Fringe Benefits: Employer Gifts

By Catina M. Scafidi, CPA, and Anthony P. Curatola

AS THE HOLIDAY SEASON GROWS NEAR AND the halls of corporate America start to permeate with holiday cheer, employees' hands will start to be filled with the ever so popular annual holiday gifts. This year's holiday gift, however, may not leave employees or employers singing a holiday tune!

Why is it that so many employers provide gifts (i.e., fringe benefits) during the holiday season instead of reaching into their pockets and paying a bonus? Whereas compensation is taxable, fringe benefits may be excluded from the employee's income if the benefits are specifically excluded from income under §132 of the Internal Revenue Code. No-additional-cost services, employee discounts, working condition fringe benefits, *de minimis* fringe benefits, qualified moving expenses reimbursements, qualified retirement planning services, qualified military base realignment and closure fringe, and qualified transportation fringe benefits are specifically excludable from gross income (IRC §132(a)). Any employer-provided fringe benefit that does not qualify for exclusion under §132 *and* is not excludable under another specific "statutory provision" of the Code must be included in the recipient's gross income as provided by IRC §61 and §83. The amount includable in the recipient's gross income is the excess of its fair market value over any amount paid by the recipient for the benefit.

According to IRC §132(e)(1), the term "*de minimis* fringe" means any property or service with a value so small that accounting for it is unreasonable or administratively impractical. Additionally, for a benefit to be deemed a *de minimis* fringe, the benefit must be offered infrequently (Reg. §1.132-6(b)). Fringe benefits that aren't "unreasonable or administratively impractical to account for" *and* aren't excludable under any other statutory provisions are taxable under Reg. §1.132-6(c). Moreover, if a benefit is excludable as a *de minimis* fringe because the benefit is too valuable or provided too frequently, then no part of the benefit would be excluded from gross income (Reg. §1.132-6(d)(4)). If the majority of value of a benefit is excludable under other statutory provisions, however, the remaining value may be excludable as a *de minimis* fringe benefit. Another attractive feature to *de minimis* fringe benefits is that they don't fall under the nondiscrimination rules like many other fringe

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benefits (IRC §132(j)(1); Reg. §1.132-6(f)).

So exactly when is a benefit deemed a *de minimis* fringe? This is a good question. As stated before, one must evaluate the *value, frequency,* and *administrative impracticability of accounting for* the benefit. Under this subjective standard, the classification of whether a benefit falls under the provisions of IRC §132(e) depends on other benefits provided by the employer. As you might suspect, the Code doesn't provide an objective standard, such as a total dollar amount. Of course, the creation of a dollar amount standard itself may create an administrative burden.

The next place to look for some guidance in this area is Treasury. According to Reg. §1.132-6, *de minimis* fringe benefits include but are not limited to occasional typing of personal letters by a company secretary; occasional personal use of an employer's copying machine; cocktail parties, group meals, or picnics for employees or their guests; traditional birthday or holiday gifts of property (not cash) with a low fair market value; occasional theater or sporting event tickets; coffee, doughnuts, and soft drinks; local telephone calls; and flowers, fruit, books, or similar property provided to employees under special circumstances (e.g., on account of illness or outstanding performance). *De minimis* fringe benefits, on the other hand, do *not* include items such as season tickets to sporting or theatrical events; the commuting use of an employer-provided automobile or other vehicle more than one day a month; membership in a private country club or athletic facility, regardless of the frequency with which the employee uses the facility; employer-provided group-term life insurance on the life of the spouse or child of an employee; and use of employer-owned or leased facilities for a weekend.

Moreover, cash, regardless of the amount, is *never* deemed to be a *de minimis* fringe benefit because "cash is always accounted for." Additionally, the term "cash" is extended to those benefits provided to an employee through the use of an employer credit card (Reg. §1.132-6(c)).

This all seems simple enough, right? Wrong. An employer who normally gifted a ham, turkey, or basket to their employees decided to discard that methodology of holiday gift giving and start a new holiday tradition. The employer started to issue holiday food gift coupons with a face value of $35 instead. The coupons were redeemable at several local grocery stores. The employer deemed this type of gift giving to fall under the provisions of *de minimis* fringe benefits as the gifts in the past had. The employer, therefore, didn't withhold or pay any employment taxes on these gift coupons. The IRS didn't share the employer's view and instead held in Private Letter Ruling 200437030 that the employer-provided gift coupon was *not* excludable from gross income and wages as a *de minimis* fringe benefit under IRC §132(a)(4).

What prompted this unfavorable ruling? The IRS looked at IRC §132(e)(1), which requires the three factors (value, frequency, and administrative impracticability of accounting for the benefit) to be addressed for an item to qualify as a *de minimis* fringe benefit. In this situation, the coupons have a specific value, and, as such, the Service held that the gift coupons are indistinguishable from cash equivalent fringe benefits such as gift certificates. Therefore, they are easy to account for, and, as previously stated, "Cash is always accounted for!" But suppose our employer gave a coupon that allowed the person to purchase a turkey or ham at the local store and no price was given on the coupon. Is this coupon indistinguishable from cash equivalent fringe benefits (i.e., taxable), or is it administratively impracticable to account for (i.e., *de minimis* fringe and not taxable)?

So what should an employer do when moved by the holiday spirit? Throw a holiday lunch or dinner for your employees! Under Reg. §1.132-6(e)(1), by hosting a holiday meal, the value of each meal would be excluded as a *de minimis* fringe benefit. An added benefit to this method of gift giving is that this type of meal and entertainment costs are fully deductible and not subject to the normal 50% deduction limit. A "win-win" situation for both the employer and employee!

Have a happy and safe holiday season. ■

Catina M. Scafidi, CPA, is tax manager at Altenburger, Uris, Caglioti, & Heyman, LLC. You can reach Catina at (856) 596-1010, ext. 122, or CatinaMScafidi@comcast.net.

Anthony P. Curatola is the Joseph F. Ford Professor of Accounting at Drexel University in Philadelphia, Pa. You can reach Tony at (215) 895-1453 or curatola@drexel.edu.

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