

# POINTS TO REMEMBER

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## CREATIVE BENEFITS

by *Dianne Bennett, Buffalo, NY*

**F**rom hammocks in quiet rooms (People Support) to paid dry cleaning, safe deposit boxes (First Union) to car seats for new parents (Allstate), bring your parents to work day (e-services company Organic) to pet health insurance (1% of companies surveyed), corporate America is trying to woo and retain X Generation and Next Generation employees in a market where the competition for talent has become fiercer than the competition for clients. Even Disney relaxed its 43-year ban on facial hair. But the glitz is less important than the substance. What employees really want, even more than money, according to numerous surveys, is opportunity for promotion, challenging work, and feedback—in any order. A very recent survey of call-center employees had them ranking wages fifth. Appreciation came first, and then feeling "in" on things, supervisors with an understanding attitude, and job security.

Most law firms can't compete with the campus in the modern business world that supplies medical centers, fitness centers, on-site day care and even nap and game rooms (try the Monster Den at Monster.com). But

there are some changes law firms can make in their employee benefits programs. They can get more creative about vacation, sick and personal days—wrapping them into one program. In addition, employees are demanding more vacation time earlier in their tenure at firms, and quicker access to programs like 401(k) plans. These programs cost money, but if they help reduce costly turnover, they will prove cost-effective in the long run. At a recent ABA Tax Section meeting, the IRS was receptive to listening to proposed changes in their rules that will make it less burdensome for firms to provide instant entry into 401(k) plans.

Try a cappuccino bar, or a coffee grinding room, and lots of free snacks, say some companies. Or things as simple as free flu shots, which should pay off in terms of healthier employees and less sick time. All of these "perks" should fit under the Code's already outdated (coffee and doughnuts probably need to be replaced with grinding rooms and cappuccinos) section 132 on fringe benefits, and the lengthy regulations under that section. The "working condition fringe" in section 132(d) and regulation section 1.132-5, and "de minimis fringes" in section 132(e) and regulation section 1.132-6 provide most of the tax exclusions for employees. The IRS would be wise not to be too rigid as companies expand the perks they are offering. They should have learned their lesson from trying to tax frequent flyer miles and attempting to cut off kidnapped child exemptions.

The basic premise to the working condition fringe is that the expense would be deductible (without taking into account limits) under section 162 if the employee had purchased the product or service. An employer expanding its perks in this field should check carefully, for example, the provisions on cash reimbursements and the special rules under

regulation section 1.132-5(a), and the rules for employer-provided home computers, because they are "listed property" under section 280F.

Appreciation—the number one employee motivator described above—sometimes is doled out as simply as passes to movies and sporting event tickets. As long as these are not season passes, they fall under the nontaxable category of de minimis fringe benefits specifically graced in regulation section 1.132-6(e). Employers going the full route of employee achievement awards need to keep in mind both the nontaxable (for the employee) and deductibility (for the employer) limitations under sections 74(c) and 274(j).

Almost all companies have some sort of arrangement for discounts these days—whether to regional restaurants or movie theaters or fitness centers. The discount program is expanding rapidly, with companies signing on for substantial discounts for products and services, many provided online, such as through [realperks.com](http://realperks.com). The Internet makes discounting much easier. There should be no income tax effects to the employees if there is no cost to the employer. If the employer is providing some of its own goods and services at a discount, the "no additional cost" provisions of section 132(b) should be applied to determine if the discounts are nontaxable. See section 132(c) and the regulations for "qualified employee discounts" under section 1.132-3 as well. Benefits to spouses and dependent children are tax-free in these two categories, under section 132(h), but benefits provided to spouses and dependent children otherwise are taxable to the employee.

A company considered one of the best to work for, Lexmark International, Inc., headquartered in Lexington, Kentucky, gives employees \$2,500 within five years of retire-

ment to retrain for another career, work on a hobby, or travel. The company also provides up to \$2,500 for supplies for employees with children with special needs and for adoption fees. The first item would be taxable to the employee, unless the tuition fell under a section 127 educational assistance plan. The adoption reimbursements should be non-taxable if they fit within section 137, and the supplies could qualify as tax-free under a cafeteria or health plan (sections 125 and 105).

