Notice 89-110

Fringe Benefit Guidance

1989-2 C.B. 447

December 4, 1989

PURPOSE

This notice provides guidance to employers and employees concerning the 1989 recordkeeping and reporting requirements for certain fringe benefit items.

BACKGROUND

Final Income Tax Regulations relating to sections 61 and 132 of the Internal Revenue Code (the Code) were published in the Federal Register on July 6, 1989. In general, these rules apply to benefits paid on or after January 1, 1989. Because employers and employees may not have appropriate records or the necessary data to comply with some of the reporting requirements contained in these regulations for 1989, this notice provides special rules with respect to employer-provided dependent group-term life insurance, the annual lease value of an employer-provided vehicle, the valuation of employer-paid fuel, the use of the commuting valuation rule by certain control employees, and reimbursements for public transit commuting expenses.

DEPENDENT GROUP-TERM LIFE INSURANCE

Under section 1.132-6(e)(2) of the regulations, the cost of employer-provided group-term life insurance on the life of the spouse or dependent of an employee is not excludible from gross income as a de minimis fringe. The effective date of this provision as it relates to such insurance is postponed until further notice.

In addition, effective January 1, 1989, and until further notice, the following rules shall apply under section 132(e) of the Code: (1) if the face amount of employer-provided group-term life insurance payable on the death of a spouse or dependent of an employee does not exceed $2,000, such insurance shall be deemed to be de minimis fringe benefit; and (2) in determining whether employer-provided dependent group-term life insurance with a higher face amount is a de minimis fringe benefit, only the excess (if any) of the cost of such insurance over the amount paid for the insurance by the employee on an after-tax basis shall be taken into account. Finally, section 1.61-2(d)(2)(ii)(b) of the regulations is clarified to provide that the cost of employer-provided dependent group-term life insurance is not includible in gross income under that section of the regulations (regardless of whether section 132(e) of the Code applies) to the extent such cost is paid by the employee on an after-tax basis. For purposes of this paragraph, the cost of insurance shall be determined under section 1.79-3(d)(2) of the regulations.

Section 1.125-2, Q&A-4(d) of the proposed regulations provides that benefits of the type described in section 132 of the Code do not constitute qualified benefits or cash, and thus may not be included in a cafeteria plan regardless of whether any such benefits are purchased with after-tax employee contributions or on any other basis. For plan years ending on or before December 31, 1991, this provision will not be considered violated if employer-provided dependent group-term life insurance is included in a cafeteria plan provided that it is treated as cash under section 1.125-2, Q&A-4(b) of the proposed regulations regardless of whether it is eligible for exclusion under section 132 of the Code. After this period, employer-provided dependent group-term life insurance cannot be included in a cafeteria plan without violating section 1.125-2, Q&A-4(d) if such benefit would also be eligible for exclusion under section 132 if offered outside a cafeteria plan. As is true of employer-provided group-term life insurance on the life of the employee in excess of the dollar limit of section 79 that is offered under a cafeteria plan, the total amount includible in the gross income of an employee who receives such insurance under a cafeteria plan is the greater of the employee's contributions toward the purchase of the insurance or the cost (determined under section 1.79-3(d)(2) of the regulations) of the insurance.

ANNUAL LEASE VALUE OF AN EMPLOYER-PROVIDED VEHICLE

The regulations provide several methods for determining the value of an employer-provided vehicle, including the automobile lease valuation rule, the vehicle cents-per-mile rule, and the commuting valuation rule. The rules contained in section 1.61-21(c)(3)(ii) of the regulations require than an employer who elects to use a special valuation rule must notify the employee of the election by the later of January 31 of the calendar year for which the election is to apply, October 31 for calendar year 1989 or 30 days after the employer first provides the benefit to the employee.

This notice provides employers who use the automobile lease valuation rule with an additional safe harbor method for computing fair market value. Beginning with vehicles provided (or deemed provided under Announcement 85-113, 1985-31 I.R.B. 31) after December 31, 1988, for vehicles that are leased by an employer, the employer will be permitted to use the manufacturer's invoice price (including options) plus 4% as a safe harbor estimation of fair market value for all purposes under section 1.61-21(d)(5)(ii) of the final regulations. This safe harbor method is available under further notice and regardless of whether the employer also manufactures the vehicle.

Section 1.61-21(d)(5)(ii)(C) of the regulations provides that for an automobile leased but not manufactured by an employer, the safe-harbor value of the automobile is either the manufacturer's suggested retail price less eight percent (including sales tax, title, and other expenses attributable to such purchase), or the retail value of such automobile as reported by a nationally recognized pricing source. For calendar year 1989, and until further notice, this safe harbor is to be applied as if the language "but not manufactured" were deleted. This change enables manufacturers and their affiliates to take advantage of this safe harbor method.

The consistency rules in sections 1.61-21(d)(7) and 1.61-21(e)(5) of the final regulations and sections 1.61-2T(d)(6)(iv) and 1.61-2T(e)(5)(ii) of the proposed and temporary regulations generally require that an employer that has elected to use a special valuation method with respect to a vehicle must continue to use this method in subsequent years. Implementation of the final regulations (or this notice) generally does not entitle employers to change valuation methods elected under the proposed and temporary regulations.

