

Cafeteria Plans

Cafeteria Plans are employer sponsored employee benefit plans that allow employees to elect benefits on a pre-tax basis. Thereby ensuring that employees and employers save taxes. Congress legally provided for Cafeteria Plans in 1978 under IRS Code Section 125. They are also referred to as Flexible Benefit Plans or Section 125 Plans.

Generally, qualified benefits under a cafeteria plan are not subject to FICA, FUTA, Medicare tax, or income tax withholding. If an employee elects to receive cash instead of any qualified benefit, it is treated as wages subject to all employment taxes. For more information, see [Publication 535](#), Chapter 5 or [Publication 15-A](#).

How does a cafeteria plan work?

Code section 125 makes it possible for employers to offer their employees a choice between cash salary and a variety of nontaxable benefits (qualified benefits).

A qualified benefit is a benefit that does not defer compensation and is excludable from an employee's gross income under a specific provision of the Code, without being subject to the principles of constructive receipt. Qualified benefits include health care, vision and dental care, group-term life insurance, disability, adoption assistance and certain other benefits. See Sections 125(a), 125(f), 79, 105, 106, 129 and 137 of the Code.

Employers may also offer flexible spending accounts to employees under a cafeteria plan that provides coverage under which specified, incurred expenses may be reimbursed. These include health flexible spending accounts for expenses not reimbursed under any other health plan and dependent care assistance programs.

The above discussion provides only the most basic rules governing a cafeteria plan. For a complete understanding of the rules, see the proposed and final regulations under Code section 125.

Cash in lieu of insurance – is this subject to IPERS?

The cafeteria plan must be reviewed by IPERS to determine if the cash in lieu of insurance is IPERS qualified. Each benefit plan must be evaluated individually. Generally, the tax treatment is Gross plus the additional cash is used calculate IPERS withholding and employer share of IPERS. If any deduction is made for a qualified health care plan (Section 125), some life insurance and/or disability insurance plans are exempt from Social Security, Medicare, Federal taxes and State taxes. The deduction for IPERS is only exempt from Federal and State Taxes, NOT Social Security and Medicare. Deductions made for some disability insurance and qualified IRAs are exempt only for Federal and State taxes.

When is cash in lieu of insurance not IPERS qualified?

- 1) Cash in lieu of insurance is not part of a formal Cafeteria Plan
- 2) The benefit provided are different for each employee
- 3) The benefit is offered to some employees, but not all employees.
- 4) Other as determined by IPERS

Any of these situations would make it not IPERS qualified. The additional cash would be taxed for Social Security, Medicare, Federal and State taxes.

The Walker Agency has put together a cafeteria plan that allows a county office to administer their own cafeteria plan. Bob Walker offers a Section 125 Health Care, Dependent Care, a Medical Spending Plan and IRA. In many counties the extension council contributes additional money to the employee to help pay for the plan. The employee elects participation in the item(s) in the plan that benefits them. Additional cash contributed to the employee in this plan is IPERS qualified. Deductions made for Healthcare, Medical Spending and Dependent Care elections in this plan are all exempt from Social Security, Medicare, Federal and State Taxes, but NOT for IPERS. The deduction for IRA election in this plan is exempt only for Federal and State Taxes. There is an upfront fee to the extension district for this plan. The county extension district administers their own Medical Spending Plan by withholding dollars from employees pay, holding it in a liability account until the employee document qualified expenses and it is paid out. The anniversary date on the Medical Spending Plan is the end of the fiscal year, so that the Medical Spending Liability Account goes to zero taking it back to cash basis for year end reporting.

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