(6) To the National Archives and Records Administration of the United States as a record which has sufficient historical or other value to warrant its continued preservation by the United States Government, or to the Archivist of the United States or his or her designee for evaluation to determine whether the record has such value;

(7) To another agency or to an instrumentality of any government jurisdiction within or under the control of the United States for a civil or criminal law enforcement activity if the activity is authorized by law, and if the head of the agency or instrumentality has made a written request to the agency which maintains the record specifying the particular portion desired and the law enforcement activity for which the record is sought;

(8) To a person pursuant to a showing of compelling circumstances affecting the health or safety of an individual if, upon such disclosure, notification is transmitted to the last known address of such individual;

(9) To either House of Congress or, to the extent of matter within its jurisdiction, any committee or subcommittee thereof, any joint committee of Congress or subcommittee of any such joint committee;

(10) To the Comptroller General, or any of his or her authorized representatives in the course of the performance of the duties of the General Accounting Office;

(11) Pursuant to the order of a court of competent jurisdiction; or

(12) To a consumer reporting agency in accordance with section 3(d) of the Federal Claims Collection Act of 1966 (31 U.S.C. 952(d)). (This "Special Disclosure" statement does not apply to any FDA system of records.)

* * * * *

Dated: December 13, 1985.

Joseph P. Hile,

Associate Commissioner for Regulatory Affairs.

[FR Doc. 85-30202 Filed 12-20-85; 8:45 am]

BILLING CODE 4160-01-M

---

21 CFR Part 178

[Docket No. 81F-0154]

Indirect Food Additives; Adjuvants, Production Aids, and Sanitizers

AGENCY: Food and Drug Administration.

ACTION: Final rule.

SUMMARY: The Food and Drug Administration (FDA) is amending the food additive regulations to provide for the safe use of 1,3,5-tris(4-*tert*-butyl-3-hydroxy-2,6-dimethylbenzyl)-1,3,5-triazine-2,4,6-(1*H*,3*H*,5*H*)-trione as an antioxidant for olefin polymers used in the manufacture of articles or components of articles intended for use in contact with food. This action responds to a petition filed by the American Cyanamid Co.

DATES: Effective December 23, 1985; objections by January 22, 1986.

ADDRESS: Written objections to the Dockets Management Branch (HFA-305), Food and Drug Administration, Rm. 4-62, 5600 Fishers Lane, Rockville, MD 20857.

FOR FURTHER INFORMATION CONTACT: Marvin D. Mack, Center for Food Safety and Applied Nutrition (HFF-335), Food and Drug Administration, 200 C St. SW., Washington, DC 20204, 202-472-5690.

SUPPLEMENTARY INFORMATION: In a notice published in the **Federal Register** of June 5, 1981 (46 FR 30197), FDA announced that a petition (FAP 1B3548) had been filed by the American Cyanamid Co., One Cyanamid Plaza, Wayne, NJ 07470, proposing that § 178.2010 *Antioxidants and/or stabilizers for polymers* (21 CFR 178.2010) be amended to provide for the safe use of 1,3,5-tris(4-*tert*-butyl-3-hydroxy-2,6-dimethylbenzyl)-1,3,5-triazine-2,4,6-(1*H*,3*H*,5*H*)-trione as an antioxidant in polypropylene and high-density polyethylene, without limitation regarding the condition of use.

In an amended notice published in the **Federal Register** of Octobr 10, 1985 (50 FR 41411), FDA announced that the petitioner had amended this petition to provide for the use of this additive in all olefin polymers, including polypropylene and high-density polyethylene, without limitation regarding the conditions of use.

FDA has evaluated data in the petition and other relevant material. It concludes that the additive is safe for use in all olefin polymers, and that the regulations should be amended as set forth below.

In accordance with § 171.1(h) (21 CFR 171.1(h)), the petition and the documents that FDA considered and relied upon in reaching its decision to approve the petition are available for inspection at the Center for Food Safety and Applied Nutrition (address above) by appointment with the information contact person listed above. As provided in 21 CFR 171.1(h), the agency will delete from the documents any materials that are not available for public disclosure before making the documents available for inspection.

The agency has carefully considered the potential environmental effects of this action and has concluded that the action will not have a significant impact on the human environment and that an environmental impact statement is not required. The agency's finding of no significant impact and the evidence supporting that finding may be seen in the Dockets Management Branch (address above) between 9 a.m. and 4 p.m., Monday through Friday. FDA's regulations implementing the National Environmental Policy Act (21 CFR Part 25) have been replaced by a rule published in the **Federal Register** of April 26, 1985 (50 FR 16636, effective July 25, 1985). Under the new rule, an action of this type would require an environmental assessment under 21 CFR 25.31a(a).

Any person who will be adversely affected by this regulation may at any time on or before January 22, 1986, submit to the Dockets Management Branch (address above) written objections thereto and may make a written request for a public hearing on the stated objections. Each objection shall be separately numbered and each numbered objection shall specify with particularity the provision of the regulation to which objection is made. Each numbered objection on which a hearing is requested shall specifically so state; failure to request a hearing for any particular objection shall constitute a waiver of the right to a hearing on that objection. Each numbered objection for which a hearing is requested shall include a detailed description and analysis of the specific factual information intended to be presented in support of the objection in the event that a hearing is held; failure to include such a description and analysis for any particular objection shall constitute a waiver of the right to a hearing on the objection. Three copies of all documents shall be submitted and shall be identified with the docket number found in brackets in the heading of this regulation. Received objections may be seen in the office above between 9 a.m. and 4 p.m., Monday through Friday.

List of Subjects in 21 CFR Part 178

Food additives, Food packaging, Sanitizing solutions.

Therefore, under the Federal Food, Drug, and Cosmetic Act and under authority delegated to the Commissioner of Food and Drugs and redelegated to the Director, Center for Food Safety and Applied Nutrition, Part 178 is amended as follows:

PART 178—INDIRECT FOOD ADDITIVES: ADJUVANTS, PRODUCTION AIDS, AND SANITIZERS

1. The authority citation for 21 CFR Part 178 continues to read as follows:

Authority: Secs. 201(s), 409, 72 Stat. 1784–1788 as amended (21 U.S.C. 321(s), 348); 21 CFR 5.10 and 5.61.

2. In § 178.2010(b) by revising limitation 1 for the item "1,3,5-Tris(4-*tert*-butyl-3-hydroxy-2,6-dimethylbenzyl)-1,3,5-triazine-2,4,6-(1*H*,3*H*,5*H*)-trione" to read as follows:

§ 178.2010 Antioxidants and/or stabilizers for polymers.

* * * * *

(b) * * *

Substances	Limitations
* *	* * *
1,3,5-Tris(4-*tert*-butyl-3-hydroxy-2,6-dimethylbenzyl)-1,3,5-triazine-2,4,6-(1*H*,3*H*,5*H*)-trione (CAS Reg. No. 40601-76-1).	For use only: 1. At levels not to exceed 0.1 percent by weight of olefin polymers complying with § 177.1520 of this chapter, under conditions of use A through H described in table 2 of § 176.170(c) of this chapter.
* *	* * *

Dated: December 12, 1985.

Richard J. Ronk,

Acting Director, Center for Food Safety and Applied Nutrition.

[FR Doc. 85-30201 Filed 12-20-85; 8:45 am]

BILLING CODE 4160-01-M

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Office of the Secretary

24 CFR Part 20

[Docket No. R-85-1240; FR-1349]

Rules of the Board of Contract Appeals

AGENCY: Office of the Secretary, HUD.

ACTION: Notice of announcement of effective date for final rule.

SUMMARY: This notice announces the effective date for the final rule published in the **Federal Register** on November 5, 1985 (50 FR 45910) that revised the procedures of the Department of Housing and Urban Development Board of Contract Appeals. This rule adopted, in substantial part, the Uniform Rules of Procedure for Board of Contract Appeals issued by the Office of Federal Procurement Policy.

The effective date provision of the rule stated that the rule would become effective upon expiration of the first period of 30 calendar days of continuous session of Congress after publication, and announced that future notice of the effectiveness of the rule would be published in the **Federal Register.** Thirty calendar days of continuous session of Congress have expired since the rule was published.

DATE: The effective date for the final rule published November 5, 1985 (50 FR 45910), is December 16, 1985.

FOR FURTHER INFORMATION CONTACT: David T. Anderson, Chairman, Board of Contract Appeals, Room 2158, Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410, telephone (202) 755-0132. (This is not a toll-free number.)

Dated: December 17, 1985.

Grady J. Norris,

Assistant General Counsel for Regulations.

[FR Doc. 85-30230 Filed 12-20-85; 8:45 am]

BILLING CODE 4210-01-M

Office of the Assistant Secretary for Public and Indian Housing

24 CFR Part 990

[Docket No. R-85-1170; FR-1834]

Modification to the Performance Funding System; Correction

AGENCY: Office of the Assistant Secretary for Public and Indian Housing, HUD.

ACTION: Final rule; correction.

SUMMARY: On June 24, 1985, we published an interim rule (50 FR 25951), which added a new paragraph (x) to the definitions section of Part 990, § 990.102. On November 18, 1985, we published a final rule (50 FR 47368), for which an effective date has not yet been announced, which also purported to add a new paragraph (x). This document corrects the latter rule to preserve the definition added by the June rule, to remove the lettered paragraph designations of the definitions, to place the definitions in alphabetical order, and to correct cross references.

In addition, the rule published on November 18, 1985 contained a few references to effectiveness of the revisions for PHA fiscal years commencing January 1, 1986. Because of the Department's statutory obligation to delay effectiveness of its final rules until after 30 continuous days of a session of Congress and the adjournment of Congress in 1985 before the necessary time period, the rule cannot be made effective January 1, 1986. The references to January 1, 1986 are being changed to April 1, 1986, the next date on which PHA fiscal years begin.

DATES: Effective date: The effective date of the rule published on November 18, 1985 (50 FR 47368) as corrected by this document, is April 1, 1986.

