

## Episode 3: Best Practices for Employers Regarding Fringe Benefits

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### Audio Transcript

**Joanna Kerpen:** Welcome to Winston's Benefits Blast podcast. I'm Joanna Kerpen and I'm joined by Ruth Wimer. Ruth and I are employee benefits partners located in Winston & Strawn's Washington, D.C. office. During this episode, we will be discussing best practices for employers regarding fringe benefits.

Hi Ruth, can you tell us, what are fringe benefits.

**Ruth Wimer:** Joanna, that's a tough one because fringe benefits are not defined for tax purposes and human resource departments are not consistent as to how fringe benefits are defined. However, it's safe to say, that when we use the term 'fringe benefits', we are generally referring to employer-provided benefits above and beyond the periodic paycheck, annual bonuses, and equity incentive plans. Fringe benefits may include the basics such as health or life insurance, but most employers provide additional, in-kind benefits which can make a big difference in employee morale.

Examples of fringe benefits can include, the well-known benefits such as employer cafeterias, cell phones, company car, transportation plans, adoption assistance plans, educational assistance plans, employee discounts, no-additional costs services, vacation, paid time off plans, and de minimis fringe benefits. Or the more exotic such as nap pods and bring your pet to work privileges.

While a vast array of employer-provided benefits could fall under the fringe benefit moniker, our discussion today gives a broad overview of fringe benefits and tips on best practices. So listen carefully.

**Joanna Kerpen:** What are some of the most common fringe benefits you see offered by employers today?

**Ruth Wimer:** Statistics show, listed in order of popularity, they are:

- Health insurance
- Life insurance
- Dental
- Retirement (such as 401k)
- FSA or HSA, which are types of health benefits
- Paid vacation
- Sick time
- Holidays
- Medical leave
- Flexible schedules
- Educational assistance

Other common benefits are:

- Cell phones
- Cafeteria plans
- Free gyms
- Free daycare
- Wellness programs
- Financial wellness counseling

**Joanna Kerpen:** If an employee receives a fringe benefit, is that fringe benefit considered taxable income to the employee?

**Ruth Wimer:** Okay, spoken like a real attorney, I would say it depends. Some are and some are not. And the rules are always changing. For example, moving expenses for work purposes are now taxable income to employees beginning in 2018. There are strict rules to qualify a fringe benefit to be tax-free to the employee for federal income tax purposes. However, one of the great hints we're giving today is that there is a treasure trove, great source to determine whether a fringe benefit is taxable income and that is IRS Pub 15-B.

Note that even where a fringe benefit is not taxable to employees the cost of the fringe benefit is generally still deductible to the employer. Note I said generally. However, this rule does have a few exceptions which must be watched for carefully.

For example, the Tax Cuts and Jobs Act removed the employer tax deduction for transportation benefit programs where an employee receives parking or transit passes on a tax-free basis. The IRS has come out with guidance on how to calculate the disallowance of the employer deduction with respect to tax-free parking benefits. This guidance should be examined carefully by those employers who offer tax-free parking.

The Tax Cuts and Jobs Act also added a 50% reduction in the amount which is deductible to the employer for de minimis meals, snacks and cafeterias provided to employees until the year 2025 when no deduction for these fringe benefits is available. In addition, under the Tax Cuts and Jobs Act, the expenses related to commuting for which there is not a concern for the safety of the employee, is also not deductible, even if included in the employee's income. Therefore, providing these types of tax-free fringe benefits to employees actually results in the loss of a tax deduction for those amounts to the employer.

**Joanna Kerpen:** What about FICA and FUTA taxes, are fringe benefits subject to those?

**Ruth Wimer:** Good question, generally where a fringe benefit is exempt from federal income tax to the employee, it's also exempt from FICA and FUTA. Note that there are few fringe benefits which are exempt from federal income tax withholding, but not from FICA tax withholding, such as personal use of a company automobile and excess group term life insurance.

**Joanna Kerpen:** Are there types of fringe benefits that an employee may not even realize is a potentially taxable benefit for them?

**Ruth Wimer:** Definitely, one such category to watch out for is where the fringe benefit is not taxable, but only if certain IRS rules are met. For example, fringe benefits must often pass complex non-discrimination tests. These tests are generally a little different for each type of fringe benefit. Recently, I've seen this problem with life insurance, educational assistance, dependent care assistance programs, and uninsured health benefits and even on several occasions, employee discounts or no-additional costs services, so this is a trap for the unwary. If a fringe benefit does not meet these non-discrimination tests, the highly paid employees are taxed on the benefit received. Fortunately, the non-highly paid employees generally do continue to receive the fringe benefit tax-free.

