

Internal Operations Manual

SUBJECT: Taxable Fringe Benefits

NUMBER: 107-07-030

DIVISION: Operations Division - Payroll

EFFECTIVE DATE: 12-01-03

APPROVED:



POLICY/PURPOSE: This policy is to provide information and procedures to determine if fringe benefits, paid through Payroll, are taxable.

AUTHORITY: IRS; Internal Revenue Code §119, 127, 132(d) 162; 217(b), pub. 521 and 15b, ORS 292.036; Oregon Accounting Manual 50.10.00 PO

APPLICABILITY: All current employees of the Department of Administrative Services, who purchase uniforms and protective clothing, apply for meal reimbursements, education reimbursements, or moving expense.

ATTACHMENTS: **Exhibit A** - Chart of Taxable & Non-taxable Cost of Travel to New Home

Exhibit B - Fringe Benefit Resource List

DEFINITIONS:

Accountable Plan (Non-taxable to employee) - An allowance or reimbursement program where amounts are non-taxable to the recipient if required rules are met:

- A business connection to the expenditure
- Adequate Accounting by the employee within 30 days of the end of the event
- Excess reimbursements or advances must be returned within 30 days of receipt

Adequate Accounting - Verification of time, place, amount and business purpose of expenses. Receipts are required.

Business Connection - Expense must be a deductible business expense incurred in connection with services performed as an employee. If not reimbursed by the employer, the expense would be deducted as a business expense on IRS Form 2106.

Fringe Benefit - Any property or service (or cash other than salary) provided to an employee by an employer for the performance of services in addition to regular pay.

A form of pay for the performance of service given by the provider of the benefit to the recipient of the benefit.

Non-taxable De Minimis Fringe Benefits: Occasional (infrequent), not routine, such as personal use of photocopier, local telephone calls.

DEFINITIONS (Continued)

Taxability – Taxable unless specifically excluded by a section of the Internal Revenue Code (IRC).

Taxable - means included in employees' wages and included on W-2, subject to federal income tax withholding, social security (6.2%) and Medicare (1.45%), unless the employee has already reached the current calendar year's maximum social security. An employer's matching contribution is required for social security and Medicare (7.65%).

Working Condition Fringe Benefits: Property or service provided by an employer for an employee that if the employee had paid for it they could have deducted as a business expense on Form 2106.

GUIDELINES:**General Rules for Working Condition Fringe Benefits**

Property or service by an employer for an employee that if the employee had paid for it, they could have deducted it as a business expense on IRS Form 2106.

- a. Benefit must relate to employer's business
- b. Employee would have been entitled to a 1040 deduction
- c. Business use must be substantiated with records
- d. Certain benefits have other specific requirements

I. CLOTHING

A. Not taxable: Jackets, slacks, work boots, coveralls, and shirts are not taxable as wages to an employee if the clothing is:

- a. Specifically required as a condition of employment
- b. Not adaptable to general usage as ordinary clothing
- c. Are, in fact, not worn for general usage

Generally, clothing with a readily distinguishable logo or employer's name is not considered suitable for general wear.

B. Taxable: Periodic allowance payments provided by the employer to the employee for the purchase of clothing or accessories to be worn on the job site.

Per IRS these allowances are taxable unless three conditions are met:

- a. The uniform and accessories must be required to be worn as a condition of employment
- b. They cannot be adaptable to general use
- c. They cannot be worn for general use

II. MEALS

Internal Revenue Code requires that a meal provided to an employee is a taxable fringe benefit unless expressly excluded from income because the employee is on overnight travel status or that the meal is part of an official meeting agenda.

Meal expense reimbursement allowance must meet the Accountable Plan rules in order to be tax-free to the employee.

A. Meal Reimbursements While Traveling Away from Home on Business

Meals while traveling away from home on business may be paid using an actual expense or per diem reimbursement method.

Using the Actual Expense Reimbursement Method:

- a. Reimbursement must be paid under the accountable plan to be tax-free
- b. The amount, date, place, business purpose (and business relationship for entertainment expenses) must be documented
- c. Reimbursement is based on what is actually spent
- d. Employee must have records and receipts
- e. Expense must not be lavish; must be reasonable based on circumstances

Per Diem Meal Allowance

- a. An employee must be traveling on business away from home overnight (or meet the "sleep and rest" rule)
- b. The employee is provided a set dollar amount depending on where and when traveling instead of keeping actual cost records. The employee must still keep records to document the time, place and business purpose of travel
- c. The reimbursement allowance will be prorated for partial travel days (day of departure and return)
- d. If traveling to more than one location in one day, employee must use rate for area where *stopping for rest or sleep*

The Per diem method is not permitted for travel unless the employee is away from home overnight.