FOR FURTHER INFORMATION CONTACT: Sally Warner Watts, Regulations Division, Office of General Counsel, Room 10276, 451 Seventh Street, SW., Washington, DC 20410-0500, telephone (202) 755-7084. (This is not a toll-free number.)

PART 990—[CORRECTED]

Accordingly, 24 CFR Part 990 is corrected as follows:

1. Section 990.102 is corrected to read as follows:

§ 990.102 Definitions.

Allowable Expense Level (AEL). The per unit per month dollar amount of expenses (excluding Utilities and expenses allowed under § 990.108) computed in accordance with § 990.105, which is used to compute the amount of operating subsidy.

Allowable Utilities Consumption Level (AUCL). The amount of Utilities expected to be consumed per unit per month by the PHA during the Requested Budget Year, which is equal to the average amount consumed per unit per month during the Rolling Base Period. After the end of the Requested Budget Year, the AUCL of the utility(ies) used for space hearing will be adjusted by a Change Factor, defined in this section.

Base Year. The PHA's fiscal year immediately preceding its first fiscal year under PFS.

Base Year Expense Level. The expense level (excluding Utilities, audits and certain other items) for the Base Year, computed as provided in § 990.105.

Change Factor. The ratio of the affected PHA fiscal year heating degree days (HDD) divided by the average annual HDD of the Rolling Base Period. (Affected year HDD divided by Rolling Base Period average HDD.)

Current Budget Year. The fiscal year in which the PHA is currently operating.

Formula. The revised formula derived from the actual expenses of the PFS sample group of PHAs, which is used in PFS, as provided in § 990.105, to determine the Formula Expense Level and the Range of each PHA. HUD plans to update the Formula each year to reflect actual costs experienced by the sample group of PHAs.

Formula Expense Level. The per unit per month dollar amount of expenses (excluding Utilities and audits)

computed under the Formula, in accordance with § 990.105.

Heating Degree Days. The annual arithmetic sum of the positive difference (those under 65 degrees) of the average of the lowest and highest daily outside temperatures in degrees Fahrenheit, subtracted from 65 degrees Fahrenheit.

HUD Field Office. The HUD Field Office that has been delegated authority under the United States Housing Act of 1937 to perform functions pertaining to this subpart for the area in which the PHA is located.

Interim Formula. The HUD system, which has been replaced by PFS, for determining the amount of operating subsidy that applied to PHA fiscal years which commenced on or after October 1, 1972, and before April 1, 1975.

Local Inflation Factor. The weighted average percentage increase in local government wages and salaries for the area in which the PHA is located and non-wage expenses based upon the Implicit Price Deflator for State and Local Government Purchases of Goods and Services. This weighted average percentage will be supplied by HUD. HUD anticipates that it will update the Local Inflation Factor each year. This revised Local Inflation Factor is applicable to PHA fiscal years beginning January 1, 1982, and for all fiscal years thereafter.

Operating Budget. The PHA's operating budget and all related documents, as required by HUD, to be submitted in accordance with the Annual Contributions Contract.

Other Income. Income other than dwelling rental income and income from investments, except the following items are excluded: grants and gifts for operations, other than for utility expenses, received from Federal, State and local governments, individuals, or private organizations; amounts charged to tenants for repairs for which the PHA incurs an offsetting expense; and legal fees in connection with eviction proceedings, when those fees are lawfully charged to tenants.

Project. Each project under an Annual Contributions Contract to which PFS is applicable, as provided in § 990.103.

Project Units. All dwelling units of a PHA's Projects.

Projected Operating Income Level. The per unit per month dollar amount of dwelling rental income plus nondwelling income, computed as provided in § 990.109.

Range. $10.31 below to $10.31 above the PHA's Formula Expense Level for the Base Year. The dollar amount is subject to change from time to time by HUD in connection with updating of the Formula. The Range is used in connection with determination of the Allowable Expense Level, as provided in § 990.105, the qualification for transition funding, as provided in § 990.106, and in consideration of requests for adjustments of the Base Year Expense Level under § 990.110.

Requested Budget Year. The budget year (fiscal year) of a PHA following the Current Budget Year.

Rolling Base Period. The 36-month period that ends 12 months before the beginning of the PHA Requested Budget Year, which is used to determine the Allowable Utilities Consumption Level used to compute the Utilities Expense Level.

Transition Funding. Funding for excessively high-cost PHAs, as provided in § 990.106.

Unit Approved for Deprogramming. (a) A dwelling unit for which HUD has approved the PHA's formal request for removal from the PHA's inventory and the Annual Contributions Contract, but for which removal, i.e., deprogramming has not yet been completed, or (b) a nondwelling structure or a dwelling unit used for nondwelling purposes that the PHA has determined will no longer be used for PHA purposes and for which HUD has approved removal from the PHA's inventory and Annual Contributions Contract.

Unit Months Available. Project Units multiplied by the number of months the Project Units are available for occupancy during a given PHA fiscal year. Except as provided in the following sentence, for purposes of this part, a unit is considered available for occupancy from the date on which the End of the Initial Operating Period for the Project is established until the time it is approved by HUD for deprogramming and is vacated or is approved for nondwelling use. On or after July 1, 1991, a unit is not considered available for occupancy in any PHA Requested Budget Year if the unit is located in a vacant building in a project that HUD has determined is nonviable.

Utilities. Electricity, gas, heating fuel, water and sewerage service.

Utilities Expense Level. The per unit per month dollar amount of Utilities expense, computed as provided in §990.107.

§ 990.105 [Corrected]

2. Section 990.105(e)(4) is corrected by removing the phrases "in calendar year 1985" and "in 1985" each time they appear, and adding in their place the phrase "before April 1, 1986".

3. Section 990.105(e)(5) is corrected by removing the phrase "in calendar year 1986 and thereafter" each time it appears, and adding in its place the phrase "on or after April 1, 1986".

(42 U.S.C. 1437g)

Dated: December 17, 1985.

Grady J. Norris,

Assistant General Counsel for Regulations.

[FR Doc. 30231 Filed 12-20-85; 8:45 am]

BILLING CODE 4210-33-M

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1 and 602

[T.D. 8063]

Income Taxes; Temporary Regulations Relating to the Taxation of Fringe Benefits and Exclusions From Gross Income for Certain Fringe Benefits

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations concerning the taxation and valuation of fringe benefits and exclusions from gross income for certain fringe benefits. Changes to the applicable law were made by the Tax Reform Act of 1984 (98 Stat. 877). The regulations affect any person providing or receiving fringe benefits. The regulations provide these persons with the guidance necessary to comply with the law.

DATE: The regulations are effective as of January 1, 1985.

FOR FURTHER INFORMATION CONTACT: Annette J. Guarisco of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service, (202-566-3918, not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains temporary regulations relating to the taxation and valuation of fringe benefits and exclusions from gross income for certain fringe benefits. Section 61 of the Internal Revenue Code of 1954 (Code) was amended, and section 132 was added to the Code, by section 531 of the Tax Reform Act of 1984 (98 Stat. 877). Temporary and proposed regulations were published in the **Federal Register** for January 7, 1985 (50 FR 747, 836). These regulations were later amended in part in the **Federal Register** for February 20, 1985 (50 FR 7038, 7073).

Subsequently, Pub. L. 99-44 (Repeal of Contemporaneous Recordkeeping Requirements) affected the proposed

and temporary regulations published in February. To implement the provisions of Pub. L. 99–44, the Service withdrew the affected proposed and temporary regulations published in February 1985 (50 FR 46004, 46086, Nov. 6, 1985) and published new proposed and temporary regulations on November 6, 1985 (50 FR 46006, 46087).

Many comments were received from the public concerning the provisions in the proposed and temporary regulations previously published in 1985. In addition, on April 16, 17, and 18, 1985, the Internal Revenue Service (Service) held public hearings on the proposed regulations. In response to the comments and the statements made at the public hearings, the regulations have been amended. Due to the extent of the amendments, the Service is issuing the regulations in temporary rather than final form and is providing a cross-reference notice of proposed rulemaking (see the Proposed Rules section of this issue of the **Federal Register**). This will provide the public with an opportunity to comment on the revised provisions of the regulations before they become final. The Service expects to hold public hearings on the regulations early next year.

The regulations contain general rules relating to valuation of fringe benefits and special rules that may be used to value certain fringe benefits, including the availability of employer-provided automobiles, the use of employer-provided vehicles for personal purposes or for commuting only, flights on employer-provided aircraft, and taxable flights on commercial airlines.

Summary of Comments and Explanation of Provisions

In General

All of the regulations issued in January, February, and November of 1985 under sections 61 and 132 (the "proposed regulations") were removed and are replaced by these revised temporary regulations (the "new temporary regulations"). Many of the provisions contained in the proposed regulations were revised in response to comments received. The explanation of provisions describes the changes made to the proposed regulations and the reasons that certain comments are not reflected in the new temporary regulations. Many of the comments received are not included in this summary because they suggested changes that were contrary to the statutory amendments or the legislative intent evidenced in committee reports accompanying the legislation.

In addition to revised rules, the new temporary regulations contain rules relating to areas not addressed in the proposed regulations. For example, the regulations contain a special rule that may be used to value meals provided at an employer-operated eating facility for employees. This section contains an explanation of many of these new rules.

Valuation of Employer-Provided Vehicles Determination of Fair Market Value

The proposed regulations provided that the Annual Lease Value is determined by reference to the fair market value of the employer-provided automobile made available to the employee. Many commentators suggested that the regulations provide additional guidance concerning determination of the fair market value of the automobile. In response, the new temporary regulations provide fair market value safe harbor rules. Many commentators requested that the proposed regulations allow the use of an automobile pricing guide to determine fair market value. Other commentators suggested that the cost of purchasing the automobile may be treated as the fair market value of the automobile, either with or without an adjustment reflecting any group or volume discount secured by the employer. In response, the new temporary regulations provide that for an automobile owned by an employer, the employer's cost of purchasing the automobile be treated as the fair market value of the automobile, provided the purchase is made at arm's length. For an automobile that is leased or revalued by an employer, the retail value provided in any nationally recognized publication that regularly reports retail automobile values may be treated as the fair market value of the automobile, provided the value is reasonable with respect to the automobile.

