

**Division of Accounting
Payroll Compliance Group**

**Bulletin # 2012-002
Awards**

INTRODUCTION

The Division of Accounting (DOA) is responsible for working with State of Delaware (State) Organizations to ensure appropriate application of regulations associated with fringe benefits offered to State employees.

This bulletin provides guidance on the tax implications of gifts, prizes and awards made to employees to ensure that proper communication is given to the employee at the time of receipt and that the State is in compliance with federal and state tax laws and regulations. Unless a specific IRS exemption applies, all payments made from state funds or items of value given to employees are considered compensation, and are subject to federal, state, and local (if applicable) income tax and associated OECs

FACTS

DEFINITIONS

- **Awards** – Given for years of service, career achievements, completing a program (Delawell), recognition events, holiday celebrations, employee/teacher of the year, the Delaware Award for Excellence and Commitment in State Service program, etc.
- **De Minimis Fringe Benefit** – any property or service whose value is so small as to make accounting for it unreasonable or administratively impractical.
 - De minimis fringe benefits are excluded from taxable income
 - Federal and State regulations do not set a defined amount for the nominal value
 - Even items of little individual value do not qualify as de minimis if they are given frequently to the same person
- **Cash Equivalent Awards** – any item that could easily be exchanged for cash, or used like cash to make purchases.
 - Cash equivalent awards do not qualify as a de minimis fringe benefit
 - Any item that can be readily converted to cash, (i.e., savings bonds, gift cards, etc.)
 - Cash equivalent awards are never excludable from taxes
- **Cash Awards:** Monetary awards are always taxable and include:
 - Those paid by any negotiable instrument (i.e., cash, check, money order, etc.)
- **Non-cash Awards:** Non-cash recognition awards may or may not be taxable and include, but not limited to:
 - Plaques; trophies; certificates
 - Pencils, pens and desk items; cups and mugs
 - Personal items of clothing such as caps, shirts, and sweatshirts
 - Other items such as pins and timepieces

- **Fair Market Value (FMV)** – the amount an individual would have to pay for the particular fringe benefit in an arm’s-length transaction. IRS Reg (§1.61-21(b)(1))
 - FMV is determined on the basis of all the facts and circumstances
 - Any special relationship between the employer and employee is not considered
 - An employee’s subjective perception of the value of a benefit is not relevant
 - The cost incurred by the employer is not considered in determining FMV

- **Gross Up** – paying a full amount without any deductions.
 - A calculation to include taxes on an award in the amount of the award
 - Advise the employee that the calculation is based on the W-4 information current as of the date of issue of the award

FINDINGS

To determine if awards are excludable from wages, employers must consider general fringe benefit rules as well as regulations included in the Internal Revenue Code.

REGULATORY REFERENCES

In rendering this opinion, we reviewed the applicable Code, Regulations, and laws as cited below.

INTERNAL REVENUE SERVICE

IRS Publication 15b and the Taxable Fringe Benefits Guide

Non-taxable Awards – The Internal Revenue Code (IRC) provides exceptions for certain awards, prizes and gifts made to employees. Examples include:

- **De minimis Award** – any award that fits the definition above such as occasional parties/picnics, items with a low FMV, refreshments, turkeys, flowers, theater tickets, etc., are not taxable to the employee. The State may reward an employee’s noteworthy, work-related accomplishments by presenting an item of tangible personal property, such as, a plaque or a memento without tax consequences provided the value of the item, in addition to other gifts, prizes or awards presented throughout the year to the employee, is less than \$100.

NOTE: Non-cash gifts, prizes or awards with a total value at more than \$100 are taxable beginning with the first dollar.

