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Why Every Company Should Consider a Section 125 Cafeteria Plan



By Joseph W Tucciarone, CEO National Network of Accountants

For many businesses today, employee benefits—especially healthcare—have become one of the largest and least controllable expenses on the balance sheet. Premiums continue to rise year after year, claims experience often feels disconnected from cost increases, and employers are under constant pressure to improve compensation, retention, and morale without eroding profitability.

Yet one of the most effective tools available to employers is also one of the most underutilized: the **Section 125 Cafeteria Plan**.

A properly designed Section 125 plan doesn't replace your existing health insurance. Instead, it works **alongside** your current program to reduce payroll taxes, increase employee take-home pay, and improve overall benefit efficiency—without increasing out-of-pocket costs for the employer.

What Is a Section 125 Cafeteria Plan?

A Section 125 Cafeteria Plan is an IRS-approved benefit structure that allows employees to pay for certain qualified benefits on a **pre-tax basis**. This means employees can allocate a portion of their wages before

federal income tax, Social Security, Medicare, and in most cases state taxes are applied.

For employers, this creates an immediate and measurable benefit: **lower payroll tax liability**.

When employees elect pre-tax benefits under a Section 125 plan, employers no longer pay the employer portion of FICA taxes on those wages. That reduction flows directly to the company's bottom line.

Lower Costs Without Cutting Benefits

Most companies assume that controlling benefit costs means reducing coverage, increasing deductibles, or shifting costs to employees. Section 125 plans take a different approach.

By restructuring how benefits are funded—not what benefits are offered—companies can:

- Reduce total payroll tax expense
- Improve net employee compensation
- Maintain or enhance benefit offerings
- Avoid disrupting existing insurance relationships

In many cases, employers can use the FICA tax savings to offset benefit enhancements, reinvest in the business, or improve cash flow—without increasing overall spend.

A Win for Employees: More Take-Home Pay

Employees feel the impact of a Section 125 plan immediately. Because contributions are made pre-tax, employees see higher net pay without asking for a raise.

In an environment where wage inflation is high and talent retention is critical, this matters. Employees are increasingly focused on what lands in their bank account—not just gross salary. A Section 125 plan helps bridge that gap in a tax-efficient way.

The result is a benefit employees actually notice, understand, and appreciate.

A Strategic Tool for Retention and Recruitment

Benefits are no longer a “nice to have.” They are a competitive necessity.

Companies that leverage Section 125 plans can position themselves as proactive, employee-focused employers—without increasing benefit budgets. This can be especially impactful for small and mid-sized businesses competing with larger organizations that appear to have deeper pockets.

When communicated properly, a Section 125 plan reinforces the message that the employer is intentionally managing costs while still prioritizing employee well-being.

Compliance Matters—and It Works When Done Correctly

Section 125 plans have been part of the tax code for decades. They are not aggressive, experimental, or new. However, compliance is critical.

Plans must be properly documented, nondiscrimination rules must be followed, and implementation must align with IRS guidelines. When structured and administered correctly, Section 125 plans are fully compliant and well-established.

This is why coordination between employers, CPAs, and benefit advisors is essential. When everyone understands the mechanics and objectives, the plan becomes a powerful planning tool rather than just another benefit line item.

Why CPAs and Advisors Care

From an advisory perspective, Section 125 plans check all the right boxes:

- Immediate tax savings
- Predictable outcomes
- Minimal disruption
- High client value perception

For business clients struggling with rising healthcare costs, compressed margins, and employee retention challenges, Section 125 plans offer a practical, compliant solution that can be implemented quickly.

It’s not about replacing what already works. It’s about **making existing systems work better together.**

The Bottom Line

In a time when businesses are being asked to do more with less, ignoring proven tax-advantaged strategies is no longer an option.

A Section 125 Cafeteria Plan allows companies to lower payroll taxes, increase employee take-home pay, strengthen benefits, and improve profitability—all at the same time.

That’s not a loophole. It’s smart planning.

And for companies looking to stabilize costs while supporting their workforce, it’s a strategy worth serious consideration.



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