Many commentators suggested that the regulations provide that the fair market value of an automobile be reduced by the value of special equipment contained in the automobile. In response, the new temporary regulations provide that the fair market value of an automobile does not include the fair market value of any specialized equipment that is added to or carried in the automobile if the presence of the equipment is necessitated by, and attributable solely to, the business needs of the employer. This rule does not apply to equipment susceptible to personal use.

First-Average Valuation Rule

The proposed regulations provided that the Annual Lease Value of each automobile must be determined based on its fair market value. Commentators suggested that this rule would be difficult to administer when an employer has a large fleet of automobiles. The new temporary regulations provide that employers may determine a fleet-average value of the automobiles in the fleet that may be used to determine an Annual Lease Value for all the automobiles in the fleet. The rule is available for an automobile the value of which does not exceed $16,500 and that is regularly used in the employer's business.

Provisions of Fuel in Kind

The proposed regulations provided that the provision of fuel in kind may be valued at 5.5 cents-per-mile. Commentators indicated that employers with large fleets of automobiles need a special rule to value fuel where fuel is not provided from a company pump but the cost is reimbursed by or charged to the employer. In response to this comment, the new temporary regulations provide that an employer may value the provision of fuel for automobiles eligible for the fleet-average valuation rule by reference to average fuel costs and miles-per-gallon rates determined by sampling the greater of 10 percent of the automobiles in the fleet or 20 automobiles.

Redetermination of Annual Lease Value

The Annual Lease Values contained in the proposed regulations are based on a four-year, level-payment lease. Thus, the proposed regulations provided that the Annual Lease Value amount must generally be used for the period beginning on the day the special rule is first used and ending on December 31 of the fourth full year following that date. A number of commentators stated that the Annual Lease Value amount should be redetermined more frequently than every four years. Because the Annual Lease Values are based on a four-year, level-payment lease, however, it would be inappropriate to redetermine the Annual Lease Value more frequently. An alternative would be to base the Annual Lease Values on a shorter lease period. This alternative would require an increase in the Annual Lease Values to reflect the shorter lease term.

Use of Daily Lease Value

The proposed regulations provided that a pro-rated Annual Lease Value may be used when the automobile is available to an employee for at least 30

days. If the automobile is available for less than 30 days, the availability of the automobile may be valued by applying the Daily Lease Value to the number of days the automobile is available to the employee. Alternatively, the availability may be valued by deeming the automobile available to the employee for at least 30 days. Some commentators suggested that the regulations provide that a pro-rated Annual Lease Value be used regardless of the number of days of availability. This suggestion was not adopted because the Daily Lease Value amount was based on an approximation of the lowest fair market rental values. The lessors' charge is higher for leases for shorter periods. The Service's market analysis indicated that a daily lease value is typically 700 percent of the daily pro-rated four-year lease rate in the proposed regulation. Consequently, the new temporary regulations retain the rules regarding Daily Lease Values.

Vehicle cents-per-mile Special Rule

The proposed regulations provided that the availability of an automobile cannot be determined by reference to a cents-per-mile rate multiplied by the number of miles driven. This rule was provided because automobiles are generally not leased on a cents-per-mile basis, but rather on the basis of the amount of time the automobile is available to the lessee.

Many commentators suggested that the regulations allow the use of a cents-per-mile rate, such as the standard mileage rate, to determine the value of the personal use of employer-provided automobiles. In response, the new temporary regulations provide that the standard mileage rate (21 cents-per-mile in 1985) may be used to determine the value of the personal use of an employer-provided vehicle (including an automobile) that is (1) reasonably expected to be regularly used in the employer's business or (2) actually driven (primarily by employees) at least 10,000 miles in a calendar year. This rule may be used for any vehicle the value of which in the calendar year in which it is first made available to an employee for personal use, or, if later, January 1, 1985, does not exceed the sum of the maximum recovery deductions allowable under section 280F(a)(2) for the first three taxable years in the recovery period for an automobile first placed in service during that calendar year. For 1985, that value is $12,800.

The reason for the regularly used in the employer's business requirement (and the alternative mileage rule) is that the vehicle cents-per-mile rule assumes that at least a fixed number of personal miles will be driven in a year (i.e., 15,000). Therefore, unlimited use of the special vehicle cents-per-mile rule would result in a significantly lower valuation for the use of an employer-provided vehicle in certain circumstances. For example, an employee who drives an employer-provided automobile valued at $12,000 for 5,000 miles (all personal) in a year, but who is not provided fuel by his employer, will include $775 in income. Under the Annual Lease Value table, which generally reflects the market value of the availability of an automobile for a year, the employee would include $3,600 in income. Because the valuation distortion is so great, use of the vehicle cents-per-mile rule is permitted only if the vehicle satisfies the regularly used in business requirement or the alternative mileage rule. The alternative mileage rule is intended to provide a mechanical alternative to the more general concept of "regularly used in business." The reason that the mileage must be primarily by employees, rather than, for example, by employees' families, is precisely because the mileage rule is intended as a mechanical alternative to the business use rule.

It should also be noted that in certain situations use of the cents-per-mile rule will result in a higher inclusion than will the automobile lease valuation rule.

Commuting Special Valuation Rule

The proposed regulations provided that the value of the commuting use of an employer-provided vehicle may be valued at $3.00 per one-way or round-trip commute. The new temporary regulations clarify that the value of the commuting use is $1.50 per one-way commute. In the case where more than one employee commutes in an employer-provided vehicle, such as in the case of an employer-sponsored car pool, the value of the commuting use is $1.50 per one-way commute per employee.

The proposed regulations provided that the commuting special rule may not be used to value the commuting use of an employer-provided vehicle by an officer or a five-percent owner of the employer. Many commentators requested that the regulations define an officer, especially for government employees. The new temporary regulations provide that, for commuting that occurs after 1985, the special rule cannot be used to value the commuting use of an employer-provided vehicle by a "control employee". This term (which is defined differently for other purposes) includes certain officers, directors, and owners and is defined in the regulations for both government and non-government employers. The new temporary regulations provide that the officer component of the control employee definition may be applied to define an officer in 1985.

Valuation of Flights on Employer-Provided Aircraft

The proposed regulations provided a special rule that may be used to value certain flights on employer-provided airplanes. The value determined under the special rule depended on the purpose of the trip by the airplane and on whether the employee receiving the fringe benefit was a "key employee".

Many commentators stated that the values provided under the special rule were excessive and that the rule was complicated and too "fact-sensitive" to administer. In response to taxpayer and congressional concerns, the Treasury Department indicated in a letter to Senator Robert Dole (131 Cong. Rec. S6369 (daily ed. May 16, 1985)) that the regulations would be amended. The new temporary regulations adopt the provisions set out in that letter. Accordingly, under the new temporary regulations, the value of a flight under the special rule depends on the weight of the aircraft and whether the employee receiving the benefit is a control employee (defined separately for government and non-government employers).

Generally, the value of a flight determined under the new temporary regulations is lower than the value of a flight determined under the proposed regulations. Under certain circumstances, however, the value of a flight determined under the proposed regulations would be lower than the value of a flight determined under the new temporary regulations. Therefore, the new temporary regulations provide that the value of a flight taken in 1985 may be valued at the lower of the value determined under the proposed regulations or the value determined under the new temporary regulations.

The new temporary regulations retain the use of the Standard Industry Fare Level (SIFL) rates to determine the value of flights on employer-provided aircraft. The regulations provide the new SIFL rates that may be used to determine the value of flights taken during the last six months of 1985. As in the proposed regulations, the multiples used are intended to approximate coach and first-class fares on commercial airlines (e.g., 125 percent of the SIFL rates approximates coach fare and 200 percent of the SIFL rates approximates first-class fare).

The proposed regulations provided that the special valuation rule may only

be used to value flights on employer-provided airplanes, rather than all aircraft (such as helicopters). The new temporary regulations provide that the special rule may be used to value flights on all employer-provided aircraft.

The proposed regulations also provided that the special valuation rule may not be used to value international flights. The new temporary regulations remove this restriction.

Many commentators noted that if an aircraft makes a certain flight for a business purpose, there is no additional cost incurred by the employer in allowing other persons to fly for personal purposes on such trip. They argued, therefore, that no income should be imputed to those persons who fly for personal purposes under such circumstances. Whether the employer incurs an additional cost, however, is not relevant to whether an employee receives a benefit. Certainly, those employees who are allowed to fly for personal purposes place some value on the flight provided.

It should be noted, however, that the proposed regulations provide that where at least 50 percent of the regular seating capacity of an aircraft is occupied by individuals whose flights are primarily for the employer's business (and whose flights are excludable as working condition fringes), the value of flights provided to employees (and certain others) will be considered to be zero. The inclusion of this special rule in the proposed regulations is intended to be a limited provision and is not to be interpreted as an exception to the general valuation principles which the Service will continue to apply outside the scope of this rule.

Valuation of Taxable Flights on Commercial Airlines

The proposed regulations provided a special valuation rule under which certain taxable flights on commercial airlines (i.e., stand-by or space-available flights) may be valued at 50 percent of the highest unrestricted coach fare of the flight taken. Many commentators protested that the 50 percent value was excessive in light of the restrictions imposed on the persons taking the flights, such as the lack of a guaranteed seat. The commentators submitted relevant data and suggested that 25 percent of the highest unrestricted coach fare is a more appropriate value of the benefit received. In response, the new temporary regulations provide that stand-by or space-available flights on commercial airlines may be valued at 25 percent of the highest unrestricted coach fare.

