

Tax Treatment of Holiday Gifts to Employees

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Holiday gifts, bonuses and awards to employees may have important tax implications for employers. As a general rule, gifts and awards (whether in cash or otherwise) an employer gives to employees are considered additional W-2 wages, subject to payroll and income taxes. In certain circumstances, however, the Internal Revenue Code ("Code") provides that non-cash gifts to employees can be treated as tax-free.

Employee gifts in the form of cash or gift certificates/coupons, regardless of the amount, are always treated by the Internal Revenue Service as W-2 "wages" subject to withholding taxes. In the case of a gift certificate or coupon, the tax applies to the face value of the certificate/coupon.

Noncash gifts and awards given to employees can be treated as tax-free only if the gift or award can be characterized as a "de minimis fringe benefit" under Section 132 of the Code, or qualifies as an "employee achievement award" under Section 274(j) of the Code. Employee achievement awards may be made either as length-of-service awards or as safety awards.

De Minimis Fringe Benefit

If an award or prize is given in a form other than cash or a gift certificate/coupon and if the value is not large, it probably can be characterized as a non-taxable "de minimis fringe benefit." The IRS defines this as any property or service provided to an employee that has so little value (taking into account how frequently similar benefits are provided to all employees) that accounting for it would be unreasonable or administratively impracticable. The value of the benefit is determined by the frequency with which it is provided to each employee, or, if this is not administratively practical, by the frequency with which it is provided to the workforce as a whole.

The law does not specify a dollar threshold for benefits to qualify as de minimis. The determination will depend on the facts and circumstances. The IRS has not given any guidance, formal or informal, for determining when the value of a non-cash gift or award may become too large to qualify as a de minimis fringe benefit.

The de minimis fringe benefit definition takes into account the frequency with which the benefit, and all similar benefits, is provided. Generally, that frequency is judged on an employee-by-employee basis. But if it would be administratively difficult for an employer to monitor the frequency with which individual employees take advantage of a benefit, the frequency with which similar fringes are provided is determined by reference to the workforce as a whole.

The IRS has indicated that the following items may be treated as de minimis benefits if they are occasional:

- Personal use of photocopier (with restrictions)
- Group meals, employee picnics
- Theater or sporting event tickets
- Coffee, doughnuts, or soft drinks
- Flowers or fruit for special circumstances
- Local telephone calls
- Traditional birthday or holiday gifts (not cash) with a low fair market value

The tax implications of holiday gifts are simple to address and employers should ensure such remuneration are taken into account for purposes of year-end W-2s and payroll period reporting. Jackson Lewis attorneys are available to discuss this and other workplace issues.

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