a product or service and the cost is so small that it would be unreasonable for you to account for it, the value need not be included in the employee's income. Examples include holiday gifts, occasional theater or sporting event tickets, flowers, fruit, or books. There is no set dollar limit, but the IRS has ruled in at least one case that a gift over \$100 must be treated as taxable income.
- **Achievement Awards,** defined as an item of "tangible personal property" (e.g., a trophy or plaque) that you give an employee for length of service or a

safety achievement. The award must be given as part of a meaningful presentation and under such conditions that it does not amount to disguised compensation. Depending on the circumstances, the excludable value of the award is limited to either \$400 or \$1,600, or the employer's actual cost.

### Employer-provided goods and services

- **Discounts on employer-provided goods or services** normally offered to customers during the course of business may be exempt from tax. This exemption does not apply to discounts on real property or on property commonly held as an investment. The discount on services cannot exceed 20%.
- **No-additional-cost services** (e.g., excess capacity services such as airline, bus, or train tickets; hotel rooms; or telephone services provided free or at a reduced price to employees working in those lines of business) are exempt if you provide such services to customers during the ordinary course of business, and incur no substantial additional cost in providing those services to your employee.
- **Retirement Planning Services,** if offered to employees and their spouses as part of a qualified retirement plan.
- **Lodging and meals on your business premises** are exempt if certain conditions are met (e.g., furnished for the employer's convenience, the employee must accept lodging as a condition of employment).
- **Qualified transportation fringe benefits** (up to \$230/mo.) such as van transportation between the employee's home and work, a transit pass, or parking valued at no more than \$230 a month. This also includes cash reimbursement for these expenses under a *bona fide* (official) reimbursement arrangement. Cash reimbursement for transit passes is excludable only if made through a voucher or similar item that can be exchanged *only* for a transit pass.
- **Use of a company van for commuting** may also qualify as a tax-exempt benefit, provided that it is a "highway vehicle" and seats at least six adults, not including the driver. At least 80% of the vehicle's mileage must reasonably be expected to be for:
  - Transporting employees between their homes and workplace, and
  - Trips during which employees occupy at least half the vehicle's adult passenger seating.

- **Employee use of an on-premises gym or other athletic facility,** if substantially all use of this facility during the calendar year is by your employees, their spouses, and their dependent children.

### Reimbursements

- **Educational Assistance.** Employees can exclude from their income up to \$5,250 of qualified employer-provided educational assistance if certain conditions are satisfied. See IRS Pub. 970 for details.
- **Moving expense reimbursements.** Applies only to moving expenses that the employee could deduct if he or she had paid or incurred them without reimbursement. Does not apply if the employee actually deducted these expenses in a previous year. See IRS Pub. 521 for details.
- **Payments or reimbursements of qualified adoption expenses.** Exclude these from earnings that are subject to federal income tax withholding. They are still subject to Social Security, Medicare, and federal unemployment (FUTA) taxes. The maximum exclusion for 2009 is \$12,150.

### Health and life insurance

- **Group-Term Life Insurance.** You can provide up to \$50,000 of group-term life insurance coverage without reporting the employer's cost in the employee's income.
- **Accident and health benefits.** As of this writing, employer contributions to an employee's accident or health insurance plan are nontaxable, including:
  - Contributions to the cost of accident or health insurance, including qualified long-term care insurance.
  - Contributions to Archer MSAs or a health savings account (HSA). See IRS Pub. 969 for details.
  - Direct or indirect payments under an accident or health plan that are payments or reimbursement of employee medical expenses, or payments for specific injuries or illnesses (such as the loss of an arm or leg).
- **COBRA premiums.** Amounts you pay to maintain medical coverage for a current or former employee under COBRA should not be reported as taxable wages, provided the plan covered by the COBRA premiums is a "qualified plan." See IRC Section 4980B(g) for details.