Valuation of Meals Provided at Employer-Operated Eating Facilities for Employees

The new temporary regulations contain a special valuation rule that may be used to value meals provided at employer-operated eating facilities for employees. Pursuant to the special rule, the fair market value of all meals provided at the facility (the "total meal value") will be deemed to equal 150 percent of the facility's direct operating costs. This total meal value, less the actual gross receipts of the facility (the "total meal subsidy"), may then be allocated among employees in any manner reasonable under the circumstances. Alternatively, the employer may determine the fair market value of the taxable part of meals provided to a particular employee under a special "individual meal subsidy" rule.

Section 132 Regulations

In General

The new temporary regulations provide rules relating to the exclusion from gross income for certain fringe benefits. Section 132 provides that certain fringe benefits, such as no-additional-cost services, qualified employee discounts, working condition fringes, and de minimis fringes may be excludable from the income of employees receiving the benefits. The regulations provide that, for purposes of the no-additional-cost service and qualified employee discount exclusions, the term "employee" means any individual who is currently employed by the employer, who was employed by the employer but separated from service by reason of retirement or disability, or who is a widow or widower of an employee. The regulations provide that a partner who performs services for a partnership is considered employed by the partnership.

The regulations provide that any individual listed above who could exclude from income no-additional-cost services or qualified employee discounts may exclude from income working condition fringes. In addition, solely for purposes of administrative convenience, the regulations provide that directors of the employer and independent contractors who perform services for the employer may generally exclude from income working condition fringes. This special rule is only available when, as set forth in Rev. Rul. 84-151, any amount included in income would also be deductible as an ordinary and necessary business expense. Therefore, this special rule does not apply, for example, to exclude from the income of an independent contractor or a director as a working condition fringe the value of the use of consumer goods under a product testing program. Directors and independent contractors are not treated as employees for any other purposes.

There is no limitation under section 132 as to who may exclude a de minimis fringe from income. Therefore, the regulations provide that any recipient may exclude a de minimis fringe from income.

Line of Business Limitation

No-additional-cost services and qualified employee discounts are available to employees of the line of business providing discounts or services. The regulations define a line of business based on the Enterprise Standard Industrial Classification Manual (ESIC Manual) prepared by the Statistical Policy Division of the U.S. Office of Management and Budget. An employer is generally considered to have more than one line of business if the employer offers for sale to customers property or services in more than one two-digit classification referred to in the ESIC Manual. Examples of two-digit classifications are general retail merchandise stores; hotels and other lodging places; and auto repair, services, and garages.

The regulations also provide special rules under which an employer's separate lines of business will be aggregated. Under one rule, if it is uncommon in the employer's industry for any of the separate lines of business to be operated without the others, the separate lines of business are treated as one line of business. Under another rule, separate lines of business are aggregated if it is common for a substantial number of employees (other than those employees who work at the headquarters or main office of the employer) to perform substantial services for more than one line of business of the employer so that any determination of which employees perform substantial services for which lines of business would be difficult. Under another aggregation rule, separate retail lines of business located on the same premises are generally treated as the same line of business.

Working Condition Fringes

Employer-Provided Transportation for Security Reasons

The proposed regulations provide that the value of transportation provided by the employer for security reasons may be excludable as a working condition fringe to the extent a deduction under section 162 or 167 would be allowable to

the employee had the employee paid for the transportation. Many commentators requested that the Service provide additional guidance concerning the appropriateness and amount of any working condition fringe exclusion for the value of security provided for bona fide business-oriented security reasons. In response, the new temporary regulations provide rules concerning the existence of bona fide business-oriented security reasons and the effect of an independent security study particular to the employer and its employees. The new temporary regulations also contain several examples of the application of the rules.

Product Testing

The regulations provide that the value of the use of consumer goods may be excludable as a working condition fringe if certain conditions are met. This portion of the regulations is based on the legislative history of section 531 of the Tax Reform Act of 1984. The exclusion for product testing is limited so as to permit employers to have the benefit of product testing programs without allowing a major deviation from the general overall legislative intent of taxation of nonstatutory fringe benefits.

Qualified Automobile Demonstration Use

The value of qualified automobile demonstration use is excludable from income as a working condition fringe. The regulations provide guidance concerning when the exclusion is available. In addition, the regulations provide a safe harbor rule that defines the sales area in which an automobile dealership is located.

Parking

The value of parking may be excluded as a working condition fringe. The regulations provide rules relating to when the exclusion is available.

Employer-Operated Athletic Facilities

Under a special rule, the value of the use of employer-operated athletic facilities may be excluded from income. The regulations provide rules concerning the definition of an employer-operated athletic facility and when the exclusion is available.

Nondiscrimination Rules

No-additional-cost services, qualified employee discounts, and meals provided at employer-operated eating facilities for employees are only excludable from the income of an employee who is an officer, owner, or highly compensated employee (i.e., a member of the "prohibited group") if the benefits are offered on substantially the same terms to each member of a group of employees that is defined under a reasonable classification set up by the employer that does not discriminate in favor of the members of the prohibited group. Many commentators suggested that the definitions of owner and highly compensated employee contained in the proposed regulations were arbitrary and mechanical. The definitions were not amended in the new temporary regulations because, based on data submitted by commentators, the Service believes that the definitions comprise a reasonable and appropriate framework for identifying employees as members of the prohibited group. In addition, many commentators requested that the Service retain definitions that provide certainty.

The regulations provide that a classification is nondiscriminatory under section 132 if the classification would be nondiscriminatory under the rules provided in the qualified plan area (section 410(b)(1)(B) of the Code and the regulations thereunder).

Employer-Operated Eating Facilities for Employees

The value of meals provided at employer-operated eating facilities for employees are excludable from income as de minimis fringes if the revenues from the facility equal or exceed the direct operating costs of the facility and the nondiscrimination requirements of section 132 are satisfied. In response to comments, direct operating costs are narrowly defined as the cost of food and beverages and the cost of labor for personnel whose services relating to the facility are performed primarily on the premises of the eating facility. If meals provided at an eating facility are not excludable because, for example, the direct operating costs of the facility exceed revenues from the facility, the special meal valuation rule provided in the regulations under section 61 (described above) may be used to value the meals provided at the facility.

Special Analyses

The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required.

No general notice of proposed rulemaking is required by 5 U.S.C. 553(b) for temporary regulations. Accordingly, the temporary regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

The collection of information requirements contained in these regulations have been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB. Control number [1545-0771].

Drafting Information

The principal author of these regulations is Annette J. Guarisco of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

List of Subjects

26 CFR 1.61-1—281.4

Income taxes, Taxable income, Deductions, Exemptions.

26 CFR Part 602

Reporting and recordkeeping requirements.

Adoption of Amendment to the Regulations

Accordingly, 26 CFR Parts 1 and 602 are amended as follows:

PART 1—[AMENDED]

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805 * * * 1.61–2T, 1.132–1T, 1.132–2T, 1.132–3T, 1.132–4T, 1.132–5T, 1.132–6T, 1.132–7T, and 1.132–8T also issued under 26 U.S.C. 132.

Par. 2. Section 1.61–2T is removed and a new § 1.61–2T is added in its place, as follows:

§ 1.61–2T Taxation of fringe benefits (Temporary).

(a) *Fringe benefits*—(1) *In general.* Section 61(a)(1) provides that, except as otherwise provided in subtitle A, gross income includes compensation for services, including fees, commissions, fringe benefits, and similar items. Examples of fringe benefits include: an employer-provided automobile, a flight on an employer-provided aircraft, an employer-provided free or discounted commercial airline flight, an employer-provided vacation, and employer-provided discount on property or services, and emkployer-provided membership in a country club or other social club, and an employer-provided ticket to an entertainment or sporting event.

(2) *Fringe benefits excluded from income.* To the extent that a particular fringe benefit is specifically excluded from gross income pursuant to another section of subtitle A, that section shall govern the treatment of the fringe benefit. Thus, if the requirements of the governing section are satisfied, the fringe benefits may be excludable from gross income. Examples of excludable fringe benefits are qualified tuition reductions provided to an employee (section 177(d)); meals and lodging furnished to an employee for the convenience of the employer (section 119); and benefits provided under a dependent care assistance program (section 129). Similarly, the value of the use by an employee of an employer-provided vehicle or a flight provided to an employee on an employer-provided aircraft may be excludable from income under section 105 (because, for example, the trnsportation is provided for medical reasons) if and to the extent that the requirements of that section are satisfied. Section 61 and the regulations thereunder shall apply, however, to the extent that they are not inconsistent with such other section. For example, many fringe benefits specifically addressed in other sections of subtitle A are excluded from gross income only to the extent that they do not exceed specific dollar or percentage limits, or only if certain other requirements are met. If the limits are exceeded or the requirements are not met, some or all of the fringe benefit may be includible in gross income. See paragraph (b)(3) of this section.

(3) *Compensation for services.* A fringe benefit provided in connection with the performance of services shall be considered to have been provided as compensation for servcies. Refraining from the performance of services (such as pursuant to a covenant not to compete) is deemed to be the performance of services for purposes of this section.

(4) *Recipient of a fringe benefit*—(i) *Definition.* A fringe benefit is included in the income of the "recipient" of the fringe benefit. The recipient of a fringe benefit is the person performing the services in connection with which the fringe benefit is provided. Thus, a person may be considered to be a recipient, even though that person did not actually receive the fringe benefit. For example, a fringe benefit provided to any person is connection with the performance of services by another person is considered to have been provided to the person who performs the services and not the person who receives the fringe benefit. In addition, if a fringe benefit is provided to a person, but taxable to a second person as the recipient, such benefit is referred to as provided to the second person and use by the first person is considered use by the second person. For example, provision of an automobile to an employee's spouse by the employer is taxable to the employee as the recipient. The automobile is referred to as available to the employee and use by the employee's spouse is considered use by the employee.

(ii) *Recipient may be other than an employee.* The recipient of a fringe benefit need not be an employee of the provider of the fringe benefit, but may be a partner, director, or an independent contractor. For convenience, the term "employee" includes a reference to any recipient of a fringe benefit, unless otherwise specifically provided in this section.

