

Division of Accounting Payroll Compliance Group

Awards Bulletin

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 employee gifts, prizes and awards to ensure that employers provide proper communication to the employee at the time of receipt, and that the State complies with federal and state tax laws and regulations. Unless a specific Internal Revenue Service (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 other employment costs (OECs)

DEFINITIONS

- **Awards:** Given for years of service, career achievements, completing a program, recognition events, holiday celebrations, employee/teacher of the year, the Governor's Team Excellence Award 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.
 - 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):** Amount an individual would have to pay for the particular fringe benefit in an arm's-length transaction. FMS is determined on the basis of all facts and circumstances. IRS Reg (§1.61-21(b)(1))
 - 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.
 - Calculation includes taxes on an award in the amount of the award.
 - Employee notified 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 (IRC).

REGULATORY REFERENCES

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

IRS Publication 15-B, Employer's Tax Guide to Fringe Benefits Publication 5137, Fringe Benefit Guide

Except for the three situations noted, prizes or awards given to employees are taxable.

Three types of non-cash awards may be excluded from income (subject to dollar limitations). Each category has specific requirements to be excludable. These categories are:

- Certain employee achievement awards
- Certain prizes or awards transferred to charities
- De minimis awards and prizes

1. Employee Achievement Awards

The following requirements must be met for an achievement award to be excludable:

- Must be given for length of service or safety; and
- Must be awarded as part of a meaningful presentation; and
- Cannot be disguised wages, or made under conditions and circumstances that create a significant likelihood that it is disguised wages.

The amount of an award that is excludable depends on whether it is considered qualified. 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 § J .274- 8(c)(5); IRC §414(q)(J); Reg § J .274-8(c)(5)

- o **Safety Achievement Award** – recognizes an employee’s accomplishments for maintaining or promoting defined safety standards; may qualify for an 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
- o **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 if:
 - employee has at least five years of service with the State (a traditional retirement award is an exception to the five year rule)
 - employee has not received a length of service award within the last five years
 - awards are presented as part of a meaningful ceremony and are not given based on an employee's classification
- o **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
 - \$1,600 in total for awards made under both qualified and nonqualified plans

2. Prizes or Awards Transferred to Charities

- Certain prizes and awards given in recognition of charitable, scientific, artistic or educational achievement are not taxable if the recipient transfers them to a charitable organization. IRC §74(b)
- The following requirements must apply for a transferred award to be excludable from wages:
 - Award is for achievement
 - Recipient is selected without entering any contest
 - No substantial future services are required
 - Recipient transfers the award to a charitable organization recognized under IRC §170(c) prior to receiving the benefit

3. De Minimis Awards and Prizes

- Prize or award that is not cash or cash equivalent, of nominal value, and provided infrequently is excludable from an employee’s wages.
- Examples of excludable De Minimis Awards:
 - Nominal gifts for birthdays, holidays
 - Holiday turkey and hams
 - Flowers, plaques, coffee mugs for special occasions

Taxable Awards – add value to the employees’ earnings in PHRST for W-2 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.

OTHER

State of Delaware Policy:

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

The Delaware Department of Human Resources provides further guidance on recognition programs at <https://dhr.delaware.gov/training/award/>.

Reporting Taxable Awards

- Employees must be advised of the pay period the award will be reported in 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 W-2.

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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