**Joanna Kerpen:** Can you think of any other fringe benefits that you see that cause employers difficulty with regards to the correct tax treatment?

**Ruth Wimer:** Absolutely. Meals and transportation provided to employees at work or when working overtime. Employers like to think that any meals provided to employees are tax-free. This is not true. The major exclusions are de minimis meals, very occasional meals when working overtime and meals for the convenience of the employer. All of these have strict definitional requirements which must be met for exclusion and employers often think they meet these rules when they do not. In an audit, the IRS will require employer penalties and amended form W-2's to the employee.

**Joanna Kerpen:** What are some new, trendy fringe benefits out there today?

**Ruth Wimer:** Another good question and everyone likes the new, trendy fringe benefits. As mentioned previously, flexible work schedules and also telecommuting are very popular and can usually cost the employer little or nothing and are very much appreciated by employees; a win-win. Note, however, that some states may require the employer to reimburse an employee for home internet under state labor laws which is a cost to the employer but may well be excluded from the employee's income as a working condition fringe.

Pet insurance, which would be taxable, as we discussed 'bring your pet to work days' which are not taxable, are also a new trend. Employee assistance programs which provide de minimis mental health counseling and concierge services are tax-free but are often underutilized.

**Joanna Kerpen:** What are some of the most common mistakes you see made by employers who offer fringe benefits?

**Ruth Wimer:** By far, the biggest mistake is not reporting and withholding on fringe benefits correctly. For example, the working condition fringe exclusion requires that the fringe such as use of an automobile or company provided aircraft be carefully documented as to the business purpose. Spousal travel is virtually never an excluded fringe benefit even if required by the employer to a company conference.

Another area of confusion is from employer-provided educational assistance because there are two types. There's Section 127 educational assistance wherein the tax exclusion is limited to \$5,250 per year, per employee and which must be nondiscriminatory. And there's Section 162 exemption, for work-related education which can be discriminatory and which can be on an unlimited amount but which cannot qualify the employee for a new career. For example, a law degree does not qualify but an MBA may, depending on the facts and circumstances.

**Joanna Kerpen:** Can you tell us something that is unique about fringe benefits?

**Ruth Wimer:** I'd be glad to, to make your time worthwhile for this podcast, there is, in addition to IRS pub 15-B which I mentioned that gives you a lot of the answers to the tax treatment. Everyone should be aware of IRS Announcement 85-113. That guidance put out by IRS has special, favorable rules regarding reporting and

withholding that allow fringe benefits to be withheld upon other than at the time in which the fringe benefit is provided. And the withholding can incur as infrequently as only once per year.

Furthermore, the benefits can be reported on a fiscal year basis unique to the fringe benefits on a 12 month period beginning on or after November 1st of each calendar year so that the employer has more time to get the totals to report on the year's form W-2.

**Joanna Kerpen:** Can an employer get into trouble for not treating fringe benefits properly?

**Ruth Wimer:** Yes, both the individual making that decision and/or the employer company can have serious legal repercussions. First, if an amount is taxable wages and it's not treated as taxable income, the employer will be separately liable from non-withheld employment taxes including federal income and FICA. The administration involved with correcting these kind of errors is extensive, requiring amended Form 941's and W-2's. This is the result for even unintentional errors.

Secondly, the individuals responsible can have serious legal problems. For example, the executive that makes the decision to not withhold payroll taxes intentionally could be held personally liable for the non-withheld taxes. This is often one of the responsible officer's biggest fears. Another legal issue the individual can have is if a named executive officer of a public company intentionally does not report a fringe benefit. For example, personal travel where the executive asserted it was business travel.

**Joanna Kerpen:** So now that we've learned all about what fringe benefits are, what are some best practices regarding fringe benefits that you would recommend for employers?

**Ruth Wimer:** I would definitely recommend that employers perform periodic fringe benefit audits to assess whether they are using the proper tax treatment for fringe benefits. Systems should be in place with the party responsible for each and every one of the fringe benefits provided by the company.

**Joanna Kerpen:** Thank you so much Ruth, this has been great. And thank you for listening to another edition of our Benefits Blast podcast. Stay tuned to future episodes for more insights on the latest legislative, regulatory and practical developments concerning employee benefits and executive compensation. Also, please check out our Benefits Blast blogs located on [Winston.com](http://Winston.com) for updates on the latest legal developments in the employee benefits area.

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Joanna Kerpen



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