(5) *Provider of a fringe benefit.* The "provider" of a fringe benefit is that person for whom the services are performed, regardless of whether that person actually provides the fringe benefit to the recipient. The provider of a fringe benefit need not be the employer of the recipient of the fringe benefit, but may be, for example, a client or customer of an independent contractor. For convenience, the term "employer" includes a reference to any provider of a fringe benefit, unless otherwise specifically provided in this section.

(6) *Effective date.* This section is effective as of January 1, 1985. No inference may be drawn from the promulgation or terms of this section concerning the application of law in effect prior to January 1, 1985.

(b) *Valuation of fringe benefits*—(1) *In general.* An employee must include in gross income the amount by which the fair market value of the fringe benefit exceeds the sum of (i) the amount, if any, paid for the benefit, and (ii) the amount, if any, specifically excluded from gross income by some other section of subtitle A. Therefore, for example, if the employee pays fair market value for what is received, no amount is includible in the gross income of the employee.

(2) *Fair market value.* In general, fair market value is determined on the basis of all the facts and circumstances. Specifically, the fair market value of a fringe benefit is that amount a (hypothetical person would have to pay a hypothetical third party to obtain (i.e., purchase or lease) the particular fringe benefit. Thus, for example, the effect of any special relationship that may exist between the employer and the employee must be disregarded. This also means that an employee's subjective perception of the value of a fringe benefit is not relevant to the determination of a fringe benefit's fair market value. In addition, the cost incurred by the employer is not determinative of the fair market value of the fringe benefit. For special rules relating to the valuation of certain fringe benefits, see paragraph (c) of this section.

(3) *Exclusion from income based on cost.* If a statutory exclusion phrased in terms of cost applies to the provision of a fringe benefit, section 61 does not require the inclusion in the recipient's gross income of the difference between the fair market value and the excludable cost of that fringe benefit. For example, section 129 provides an exclusion from an employee's gross income for amounts paid or incurred by an employer to provide dependent care assistance to employees. Even if the fair market value of the dependent care assistance exceeds the employer's cost, the excess is not subject to inclusion under section 61 and this section. If the statutory cost exclusion is a limited amount, however, then the fair market value of the fringe benefit attributable to any excess cost is subject to inclusion.

(4) *Fair market value of the availability of an employer-provided vehicle.* If the vehicle special valuation rules of paragraph (d), (e), or (f) of this section are not used by a taxpayer entitled to use such rules, the value of the availability of an employer-provided vehicle is determined under the general valuation principles set forth in this section. In general, such valuation must be determined by reference to the cost to a hypothetical person of leasing from a hypothetical third party the same or comparable vehicle on the same or comparable terms in the geographic area in which the vehicle is available for use. Unless the employee can substantiate that the same or comparable vehicle could have been leased on a cents-per-mile basis, the value of the availability of the vehicle cannot be determined by reference to a cents-per-mile rate applied to the number of miles the vehicle is driven. An example of a comparable lease term is the amount of time that the vehicle is available to the employee for use, e.g., a one-year period.

(5) *Fair market value of a flight on an employer-provided aircraft.* If the non-commercial flight special valuation rule of paragraph (g) of this section is not used (or is not properly used) by a taxpayer entitled to use such rule, the value of a flight on an employer-provided aircraft is determined under the general valuation principles set forth

in this section. An example of how the general valuation principles would apply is that if an employee whose flight is primarily personal controls the use of an aircraft with respect to such flight, such flight is valued by reference to how much it would cost a hypothetical person to charter the same or comparable aircraft for the same or comparable flight. The cost to charter the aircraft must be allocated among all employees on board the aircraft based on all the facts and circumstances, including which employees controlled the use of the aircraft. Notwithstanding the allocation required by the preceding sentence, no additional amount shall be included in the income of any employee whose flight is properly valued under the special valuation rule of paragraph (g) of this section.

(c) *Special valuation rules*—(1) *In general.* Paragraphs (d) through (j) of this section provide special valuation rules that may be used under certain circumstances for certain commonly provided fringe benefits. Paragraph (d) provides a lease valuation rule relating to employer-provided automobiles. Paragraph (e) provides a cents-per-mile valuation rule relating to employer-provided vehicles. Paragraph (f) provides a commuting valuation rule relating to employer-provided vehicles. Paragraph (g) provides a flight valuation rule relating to flights on employer-provided aircraft. Paragraph (h) provides a flight valuation rule relating to flights on commercial airlines. Paragraph(i) is reserved. Paragraph (j) provides a meal valuation rule relating to employer-operated eating facilities for employees. For general rules relating to the valuation of fringe benefits not eligible for valuation under the special valuation rules, see paragraph (d) of this section.

(2) *Use of the special valuation rules—(i) In general.* The Special valuation rules may be used for income, employment tax, and reporting purposes. Use of any of the special valuation rules is optional. An employer need not use the same vehicle special valuation rule for all vehicles provided to all employees. For example, an employer may use the automobile lease valuation rule for automobiles provided to some employees, and the commuting and vehicle cents-per-mile valuation rules for automobiles provided to other employees. Except as otherwise provided, however, if either the commercial flight valuation rule or the noncommercial flight valuation rule is used, such rule must be used by an employer to value all flights taken by employees in a calendar year. Effective January 1, 1986, if an employer uses one of the special rules to value the benefit provided to an employee, the employee may not use another special rule to value that benefit. The employee may, however, use general valuation rules based on facts and circumstances (see paragraph (b) of this section). Effective January 1, 1986, an employee may only use a special valuation rule if the employer uses the rule. If a special rule is used, it must be used for all purposes. If an employer properly uses a special rule and the employee uses the special rule, the employee must include in gross income the amount determined by the employer under the special rule less any amount reimbursed by the employee to the employer. The employer and the employee may use the special rules to determine the amount of the reimbursement due the employer by the employee. If an employer properly uses a special rule and properly determines the amount of an employee's working condition fringe under section 132 and § 1.132–1T (under the general rule or under a special rule), and the employee uses the special valuation rule, the employee must include in gross income the amount determined by the employer less any amount reimbursed by the employee to the employer.

(ii) *Transitional rules*—(A) *Use of vehicle special valuation rules for 1985 and 1986.* For purposes of valuing the use or availability of a vehicle, the consistency rules provided in paragraphs (d)(6) and (e)(5) of this section (relating to the automobile lease valuation rule and the vehicle cents-per-mile valuation rule, respectively) apply for 1987 and thereafter. Therefore, for 1985 and 1986 an employer (and employee, subject to paragraph (c)(2)(i) of this section) may use any applicable special valuation rule (or no special valuation rule) to value the use or availability of a vehicle, subject to paragraph (c)(2)(ii)(B) of this section.

(B) *Consistency Rules for 1985 and 1986.* If an employer uses the automobile lease valuation rule of paragraph (d) of this section in 1985 or 1986 with respect to an automobile, such rule must be used for the entire calendar year with respect to the automobile except for any period during which the commuting valuation rule of paragraph (f) of this section is properly used. If an employer uses the vehicle cents-per-mile valuation rule of pararaph (e) of this section in 1985 or 1986 with respect to a vehicle, such rule must be used for the entire calendar year with respect to the vehicle except for any period during which the commuting valuation rule of paragraph (f) of this section is properly used. The rules of this paragraph (c)(2)(ii)(B) also apply to employees using the special valuation rules of paragraphs (d) or (e) of this section.

(C) *Employee's use of special valuation rules for 1985.* An employee may use a special valuation rule (other than the rule in paragraph (e) of this section relating to the vehicle cents-per-mile valuation rule) during 1985 even if the employer does not use the same special valuation rule during 1985. An employee's use of a special valuation rule in 1986 and thereafter must be consistent with his employer's use of the rule as required under paragraph (c)(2)(i) of this section.

(D) *Examples.* The following examples illustrate the rules of paragraph (c)(2)(ii) of this section:

Example (1). Assume that an employer properly uses the automobile lease valuation rule in 1985. The employer may use the vehicle cents-per-mile valuation rule in 1986 if the requirements of the vehicle cents-per-mile valuation rule are satisfied.

Example (2). Assume that an employer does not use a special valuation rule to value the availability of an automobile in 1985. The employer may use any of the special valuation rules in 1986 if the requirements of the rule chosen are satisfied. The same applies for 1987.

Example (3). Assume that an employer properly uses the vehicle cents-per-mile valuation rule in 1985. The employer may continue to use to the rule or use any of the other special valuation rules to value the benefit provided in 1986 if the requirements of the rule chosen are satisfied. Alternatively, the employer may use none of the special valuation rules in 1986 but use any of the rules in 1987 if the requirements of the rule chosen are satisfied.

Example (4). Assume that an employee properly uses the automobile lease valuation rule in 1985. In 1986 and thereafter the employee may use a special valuation rule only if the employee's employer uses the same special valuation rule. The employee may use general valuation principles to value the benefit provided in 1986 and thereafter.

(3) *Election to use the special valuation rules*—(i) *In general.* A particular special valuation rule is deemed to have been elected by the employer (and, if applicable, by the employee), if the employer (and, if applicable, the employee) determines the value of the fringe benefit provided by applying the special valuation rule and treats such value as the fair market value of the fringe benefit for income, employment tax, and reporting purposes. Neither the employer nor the employee is required to notify the Internal Revenue Service of the election.

(ii) *Notification to employee.* Effective January 1, 1987, an employer who elects to use a special valuation rule must

notify the employee of the election by the later January 31 of the calendar year for which the election is to apply or 30 days after the employer first provides the benefit to the employee. An employer who elects to use a special valuation rule with respect to 1986 must notify the employee of the election by the later of March 31, 1986, or 30 days after the employer first provides the benefit to the employee. An employer who elects to use a special valuation rule with respect to 1985 need not provide notification of this election to the employee.

(4) *Application of section 414 to employers.* For purposes of paragraphs (c) through (j) of this section, except as otherwise provided therein, the term "employer" includes all entities required to be treated as a single employer under section 414 (b), (c), or (m).