- **Achievement Awards**
 - The maximum amount of excludable awards to a single employee during the calendar year is limited to:
 - \$400 for awards made under a non-qualified plan, or
 - \$1600 in total for awards made under both qualified and non-qualified plans
 - **Qualified Plan Award** – an award is a qualified plan award if it is:
 - made under an established written plan, and
 - does not discriminate in favor of highly paid employees
 - the **average cost** of **all** employee achievement awards (both qualified and non-qualified awards for length of service and safety) made by the employer during a single year does not exceed \$400. Awards of \$50 or less are not included in computing the average. *Reg. § 1.274-8(c)(5); IRC §414(q)(1); Reg. §1.274-8(c)(5)*

- **Safety Achievement Award** – recognizes an employee’s accomplishments for maintaining or promoting defined safety standards; it may qualify for exclusion from taxation; if the award,
 - is limited annually to less than 10% of total eligible employees
 - is not presented to managers, administrators, or professional employees

- **Length of Service Award** – an in-kind gift for an employee as part of an employee achievement event may qualify as a non-taxable benefit (i.e., \$200 plaque); if,
 - the employee has at least five years of service with the State
 - the employee has not received a length of service award within the last five years
 - the awards are presented as part of a meaningful ceremony and are not given based on an employee’s classification

- **Retirement Award** – may qualify for exclusion from taxation
 - Requires documentation describing the relationship between the retiree's length of service and the value of the award
 - Traditional retirement gifts are treated separately from achievement awards, they may be given within the five year period required for other length of service awards

- **Sympathy Gifts** – for a recent death or major illness (i.e., flowers, cards)
- **Redemption Coupons** – a substitute for a specified item at a designated store. It can only be redeemed at the specified store; and, only for the specified item (i.e., holiday turkey). Such coupons are not cash equivalents because of the very limited way they must be redeemed. This is not a taxable fringe benefit assuming the benefit is provided infrequently (i.e., once a year) and meets the de minimis criteria explained above.

Taxable Awards – add value to the employees’ earnings in PHRST for W2 reporting.

- **Constructive Receipt**
 - The taxable amount of an award is reported in the calendar year the employee receives the award even if the award program is based on a fiscal year.
 - All taxable awards must be included in the employee’s wages at the time award is received by the employee; but, no later than the last check of the calendar year.

- **Non-de minimis Awards** – items with a high FMV

- **Cash Equivalent Awards** – do not qualify as a de minimis fringe benefit because they have a defined face value, and may be used like or converted to cash; therefore, they are never excludable from taxes. (i.e., gift cards, gift certificates, and savings bonds)

- **Savings Bonds** – The Bond is a cash equivalent award because it has a defined face value; however, the face value is not its actual value until it reaches maturity. The FMV of the Bond (usually the cost of the Bond) when it is given to the employee is the taxable amount.

- **Employee Choice** – If employees have considerable choice in selecting the item received as a non-cash award, the award rarely meets the conditions for de minimis, regardless of its FMV.
 - Offering significant choice is the same as giving a cash-equivalent gift certificate.
 - Catalog programs that give employees a wide choice within specified limits, such as color-coded categories where all the items are about the same value, are equivalent to giving a gift certificate even if the employee cannot get the excess amount of award credit if he or she chooses an item from a lower value category.
 - Tax liability is based on the value of the highest award category that the employee is eligible to choose from, regardless of which category is selected.
 - Cash equivalence is based on the FMV of the item, not the cost to the employer.
 - The FMV of the selected item or, if higher, the FMV of the category from which the employee was eligible to choose, is the amount reported as a taxable.

DELAWARE CODE

N/A

OTHER

State of Delaware Policy:

Funding Sources – The funding charged for awards must be appropriate and not create any questionable or disallowed charges. Awards must not be charged to a grant.

Reporting Taxable Awards

- Employees must be advised of the pay period the award will be reported in the PHRST system as the taxes withheld on the reported benefit will reduce the employee's net income that pay period.
- Cash gifts, prizes or awards, including gift certificates and gift cards (cash equivalents),
 - are considered supplemental wages (i.e., additional compensation)
 - are reportable as taxable, regardless of the dollar amount, beginning with the first dollar
 - must be reported in the PHRST Payroll system and are subject to federal, state and local (if applicable) income tax as well as OECs (OASDI, Medicare, Pension, etc.).
- OECs are determined through eligibility criteria associated with the Position.
- The taxable value of the gift, prize or award is included in the employee's W2.

TAX ADVICE DISCLAIMER

Although the opinion provided here is presented in good faith and believed to be correct, it is General in nature and is not intended as tax advice. Furthermore, the facts and regulatory references applicable to this scenario may not be applicable to or suitable for other similar scenarios that may require consideration of other factors.

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