B. Meals Away From Tax Home But Not Overnight (IRS Definition, Not "In Travel Status")

Meals are taxable as a wage to employee because they do not meet the business connection requirement of the Accountable Plan rules. Travel must be away from home overnight to be tax-free.

C. Meal Reimbursements While Not Traveling Away From Home

Reimbursements or allowances provided to employees for meals with business meetings or while entertaining customers may be tax free if the expenses are ordinary, necessary, and meet the following criteria:

- a. Reimbursement must be paid under the accountable plan to be tax-free
- b. The amount, date, place, business purpose (and business relationship for entertainment expenses) must be documented

Meal Reimbursements While Not Traveling Away From Home (*Continued*)

- c. Reimbursement is based on what is actually spent
- d. Employee must have records and receipts
- e. Expense must not be lavish; must be reasonable based on circumstances

Directly-related test: Meal reimbursements are non-taxable if the business event takes place in a clear business setting and the expenses are considered directly related to agency business.

Associated Test: Meal reimbursements are non-taxable if a substantial business discussion occurs which directly precedes or follows the meal. Meals officially scheduled as part of a business conference or convention meet the associated test.

III. EDUCATIONAL REIMBURSEMENTS

A. Taxable: After December 31, 1994, the Internal Revenue Code, Section 127, has required educational assistance payments made to or on behalf of an employee for educational courses unrelated to an employee's current job, to be taxable. Employees are responsible for the payment of all net income taxes due. Employers are responsible to withhold income tax and Social Security tax from taxable payments.

B. Non-taxable: Education assistance payments made after December 31, 1994, for courses directly related to the employee's current job remain tax exempt.

The category of training can effect the taxable status of tuition. Training falls under three categories:

- a. Job Required - Needed to meet minimum job performance (mandatory)
- b. Job Related - To increase/improve skills above minimum job performance
- c. Career Development - For self-enhancement (not necessarily job related)

If there is no relationship between the training and the current position duties, the class is considered to be taxable.

The employee's supervisor/manager is responsible for determining the taxability of education assistance payments.

EDUCATIONAL REIMBURSEMENTS (Continued)

Education assistance payments will not be made without the signed approval of a manager. Payroll will review the category determined by the manager for reasonableness and will refer any questions to the Payroll Supervisor.

All payments made for tuition will be made through the Payroll System. For job required training, DAS pays the tuition directly to the institution.

For job related or career development classes, employees must pay tuition and keep the receipt

showing amount paid for registration, books, etc. When the class is completed the employee must submit the following documents to the OBA Payroll Section for reimbursement:

- a. Proof of successful completion (grade report or certificate)
- b. Copy of receipt
- c. Signed completed Training Request Form
- d. Reimbursement Request Form with proper authorization signature

If the course is determined to be taxable (not job related), taxes will be withheld on the reimbursement at the same rate that taxes are withheld for pay.

If the course is job required and the institution has been paid, the employee must submit a copy of the grade report to Payroll for the employee file. If the course is not passed, the employee must retake the course at his or her own expense and obtain a passing grade.

Exceptions: For job related and career development, exceptions can be made to reimbursement procedures if the manager determines there is a financial hardship to the employee.

In this case the employee must sign a statement that they will repay DAS if they do not pass. A grade of "C" or above is considered passing in a graded course. A "pass" is needed in a pass/fail class. After the course is completed, proof of successful completion must be submitted to Payroll for the employee file.

IV. MOVING EXPENSE**General Rule**

A moving expense reimbursement received directly or indirectly from an employer (under an accountable plan) is not taxable to the employee if specific tests in IRC Section 217 are met.

Specific Tests

- a. Individual must be an employee
- b. Employee must pay or incur the expense
- c. Expenses are closely related to starting work at your new job location
- d. Expenses must qualify as moving expenses under IRC Section 217

MOVING EXPENSE (Continued)**e. Certain Time and Distance requirements must be met:**

- Employee must be employed 39 weeks and new job is at least 50 miles farther from your former home than your old job location was from your former home.