(5) *Valuation formulas contained in the special valuation rules.* The valuation formulas contained in the special valuation rules are provided only for use in connection with such rules. Thus, when a special valuation rule is properly applied to a fringe benefit, the Commissioner will accept the value calculated pursuant to the rule as the fair market value of that fringe benefit. However, when a special valuation rule is not properly applied to a fringe benefit (see, for example, paragraph (g)(11) of this section), or when a special valuation rule is not used to value a fringe benefit by a taxpayer entitled to use the rule, the fair market value of that fringe benefit may not be determined by reference to any value calculated under any special valuation rule. Under the circumstances described in the preceding sentence, the fair market value of the fringe benefit must be determined pursuant to paragraph (b) of this section.

(6) *Modification of the special valuation rules.* The Commissioner may, if he deems it necessary, add, delete, or modify the special valuation rules, including the valuation formulas contained herein, on a prospective basis.

(7) *Special Accounting Period.* If the employer is using the special accounting rule provided in Announcement 85–113 (1985–31 I.R.B., August 5, 1985) (relating to the reporting of and withholding on the value of noncash fringe benefits), benefits which are deemed provided in a subsequent calendar year pursuant to such rule are considered as provided in such subsequent calendar year for purposes of the special valuation rules. Thus, if a particular special valuation rule is in effect for a calendar year, it applies to benefits deemed provided during such calendar year under the special accounting rule.

(d) *Automobile lease valuation rule*—(1) *In general*—(i) *Annual Lease Value.* Under the special valuation rule of this paragraph (d), if an employer provides an employee with an automobile that is available to the employee for an entire calendar year, the value of the benefit provided in the Annual Lease Value (determined under paragraph (d)(2) of this section) of that automobile. Except as otherwise provided, for an automobile that is available to an employee for less than an entire calendar year, the value of the benefit provided is either a pro-rated Annual Lease Value or the Daily Lease Value (as defined in paragraph (d)(4) of this section), whichever is applicable. Absent any statutory exclusion relating to the employer-provided automobile (see, for example, section 132(a)(3) and § 1.132–5T(b)), the amount of the Annual Lease Value (or a pro-rated Annual Lease Value or the Daily Lease Value, as applicable) is included in the gross income of the employee.

(ii) *Definition of automobile.* For purposes of this paragraph (d), the term "automobile" means any four-wheeled vehicle manufactured primarily for use on public streets, roads, and highways.

(2) *Calculation of Annual Lease Value*—(i) *In general.* The Annual Lease Value of a particular automobile is calculated as follows:

(A) Determine the fair market value of the automobile as of the first date on which the automobile is made available to any employee of the employer for personal use. For an automobile first made available to any employee for personal use prior to January 1, 1985, determine the fair market value as of January 1, 1985. For rules relating to determination of the fair market value of an automobile for purposes of this paragraph (d), see paragraph (d)(5) of this section.

(B) Select the dollar range in column 1 of the Annual Lease Value Table, set forth in paragraph (d)(2)(iii) of this section, corresponding to the fair market value of the automobile. Except as otherwise provided in paragraphs (d)(2)(iv) and (v) of this section, the Annual Lease Value for each year of availability of the automobile is the corresponding amount in column 2 of the Table.

(ii) *Use by employee only in 1985.* If the employee, but not the employer, is using the special rule of this paragraph (d), the employee may calculate the Annual Lease Value in the same manner as described in paragraph (d)(2)(i)(A) of this section, except that the fair market value of the automobile is determined as of the first date on which the automobile is made available to the employee for personal use or, for an automobile made available to the employee for personal use prior to January 1, 1985, by determining the fair market value as of January 1, 1985. If the employer is also using the special rule of this paragraph (d), however, then the employee to whom the automobile is made available must use the special rule, if at all, by using the Annual Lease Value calculated by the employer. The rules of this paragraph (d)(2)(ii) apply only for 1985.

(iii) *Annual Lease Value Table.*

Automobile fair market value (1)	Annual lease value (2)
$0 to $999	$600
$1,000 to $1,999	850
$2,000 to $2,999	1,100
$3,000 to $3,999	1,350
$4,000 to $4,999	1,600
$5,000 to $5,999	1,850
$6,000 to $6,999	2,100
$7,000 to $7,999	2,350
$8,000 to $8,999	2,600
$9,000 to $9,999	2,850
$10,000 to $10,999	3,100
$11,000 to $11,999	3,350
$12,000 to $12,999	3,600
$13,000 to $13,999	3,850
$14,000 to $14,999	4,100
$15,000 to $15,999	4,350
$16,000 to $16,999	4,600
$17,000 to $17,999	4,850
$18,000 to $18,999	5,100
$19,000 to $19,999	5,350
$20,000 to $20,999	5,600
$21,000 to $21,999	5,580
$22,000 to $22,999	6,100
$23,000 to $23,999	6,350
$24,000 to $24,999	6,600
$25,000 to $25,999	6,850
$26,000 to $27,999	7,250
$28,000 to $29,999	7,750
$30,000 to $31,999	8,250
$32,000 to $33,999	8,750
$34,000 to $35,999	9,250
$36,000 to $37,999	9,750
$38,000 to $39,999	10,250
$40,000 to $41,999	10,750
$42,000 to $43,999	11,250
$44,000 to $45,999	11,750
$46,000 to $47,999	12,250
$48,000 to $49,999	12,750
$50,000 to $51,999	13,250
$52,000 to $53,999	13,750
$54,000 to $55,999	14,250
$56,000 to $57,999	14,750
$58,000 to $59,999	15,250

For vehicles having a fair market value in excess of $59,999, the Annual Lease Value is equal to: (.25 X the fair market value of the automobile) + $500.

(iv) *Recalculation of Annual Lease Value.* The Annual Lease Values determined under the rules of this paragraph (d) are based on a four-year lease term. Therefore, except as otherwise provided in paragraph (d)(2)(v) of this section, the Annual Lease Value calculated by applying paragraph (d)(2) (i) or (ii) of this section shall remain in effect for the period that begins with the first date the special valuation rule of paragraph (d) of this section is applied by the employer to the automobile and ends on December 31 of the fourth full calendar year following

that date. The Annual Lease Value for each subsequent four-year period is calculated by determining the fair market value of the automobile as of the January 1 following the period described in the previous sentence and selecting the amount in column 2 of the Annual Lease Value Table corresponding to the appropriate dollar range in column 1 of the Table. If, however, the employer is using the special accounting rule provided in Announcement 85–113 (1985–31 I.R.B., August 5, 1985) (relating to the reporting of and withholding on the value of noncash fringe benefits), the employer may calculate the Annual Lease Value for each subsequent four-year period as of the beginning of the special accounting period that begins immediately prior to the January 1 described in the previous sentence. For example, assume that pursuant to Announcement 85–113, an employer uses the special accounting rule. Assume further that beginning on November 1, 1985, the special accounting period is November 1 to October 31 and that the employer elects to use the special valuation rule of this paragraph (d) as of January 1, 1985. The employer may recalculate the Annual Lease Value as of November 1, 1988, rather than as of January 1, 1989.

(v) *Transfer of the automobile to another employee.* Unless the primary purpose of the transfer is to reduce Federal taxes, if an employer transfers an automobile from one employee to another employee, the employer may recalculate the Annual Lease Value based on the fair market value of the automobile as of January 1 of the year of transfer. If, however, the employer is using the special accounting rule provided in Announcement 85–113 (1985–31 I.R.B., August 5, 1985) (relating to the reporting of and withholding on the value of noncash fringe benefits), the employer may recalculate the Annual Lease Value based on the fair market value of the automobile as of the beginning of the special accounting period in which the transfer occurs. If the employer does not recalculate the Annual Lease Value, and the employee to whom the automobile is transferred uses the special valuation rule, the employee may not recalculate the Annual Lease Value.

(3) *Services included in, or excluded from, the Annual Lease Value Table*—(i) *Maintenance and insurance included.* The Annual Lease Values contained in the Annual Lease Value Table include the fair market value of maintenance of, and insurance for, the automobile. Neither an employer nor an employee may reduce the Annual Lease Value by the fair market value of any service included in the Annual Lease Value that is not provided by the employer, such as reducing the Annual Lease Value by the fair market value of a maintenance service contract or insurance. An employer or employee may take into account the services actually provided with respect to the automobile by valuing the availability of the automobile under the general valuation rules of paragraph (b) of this section.

(ii) *Fuel excluded*—(A) *In general.* The Annual Lease Values do not include the fair market value of fuel provided by the employer, regardless of whether fuel is provided in kind or its cost is reimbursed by or charged to the employer.

(B) *Valuation of fuel provided in kind.* The provision of fuel in kind may be valued at fair market value based on all the facts and circumstances or, in the alternative, it may be valued at 5.5 cents per mile for all miles driven by the employee. However, the provision of fuel in kind may not be valued at 5.5 cents per mile for miles driven outside the United States, Canada, and Mexico. For purposes of this section, the United States includes the United States and its territories.

(C) *Valuation of fuel where cost reimbursed by or charged to employer.* The fair market value of fuel, the cost of which is reimbursed by or charged to an employer, is generally the amount of the actual reimbursement or the amount charged, provided the purchase of the fuel is at arm's length. If an employer with a fleet of at least 20 automobiles that meet the requirements of paragraph (d)(5)(v)(C) of this section reimburses employees for the cost of fuel or allows employees to charge the employer for the cost of the fuel, however, the fair market value of fuel provided to those automobiles may be determined by reference to the employer's fleet-average cents-per-mile fuel cost. The fleet-average cents-per-mile fuel cost in equal to the fleet-average per-gallon fuel cost divided by the fleet-average miles-per-gallon rate. The averages described in the preceding sentence must be determined by averaging the per-gallon fuel costs and miles-per-gallon rates of a representative sample of the automobiles in the fleet equal to the greater of ten percent of the automobiles in the fleet or 20 automobiles for a representative period, such as a two month period.