An exception is hereby provided, however, in the case of employers that properly elected to use a special valuation method other than the vehicle cents-per-mile valuation rule with respect to a vehicle, either for the first time or as permitted under the consistency rules, because its value exceeded the applicable limitation in section 1.61-21(e)(1)(iii) of the final regulations or in section 1.61-2T(e)(1)(iii) of the proposed and temporary regulations. Such employers will not be considered in violation of the consistency rules if they properly elect to use the vehicle cents-per-mile valuation rule with respect to the vehicle, and its value would not have exceeded the applicable limits in those sections when the initial election was made if the additional safe harbor valuation rules in section 1.61-21(d)(5)(ii) of the final regulations and this notice had been available at that time. In addition, if this change of election is made with respect to calendar year 1989, the date of the required notice under section 1.61-2(c)(3)(ii) of the final regulations is postponed until December 31, 1989.

VALUATION OF EMPLOYER-PAID FUEL

In general, the final regulations provide three approaches to valuing employer-paid fuel based on: (1) the actual cost of the fuel to the employer; (2) a value of 5 1/2 cents per personal mile driven; and (3) the fleet-average cents-per-mile fuel cost of a representative sample (at least 10%) of qualifying cars in the fleet. Option (2) is available only if either (a) the fuel is provided in kind, or (b) the fair market value of the vehicle is determined by the fleet-average method and determining the amount of the actual reimbursement or the amount charged for the purchase of fuel would impose unreasonable administrative burdens on the employer. Option (3) is available only for vehicles valued at $16,800 or less. Under this notice, effective for 1990, and prior calendar years, option (2) may be used regardless of whether the fuel was provided in kind or the value of the vehicle was determined under the fleet average method.

COMMUTING VALUATION RULE AND CERTAIN CONTROL EMPLOYEES

Under section 1.61-21(f)(5)(iii) of the regulations, non-government employees whose compensation equals or exceeds $100,000 are considered control employees. For government employees, section 1.61-21(f)(6)(ii) of the regulations provides that a control employee is one whose compensation equals or exceeds $75,500. Pursuant to section 1.61-21(f)(1)(v) of the regulations, control employees are not permitted to use the $1.50 commuting valuation rule.

This notice permits an employee who is considered a control employee solely because his or her compensation equals or exceeds the applicable amount listed above to use the $1.50 commuting valuation rule from January 1, 1989, through December 31, 1989.

In the case of an employer that uses the special accounting period provided in Announcement 85-113, 1985-31 I.R.B. 31, an employee whose compensation exceeds the applicable limit provided in section 1.61-21(f)(5)(i) or (iii) of the regulations may use the $1.50 commuting valuation rule until the first day of such special accounting period beginning after December 31, 1989.

REIMBURSEMENTS FOR PUBLIC TRANSIT COMMUTING EXPENSES

Section 531(a) of the Deficit Reduction Act of 1984 (Act) (Public Law 98-369, 1984-3 (Vol. 1) C.B. 386) added section 132(e) to the Code to provide an exclusion from gross income for de minimis fringes. The legislative history to this Act specifically lists monthly transit passes provided at a discount not exceeding $15 as an example of a de minimis fringe. (H.R. Rep. No. 861, 98th Cong., 2d Sess. 1168 (1984), 1984-3 (Vol. 2) C.B. 422). This exclusion was clarified by the Senate Finance Committee Report to the Tax Reform Act of 1986 (S. Rep. No. 313, 99th Cong., 2d Sess. 1026 (1986)) to indicate that the de minimis fringe benefit exclusion includes tokens, vouchers, and reimbursements to cover the costs of commuting by public transit, as long as the amount of such reimbursement, etc., provided by the employer does not exceed $15 a month ($180 a year). This report also states that the value of all such transit benefits (including any discounts on passes) furnished to the same individual are aggregated for purposes of determining whether the $15 limit is reached.

The final section 132 regulations do not include reimbursements of transit costs as a de minimis fringe. In order to comport with legislative intent, this notice provides that reimbursements made by an employer to an employee under a bona fide reimbursement arrangement to cover the cost of commuting on a public transit system will be excludible as a de minimis fringe provided that the employee does not receive more than $15 in such reimbursements with respect to commuting costs paid in any given month. For purposes of this rule, the $15 limit shall be reduced, but not below zero, by the amount of any in-kind public transit commuting benefits provided during such month that are excludible from gross income as a de minimis fringe under section 1.132-6(d)(1) of the regulations. This rule applies to any reimbursements paid (or deemed paid under Announcement 85-113) after December 31, 1988, and is available until further notice.

COMMENTS REQUESTED

The Internal Revenue Service invites comments concerning other fringe benefit items for which immediate guidance may be necessary to facilitate reporting on Form W-2 for the 1989 tax year.

Written comments should be sent to the Internal Revenue Service, Office of the Assistant Chief Counsel (Employee Benefits and Exempt Organizations), Branch 2, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044.

RELIANCE

This document serves as an "administrative pronouncement" as that term is described in section 1.6661-3(b)(2) of the Income Tax Regulations, and may be relied upon to the same extent as a revenue ruling or revenue procedure.

DRAFTING INFORMATION

The principal author of this notice is Janet S. Lloyd of the Office of the Assistant Chief Counsel (Employee Benefits and Exempt Organizations). For further information regarding this notice, contact Mrs. Lloyd on (202) 566-4747 (not a toll-free call).