

**November 2003**

## **Fringe Benefits Carry Tax Implications**

It's important to understand the tax status of the benefits provided by the employer. Even in today's economy, most job hunters recognize that employment offers more than just salary. Fringe benefits, especially tax-free ones, are an important part of any compensation package. Here is an overview of some of the more common fringe benefits and their tax treatment:

- **Health Benefits** - For many people, health insurance is the most important employee benefit. The premium costs that your employer pays for medical, dental, and vision coverage for you and your family is not considered taxable income. In addition, any portion of the healthcare insurance premium that you pay can be taken from pre-tax dollars. If you anticipate paying healthcare costs that your employer's insurance plan does not reimburse, ask if a healthcare flexible spending account plan is available. This type of plan would allow you to pay for those expenses with pre-tax dollars. (See cafeteria plans below.)
- **Retirement Plans** - Another significant benefit offered by many companies are 401(k) or other qualified deferred compensation plans. With such plans, you elect to have a portion of your compensation deducted from your paycheck before taxes and deposited in your retirement savings plan. Your taxable income is lowered and your contributions grow tax-deferred until you begin to take distributions from the account. If your employer offers matching contributions, it will boost your savings more quickly.
- **Group Term Life Insurance** - An employee can generally exclude from income employer payments of premiums on a policy of up to \$50,000 of qualified group term life insurance. Coverage above that amount may result in your compensation increasing a few dollars to account for the extra premium "cost" as determined from an IRS table based on the age of the covered employee. However, the tax you pay is usually less than what you would pay privately for such an insurance policy.
- **Disability Insurance** - Employer-paid premiums for disability insurance are not taxable to the employee. However, when the employer pays the premium, the disability payments received by the employee are taxable. On the other hand, if the policy's premiums are paid by the employee (on an after-tax basis); any disability payments received are not taxable.

- **Company Car** - Getting a company car may seem like a great perk, but remember that when the car is driven for personal use, there are tax implications. Personal use of an employer-provided vehicle is taxable and the value of the personal use must be included in the employee's gross income on Form W-2. However, de minimis personal use, such as stopping for lunch during the normal course of conducting business, is not considered personal use and is not taxable.
- **Child Care Expenses** - If your prospective employer offers childcare, you may reap a tax benefit. Childcare expenses paid by your employer under a non-discriminatory plan are tax-free up to \$5,000 a year. This is true whether the money goes to a qualified care provider you select or covers the cost of care at an employer-provided facility. If your employer doesn't provide this tax-free benefit, you may be able to get some tax relief through a flexible spending account. (See cafeteria plans.)
- **Educational Assistance Programs** - Company-provided educational expenses of up to \$5,250 under an employer's educational assistance program are tax-free. The course need not be job-related.
- **Cafeteria Plans** - Under a cafeteria plan, employees choose from a "menu" of taxable and nontaxable benefits that best suit their individual needs, preferences, or lifestyles. For working couples, a cafeteria plan means that if one spouse has health insurance, the other may forego health coverage and choose another benefit in its place.

Cafeteria plans often include flexible spending accounts, which allow you to pay certain expenses such as medical and dependent care costs, with pre-tax dollars. Your contributions to these plans are exempt from federal income taxes. However, it is important to carefully estimate the amount you contribute to a flexible account because any funds that are unused at the end of the year are forfeited.

- **Employee Discounts** - Employee discounts are tax-free if the discounts are on products or services generally sold in the business for which the employee works. For merchandise, the discount exclusion is limited to the product's gross profit percentage. For example, if a company sells an item for \$75 and its cost is \$50, its gross profit margin is \$25. Thus, an employee's tax-free discount could not exceed \$25. For services, the exclusion is limited to 20 percent of the value of the service.
- **Signing Bonus** - Although signing bonuses have become scarce, should you be offered one, be prepared to pay taxes on the full amount.
- **De Minimus Benefits** - Occasional personal use of business equipment such as copiers, faxes and phones are tax free to employees. Similar tax-free status applies to coffee, doughnuts, soda, office parties and picnics, small gifts to employees, and other similar nominal employee perks.
- **Adoption Benefits** - Generally, an employee can exclude from income qualified adoption expenses of up to \$10,000 paid or reimbursed to you by an employer.

This exclusion is phased out depending on your modified adjusted gross income.

- **Transportation Expenses** - For 2003, an employee may exclude from their income a maximum of \$100 a month for the value of employer provided transit passes and the first \$190 for qualified parking expense. Amounts paid in excess of these limits must be included as taxable income.
- **Frequent Flyer Miles** - Flying frequently for business may enable you to obtain another tax free benefit: the value of frequent flyer miles accumulated as a result of business travel.

CPAs point out that the total value of all taxable fringe benefits received by an employee must be included in wages reported on the W-2. If you have any questions about the tax status of your benefits, consult with a CPA.

Very Truly Yours,

Krebs & Co., CPA's, Inc.  
dba **Krebs Advisory Group**