(iii) *All other services excluded.* The fair market value of any service not specifically identified in paragraph (d)(3)(i) of this section that is provided by the employer with respect to an automobile (such as the services of a chauffeur) must be added to the Annual Lease Value of the automobile in determining the fair market value of the benefit provided.

(4) *Availability of an automobile for less than an entire calendar year*—(i) *Pro-rated Annual Lease Value used for continuous availability of 30 or more days.* Except as otherwise provided in paragraph (d)(4)(iv) of this section, for periods of continuous availability of 30 or more days, but less than an entire calendar year, the value of the availability of the employer-provided automobile is the pro-rated Annual Lease Value. The pro-rated Annual Lease Value is calculated by multiplying the applicable Annual Lease Value by a fraction, the numerator of which is the number of days of availability and the denominator of which is 365.

(ii) *Daily Lease Value used for continuous availability of less than 30 days.* Except as otherwise provided in paragraph (d)(4)(iii) of this section, for periods of continuous availability of one or more but less than 30 days, the value of the availability of the employer-provided automobile is the Daily Lease Value. The Daily Lease Value is calculated by multiplying the applicable Annual Lease Value by a fraction, the numerator of which is four times the number of days of availability and the denominator of which is 365.

(iii) *Election to treat all periods as periods of at least 30 days.* A pro-rated Annual Lease Value may be applied with respect to a period of continuous availability of less than 30 days, by treating the automobile as if it had been available for 30 days, if to do so would result in a lower valuation than applying the Daily Lease Value to the shorter period of actual availability.

(iv) *Periods of unavailability*—(A) *General rule.* In general, a pro-rated Annual Lease Value (as provided in paragraph (d)(4)(i) of this section) is used to value the availability of an employer-provided automobile when the automobile is available to an employee for a period of continuous availability of at least 30 days but less than the entire calendar year. Neither an employer nor an employee may use a pro-rated Annual Lease Value when the reduction of Federal taxes is the primary reason the automobile is unavailable to an employee during the calendar year.

(B) *Unavailability for personal reasons of the employee.* If an automobile is unavailable to an employee because of personal reasons of the employee, such as while the employee is on vacation, a pro-rated Annual Lease Value may not be used.

For example, assume an automobile is available to an employee during the first five months of the year and during the last five months of the year. Assume further that the period of unavailability occurs because the employee is on vacation. The Annual Lease Value, if it is applied, must be applied with respect to the entire 12 month period. The Annual Lease Value may not be pro-rated to take into account the two-month period of unavailability.

(5) *Fair market value*—(i) *In general.* For purposes of determining the Annual Lease Value of an automobile under the Annual Lease Value Table, the fair market value of an automobile is that amount a hypothetical person would have to pay a hypothetical third party to purchase the particular automobile provided. Thus, for example, any special relationship that may exist between the employee and the employer must be disregarded. Also, the employee's subjective perception of the value of the automobile is not relevant to the determination of the automobile's fair market value. In addition, except as provided in paragraph (d)(5) (ii) of this section, the cost incurred by the employer of either purchasing of leasing the automobile is not determinative of the fair market value of the automobile.

(ii) *Safe-harbor valuation rule.* For purposes of calculating the Annual Lease Value of an automobile under this paragraph (d), the safe-harbor value of the automobile may be used as the fair market value of the automobile For an automobile owned by the employer, the safe-harbor value of the automobile is the employer's cost of purchasing the automobile, provided the purchase is made at arm's length. For an automobile leased by the employer, the safe-harbor value of the automobile is the value determined under paragraph (d)(5)(iii) of this section.

(iii) *Use of nationally recognized pricing guides.* The fair market value of an automobile that is (A) provided to an employee prior to January 1, 1985, (B) being revalued pursuant to paragraphs (d)(2) (iv) or (v) of this section, or (C) is a leased automobile being valued pursuant to paragraph (d)(5)(ii) of this section, may be determined by using the retail value of such automobile as reported in a nationally recognized publication that regularly reports new or used automobile retail values, whichever is applicable. The values contained in (and obtained from) the publication must be reasonable with respect to the automobile being valued.

(iv) *Fair market value of special equipment*—(A) *Certain equipment excluded.* The fair market value of an automobile does not include the fair market value of any telephone or any specialized equipment that is added to or carried in the automobile if the presence of such equipment is necessitated by, and attributable to, the business needs of the employer.

(B) *Use of specialized equipment outside of employer's business.* The value of specialized equipment must be included, however, if the employee to whom the automobile is available uses the specialized equipment in a trade of business of the employee other than the employee's trade or business of being an employee of the employer.

(C) *Equipment susceptible to personal use.* The exclusion rule provided in this paragraph (d)(5)(iv) does not apply to specialized equipment susceptible to personal use.

(v) *Fleet-average valuation rule*—(A) *In general.* An employer with a fleet of 20 or more automobiles may use a fleet-average value for purposes of calculating the Annual Lease Values of the automobiles in the fleet. The fleet-average value is the average of the fair market values of each automobile in the fleet. The fair market value of each automobile in the fleet shall be determined, pursuant to the rules of paragraphs (d)(5) (i) through (iv) of this section, as of the later of January 1, 1985, or the first date on which the automobile is made available to any employee of the employer for personal use.

(B) *Period for use of rule.* The fleet-average valuation rule of this paragraph (d)(5)(v) may be used by an employer as of January 1 of any calendar year following the calendar year in which the employer acquires a fleet of 20 or more automobiles. The Annual Lease Value calculated for the automobiles in the fleet, based on the fleet-average value, shall remain in effect for the period that begins with the first January 1 the fleet-average valuation rule of this paragraph (d)(5)(v) is applied by the employer to the automobiles in the fleet and ends on December 31 of the subsequent calendar year. The Annual Lease Value for each subsequent two year period is calculated by determining the fleet-average value of the automobiles in the fleet as of the first January 1 of such period. An employer may cease using the fleet-average valuation rule as of any January 1. The fleet-average valuation rule does not apply as of January 1 of the year in which the number of automobiles in the employer's fleet declines to fewer than 20. If, however, the employer is using the special accounting rule provided in Announcement 85-113 (I.R.B. No. 31, August 5, 1985), the employer may apply the rules of this paragraph (d)(5)(v)(B) on the basis of the special accounting period rather than the calendar year. (This is accomplished by substituting (1) the beginning of the special accounting period that begins immediately prior to the January 1 described in this paragraph (d)(5)(v)(B) for January 1 wherever it appears in this paragraph (d)(5)(v)(B) and (2) the end of such accounting period for December 31.) The revaluation rules of paragraph (d)(2) (iv) and (v) of this section do not apply to automobiles valued under this paragraph (d)(5)(v).

(C) *Limitations on use of fleet-average rule.* The rule provided in this paragraph (d)(5)(v) may not be used for any automobile whose fair market value (determined pursuant to paragraphs (d)(5) (i) through (iv) of this section as of either the first date on which the automobile is made available to any employee of the employer for personal use or, if later, January 1, 1985) exceeds $16,500. In addition, the rule provided in this paragraph (d)(5)(v) may only be used for automobiles that the employer reasonably expects will regularly be used in the employer's trade or business. Infrequent use of the vehicle, such as for trips to the airport or between the employer's multiple business premises, does not constitute regular use of the vehicle in the employer's trade or business.

(D) *Additional automobiles added to the fleet.* If the rule provided in this paragraph (d)(5)(v) is used by an employer, it must be used for every automobile included in or added to the fleet that meets the requirements of paragraph (d)(5)(v)(C) of this section. The fleet-average value in effect at the time an automobile is added to the fleet is treated as the fair market value of the automobile for purposes of determining the Annual Lease Value of the automobile until the fleet-average value changes pursuant to paragraph (d)(5)(v)(B) of this section.

(E) *Use of the fleet-average rule by employees.* An employee can only use the fleet-average value if it is used by the employer. If an employer uses the fleet-average value, and the employee uses the special valuation rule of paragraph (d) of this section, the employee must use the fleet-average value.

(6) *Consistency rules*—(i) *Use of the automobile lease valuation rule by an employer.* Except as provided in paragraph (d)(5) (v)(B) of this section, an employer may adopt the automobile lease valuation rule of this paragraph (d) for an automobile only if the rule is adopted with respect to the later of the period that begins on January 1, 1987, or the first period in which the automobile

is made available to an employee of the employer for personal use or, if the commuting valuation rule of paragraph (f) of this section is used when the automobile is first made available to an employee of the employer for personal use, the first period in which the commuting valuation rule is not used.

(ii) *An employer must use the automobile lease valuation rule for all subsequent periods.* Once the automobile lease valuation rule has been adopted for an automobile by an employer, the rule must be used by the employer for all subsequent periods in which the employer makes the automobile available to any employee, except that the employer may, for any period during which use of the automobile qualifies for the commuting valuation rule of paragraph (f) of this section, use the commuting valuation rule with respect to the automobile.

(iii) *Use of the automobile lease valuation rule by an employee.* Except as provided in paragraph (c)(2)(ii)(C) of this section, an employee may adopt the automobile lease valuation rule for an automobile only if the rule is adopted (A) by the employer and (B) with respect to the first period in which the automobile for which the employer (consistent with paragraph (d)(6)(i) of this section) adopted the rule is made available to that employee for personal use, or, if the commuting valuation rule of paragraph (f) of this section is used when the automobile is first made available to that employee for personal use, the first period in which the commuting valuation rule is not used.

(iv) *An employee must use the automobile lease valuation rule for all subsequent periods.* Once the automobile lease valuation rule has been adopted for an automobile by an employee, the rule must be used by the employee for all subsequent periods in which the automobile for which the rule is used is available to the employee, except that the employee may, for any period during which use of the automobile qualifies for use of the commuting valuation rule of paragraph (f) of this section and for which the employer uses the rule, use the commuting valuation rule with respect to the automobile.

