TAX YEAR
2023

Fringe Benefits

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Tax Treatment of Fringe Benefits

The term "fringe benefit" refers to any benefit provided to an employee that is in addition to money. All benefits provided to an employee are taxable unless the law specifically excludes or defers tax on the benefit. Thus, a fringe benefit can be taxable, tax-deferred, or excluded from taxation.

The personal use of an employer-provided vehicle is an example of a taxable fringe benefit. An employer contribution to a qualified retirement plan on behalf of the employee is an example of a tax-deferred fringe benefit. Employer-provided health insurance for an employee is an example of a tax-free fringe benefit.

Business Owner

A small business owner in a corporate setting may be both the owner and an employee of his or her business. By taking advantage of excludable fringe benefits, the owner receives a double benefit. First, the cost of the benefit is deductible by the business. Second, the cost of the benefit is tax free to the employee-owner.

Nondiscrimination Rules for Fringe Benefits

Nondiscrimination rules are designed to prevent business owners from offering tax-favored fringe benefits to themselves but not their employees. In general, if fringe benefits are offered to all employees, then all employees, including the top paid employees, receive tax-favored treatment on employee benefits. However, if a plan favors highly-compensated employees or key employees, the value of the benefit must be included in their taxable wages. The terms "highly-compensated employees" and "key employees" can mean different things depending on the applicable plan. Special restrictions apply for fringe benefits for sole proprietors, partners, certain LLC members, and S corporation shareholders. Contact us if you are a business owner considering providing fringe benefits to yourself and your employees.

Employer-Provided Vehicles

If an employer provides an employee with a company-owned vehicle, the employer must include the value of any personal use in the employee's Form W-2 as other compensation. Social Security and Medicare tax must be withheld. Federal income tax withholding is optional if the employee was notified and the value of the benefit is included in boxes 1, 3, 5, and 14 of Form W-2. The employer has several options on how to calculate the value of the benefit.

- General valuation,
- Annual lease value method,
- Cents-per-mile method, and
- Commuting value method.

Employer-Provided Cell Phones

The value of an employer-provided cell phone, provided primarily for noncompensatory business reasons, is excludable from an employee's income.

Noncompensatory Business Purposes

An employer needs substantial business reasons for providing the cell phone. Examples include:

- Need to contact the employee at all times for work-related emergencies,
- Requirement that the employee be available to speak with clients at times when the employee is away from the office, and
- Need to speak with clients located in other time zones at times outside the employee's normal workday.