Providing Incentives Can Be “Taxing”

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Employers should not overlook the income tax reporting and withholding compliance issues when providing incentives, rewards, bonuses – whether for vaccination, holiday gifts, safety programs, attendance, and the like. The calculation of overtime pay could be impacted as well.

Tax Compliance

Under the Tax Code (Section 132(a)(4)), *de minimis benefits* are excluded from taxation. A *de minimis benefit* is one which is so small, considering its value and the frequency with which it is provided, as to make accounting for it unreasonable or impractical. Examples provide by the IRS include: controlled, occasional employee use of a photocopier; occasional snacks, coffee, doughnuts, etc.; occasional tickets for entertainment events; holiday gifts; occasional meal money or transportation expense for working overtime; flowers, fruit, books, etc., provided under special circumstances; and personal use of a cell phone provided by an employer primarily for business purposes.

The IRS says that an employer should always consider the frequency and value of item when making a judgment regarding a *de minimis benefit*. Importantly, the IRS states that an essential element of a de minimis benefit is that it is occasional or unusual in frequency and it must not be a form of disguised compensation. Items exceeding $100 in value cannot be considered *de minimis* under any circumstance according to an IRS ruling.

Importantly, payments of cash and cash equivalents are usually considered a wage as there is no administrative burden to account for a wage payment, according to the IRS. That said, the IRS does allow for the occasional meal / transportation payment for an employee’s unusual and occasional overtime. Consider also that gift cards and gift certificates are considered “cash equivalent” items so are never considered *de minimis benefits*. Most often, gift cards and certificates that are redeemable for general merchandise or have a cash equivalent value are not *de minimis benefits* and are taxable. However, gift cards and certificates that allow employees to receive a specific item of personal property that is minimal in value, provided infrequently, and is administratively impractical to account for, should be excludable as a *de minimis benefit*.

FLSA Compliance

When providing these types of incentives, Employers often overlook this important consideration: if the incentive is a taxable wage (because it is not a *de minimis benefit*), the amount taxable should be considered in the employees' regular rate of pay for the period the incentive is provided. As a result, the taxable amount will increase the overtime rate of pay for non-exempt employees receiving a taxable incentive.