Expenses covered are:

- a. Moving household and personal effects from the old residence to the new, including the cost of packing, in-transit storage, and insurance. Agencies should refer to DAS HRSD policies for guidance and applicable limitations.**
- b. Travel and lodging from the former residence to the new one. In order to be non-taxable, mileage must be paid according to the IRS approved moving mileage rate.**
 - **Travel Time Begins** one (1) day after former residence is no longer suitable for occupancy and includes 1 night lodging at prior residence.
 - **Travel Time Ends** on the date the employee secures lodging at the new place of residence. The qualified expenses are deductible only for the first day the employee arrives at new location.

All other moving expense payments are, on their face, taxable.

Please note that the lists given below include common examples and are not all inclusive. For more details please see *Moving Expenses*, IRS Publication 521 or the website

<http://search.msn.com/preview.aspx?&q=IRS+Publication+521>

| COSTS OF TRAVELING TO NEW HOME: | |
|--|--|
| NON TAXABLE (Deductible) | TAXABLE (Non-deductible) |
| <p>Moving other household members (not necessary to travel together)</p> <p>Airfare</p> <p>Travel by car** 13 cents per mile (2002 rate) or actual gas and oil costs</p> <p>Lodging expenses while traveling</p> <p>Parking Fees</p> <p>Tolls</p> | <p>Pre-Move house-hunting</p> <p>Meals</p> <p>Trips back and forth to prior home</p> <p>Transportation expenses: a. Car repairs, general maintenance, insurance and depreciation on vehicle b. Mileage reimbursement in excess of 13 cents (2002 rate) per mile.</p> <p>Living or other expenses related to waiting for movers to arrive or getting into new home.</p> |
| COSTS OF MOVING HOUSEHOLD GOODS AND PERSONAL EFFECTS | |
| NON TAXABLE (Deductible) | TAXABLE (Non-deductible) |
| <p>Packing, crating and transporting goods</p> <p>Connecting/disconnecting utilities</p> <p>Shipping your car</p> <p>Shipping your pet</p> <p>Storage and insurance of goods (Any period of 30 consecutive days after goods are moved from your prior home and before they're delivered to your new home.)</p> | <p>Meals and lodging in temporary home</p> <p>Storage or transporting your boat or RV</p> <p>Selling costs or losses on sale of prior residence</p> <p>Lease cancellation fees</p> <p>Mortgage cancellation fees</p> <p>Cancelled club memberships</p> <p>Loss of tuition fee paid but not used because of move</p> |
| <p>Moving Expense Reimbursements are <i>not included in income</i> if the expenses qualify under IRC Section 217 and are reimbursed in the same calendar year they are deducted.</p> | |
| <p>**See Pub. 521, page 7, Travel by Car. All household members do not need to travel together or at the same time. You are allowed more than one car---reasonable expenses.</p> | |

FRINGE BENEFIT RESOURCE LIST

State Resources

Das State Controller's Division, John Radford, State Controller

Oregon State Payroll Services Sharon McKeehan, Manager (503) 378-6777 ext. 230

Assistance with questions about taxable fringe benefits and how to process transactions in the payroll system.

Web pages:

SCD web pages: <http://scd.das.state.or.us/scd.htm>

Oregon Accounting Manual: <http://scd.das.state.or.us/oam/scdpolicy/tableofcontent.htm>

- Travel – Chapter 40
- Payroll – Chapter 45
- Taxable Issues – Chapter 50

Oregon State Payroll: <http://scd.das.state.or.us/osps/>

Letters of Recommended Payroll Practice: <http://scd.das.state.or.us/osps/publications/appendd.pdf>

- Moving Expense
- Taxable Meals

DAS Human Resources Services Division

Policy 40.055.10 Employee Relocation Allowance (Moving Expense)
<http://www.hr.das.state.or.us/hrsd/policy/P4005510.pdf>

IRS Resources

Online at: http://www.irs.ustreas.gov/prod/forms_pubs/pubs.html

Suggested references:

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| Publication 15 – | Circular E, Employers Tax Guide |
| Publication 15 - A | Employer's Supplemental Tax Guide - |
| Publication 15 - B | Tax guide to Fringe Benefits |
| Publication 463 – | Travel, Entertainment, Gift and Car Expenses |
| Publication 503 – | Tax Benefits for Work Related Education |
| Publication 520 – | Scholarships and Fellowships |
| Publication 521 – | Moving Expenses |
| Publication 525 – | Taxable and Non Taxable Income |
| Publication 535 – | Business Expenses |
| Publication 970 – | Tax Benefits for Higher Education |