Education outside the workplace—tuition reimbursement programs that are tax-free if certain basic requirements are met under section 127—are gaining in popularity. Some companies are providing tuition for children of employees. These are taxable, but better than paying with tax-paid dollars of one's own.

In-house education is growing in importance as well. Some of the training is outside the traditional box of law and management, but most is not. Employees rightly see this as helping their own personal and professional development, a firm commitment to them as people—no matter where they end up. And, in helping them be more marketable, the firm somewhat counter-intuitively is helping bind them to the firm. Here, too, the tax issues may get tricky with training not related to law itself, but between the section 127 plan and the section 132 working condition fringes, the training should be tax-free to the employee. If the training does not fit into one of these two categories, it is taxable. See section 132(j)(8).

Family friendly is not appealing just to women. Almost the same percentage of men (82%) as women (85%) in the 20-39 age group place family time at the top of their work priority issues, according to a study this year by the Radcliffe Public Policy Center. The U.S. Census Bureau this year noted that for the

first time since it started keeping track, more than half of married-couple families with wives of childbearing age had children and had both parents in the workforce. Law firms that provide flex-time schedules, telecommuting, and family leaves are likely to retain their associates and employees more than ones that do not. (Family friendly may not sit well with all employees. Something of a backlash has developed among employees without children. The movement “No Kidding!” has more than 50 chapters, to try to deal with, as they call it, a “procreation-crazed” America.)

High billables and the stress of work overall may be part of the trend toward providing home services from work. More companies are providing concierge-type services, such as dry cleaning, shoeshines and car detailing, from work. And the trend now seems to be to provide it through the Internet, with specially designed company portals, such as those sold by Abilizer (formerly perksatwork.com). There also seems to be little doubt why Salomon Smith Barney in London provides gourmet meals, fresh underwear and free toothbrushes to those who work past 7 p.m. Again, given the circumstances, these items should not be taxable to the employee.

This year's survey by the Society of Human Resource Managers (SHRM) of 600 HR managers showed some cutbacks and slowing in employee perks, especially in costly ones like vacation days and personal time. What employees likely will need most in the coming years is more time off, not less, particularly to care for elderly parents. About 25% of all U.S. households now provide care for their aging relatives. Emergency care—for children or elderly relatives—is the “perk” employees now think they will need the most. According to a Hewitt survey this year, 13% of companies it surveyed provide emergency childcare.

Again, if the company cannot afford to provide the time or the space, it should look for providing the resources to get this care for its employees. In larger cities firms can negotiate with a service provider to provide a certain amount of days or hours of this type of emergency care. Traditional employee assistance programs (EAPs), which in many cases may need to meet certain welfare plan requirements under the Employee Retirement Income Security Act (ERISA) or at least the reporting requirements of section 6039, could and should be used more by firms. National usage is at about 12%; in Seattle it's about 45%—which says something about the younger and more entrepreneurial companies and how they try to keep their workers.

It's cute and it's funny to look at some of the perks being given to employees these days, whether in-firm massages (that reduce stress, so they say) or pets at work (30 out of 1,000 companies surveyed by Wm. M. Mercer Company) that also reduce stress, some say, but the climate of a workplace is extraordinarily important to today's worker, and law firms would do well to remember that.

## CAPITALIZATION VS. EXPENSING: WHAT MORE DO WE KNOW FROM RECENT RULINGS?

*by Annette Nellen, San Jose, CA*

Whether an expenditure should be capitalized or currently expensed has been a difficult determination under the tax law for decades. Since 1992 when the U.S. Supreme Court “clarified” the capitalization versus expensing rule in the *Indopco* decision,<sup>1</sup> practitioners and revenue agents have perhaps been even more perplexed with the question. While there are

<sup>1</sup> *Indopco, Inc. v. Commissioner*, 503 U.S. 79 (1992).