(v) *Replacement automobiles.* Notwithstanding anything in this paragraph (D)(6) to the contrary, if the automobile lease valuation rule is used by an employer, or by an employer and an employee, with respect to a particular automobile, and a replacement automobile is provided to the employee for the primary purpose of reducing Federal taxes, then the employer, or the employer and the employee, using the rule must continue to use the rule with respect to the replacement automobile.

(e) *Vehicle cents-per-mile valuation rule*—(1) *In general*—(i) *General rule.* Under the vehicle cents-per-mile valuation rule of this paragraph (e), if an employer provides an employee with the use of a vehicle that (A) the employer reasonably expects will be regularly used in the employer's trade or business throughout the calendar year (or such shorter period as the vehicle may be owned or leased by the employer) or (B) satisfies the requirements of paragraph (e)(1)(ii) of this section, the value of the benefit provided in the calendar year is the standard mileage rate provided in the applicable Revenue Ruling or Revenue Procedure ("cents-per-mile rate") multiplied by the total number of miles the vehicle is driven by the employee for personal purposes. For 1985, the standard mileage rate is 21 cents per mile for the first 15,000 miles and 11 cents per mile for all miles over 15,000. See Rev. Proc. 85–49. The standard mileage rate must be applied to personal miles independent of business miles. Thus, for example, if an employee drives 20,000 personal miles and 35,000 business miles in 1985, the value of the personal use of the vehicle is $3,700 (15,000 × $.21 + 5,000 × $.11). For purposes of this section, the use of a vehicle for personal purposes is any use of the vehicle other than use in the employee's trade or business of being an employee of the employer. Infrequent use of the vehicle, such as for trips to the airport or between the employer's multiple business premises, does not constitute regular use of the vehicle in the employer's trade or business.

(ii) *Mileage Rule.* A vehicle satisfies the requirements of this paragraph (e)(1)(ii) in a calendar year if (A) it is actually driven at least 10,000 miles in the year, and (B) use of the vehicle during the year is primarily by employees. For example, if a vehicle is used by only one employee during the year and that employee drives a vehicle at least 10,000 miles in a calendar year, such vehicle satisfies the requirements of this paragraph (e)(1)(ii) even if all miles driven by the employee are personal. The requirements of this paragraph (e)(1)(ii), however, will not be satisfied if during the year the vehicle is transferred among employees in such a way which enables an employee whose use was at a rate significantly less that 10,000 miles per year to meet the 10,000 mile threshold. Assume that an employee uses a vehicle for the first six months of the year and drives 2,000 miles, and that vehicle is then used by other employees who drive the vehicle 8,000 miles in the last six months of the year. Because the rate at which miles were driven in the first six months of the year would result in only 4,000 miles being driven in the year, and because the first employee did not use the vehicle during the last six months of the year, the requirements of this paragraph (e)(1)(ii) are not satisfied. The requirement of paragraph (e)(1)(ii)(B) of this section is deemed satisfied if employees use the vehicle on a consistent basis for commuting. If the employer does not own or lease the vehicle during a portion of the year, the 10,000 mile threshold is to be reduced proportionately to reflect the periods when the employer owned or leased the vehicle. For purposes of this paragraph (e)(1)(ii), use of the vehicle by an individual (other than the employee) whose use would be taxed to the employee is not considered use by the employee.

(iii) *Limitation on use of the vehicle cents-per-mile valuation rule.* The value of the use of an automobile (as defined in paragraph (d)(1)(ii) of this section) may not be determined under the vehicle cents-per-mile valuation rule of this paragraph (e) if the fair market value of the automobile (determined pursuant to paragraphs (d)(5) (i) through (iv) of this section as of the later of January 1, 1985, or the first date on which the automobile is made available to any employee of the employer for personal use) exceeds the sum of the maximum recovery deductions allowable under section 280F(a)(2) for the first three taxable years in the recovery period for an automobile first placed in service during that calendar year. For 1985, that value is $12,800.

(2) *Definition of vehicle.* For purposes of this paragraph (e), the term "vehicle" means any motorized wheeled vehicle manufactured primarily for use on public streets, roads, and highways. The term "vehicle" includes an automobile as defined in paragraph (d)(1)(ii) of this section.

(3) *Services included in, or excluded from, the cents-per-mile rate*—(i) *Maintenance and insurance included.* The cents-per-mile rate includes the fair market value of maintenance of, and insurance for, the vehicle. An employer may not reduce the cents-per-mile rate by the fair market value of any service included in the cents-per-mile rate but not provided by the employer. An employer or employee may take into account the services provided with respect to the automobile by valuing the availability of the automobile under the general valuation rules of paragraph (b) of this section.

(ii) *Fuel provided by the employer*—(A) *Miles driven in the United States, Canada, and Mexico.* With respect to miles driven in the United States, Canada, and Mexico, the cents-per-mile rate includes the fair market value of fuel provided by the employer. If fuel is not provided by the employer, the cents-per-mile rate may be reduced by no more than 5.5 cents or the amount specified in any applicable Revenue Ruling or Revenue Procedure. For purposes of this section, the United States includes the United States and its territories.

(B) *Miles driven outside the United States, Canada, and Mexico.* With respect to miles driven outside the United States, Canada, and Mexico, the fair market value of fuel provided by the employer is not reflected in the cents-per-mile rate. Accordingly, the cents-per-mile rate may be reduced but by no more than 5.5 cents or the amount specified in any applicable Revenue Ruling or Revenue Procedure. If the employer provides the fuel in kind, it must be valued based on all the facts and circumstances. If the employer reimburses the employee for the cost of fuel or allows the employee to charge the employer for the cost of fuel, the fair market value of the fuel is generally the amount of the actual reimbursement or the amount charged, provided the purchase of fuel is at arm's length.

(4) *Valuation of personal use only.* The vehicle cents-per-mile valuation rule of this paragraph (e) may only be used to value the miles driven for personal purposes. Thus, the employer must include an amount in an employee's income with respect to the use of a vehicle that is equal to the product of the number of personal miles driven by the employee and the appropriate cents-per-mile rate. The employer may not include in income a greater or lesser amount; for example, the employer may not include in income 100 percent (all business and personal miles) of the value of the use of the vehicle. The term "personal miles" means all miles driven by the employee except miles driven by the employee is the employee's trade or business of being an employee of the employer.

(5) *Consistency rules*—(i) *Use of the vehicle cents-per-mile valuation rule by an employer.* An employer must adopt the vehicle cents-per-mile valuation rule of this paragraph (e) for a vehicle by the later of the period that begins on January 1, 1987, or the first period in which the vehicle is used by an employee of the employer for personal use or, if the commuting valuation rule of paragraph (f) of this section is used when the vehicle is first used by an employee of the employer for personal use, the first period in which the commuting valuation rule is not used.

(ii) *An employer must use the vehicle cents-per-mile valuation rule for all subsequent periods.* Once the vehicle cents-per-mile valuation rule has been adopted for a vehicle by an employer, the rule must be used by the employer for all subsequent periods in which the vehicle qualifies for use of the rule, except that (A) the employer may, for any period during which use of the vehicle qualifies for the commuting valuation rule of paragraph (f) of this section, use the commuting valuation rule with respect to the vehicle, and (B) if the employer elects to use the automobile lease valuation rule of paragraph (d) of this section for a period in which the vehicle does not qualify for use of the vehicle cents-per-mile valuation rule, then the employer must comply with the requirements of paragraph (d)(6) of this section. If the vehicle fails to qualify for use of the vehicle cents-per-mile valuation rule during a subsequent period, the employer may adopt for such subsequent period and thereafter any other special valuation rule for which the vehicle then qualifies. For purposes of paragraph (d)(6) of this section, the first day on which an automobile with respect to which the vehicle cents-per-mile rule had been used fails to qualify for use of the vehicle cents-per-mile valuation rule may be deemed to be the first day on which the automobile is available to an employee of the employer for personal use.

(iii) *Use of the vehicle cents-per-mile valuation rule by an employee.* An employee may adopt the vehicle cents-per-mile valuation rule for a vehicle only if the rule is adopted (A) by the employer and (B) with respect to the first period in which the vehicle for which the employer (consistent with paragraph (e)(5)(i) of this section) adopted the rule is available to that employee for personal use or, if the commuting valuation rule of paragraph (f) of this section is used by both the employer and the employee when the vehicle is first used by an employee for personal use, the first period in which the commuting valuation rule is not used.

(iv) *An employee must use the vehicle cents-per-mile valuation rule for all subsequent periods.* Once the vehicle cents-per-mile valuation rule has been adopted for a vehicle by an employee, the rule must be used by the employee for all subsequent periods of personal use of the vehicle by the employee for which the rule is used by the employer, except that the employee may, for any period during which use of the vehicle qualifies for use of the commuting valuation rule of paragraph (f) of this section and for which such rule is used by the employer, use the commuting valuation rule with respect to the vehicle.

(v) *Replacement vehicles.* Notwithstanding anything in this paragraph (e)(5) to the contrary, if the vehicle cents-per-mile valuation rule is used by an employer, or by an employer and an employee, with respect to a particular vehicle, and a replacement vehicle is provided to the employee for the primary purpose of reducing Federal taxes, then the employer, or the employer and the employee, using the rule must continue to use the rule with respect to the replacement vehicle if the replacement vehicle qualifies for use of the rule.

(f) *Commuting valuation rule*—(1) *In general.* Under the commuting valuation rule of this paragraph (f), the value of the commuting use of an employer-provided vehicle may be determined pursuant to paragraph (f)(3) of this section if the following criteria are met by the employer and employees with respect to the vehicle:

(i) The vehicle is owned or leased by the employer and is provided to one or more employees for use in connection with the employer's trade or business and is used in the employer's trade or business;

(ii) For bona fide noncompensatory business reasons, the employer requires the employee to commute to and/or from work in the vehicle;

(iii) The employer has established a written policy under which the employee may not use the vehicle for personal purposes, other than for commuting or de minimis personal use (such as a stop for a personal errand on the way between a business delivery and the employee's home);

(iv) Except for de minimis personal use, the employee does not use the vehicle for any personal purpose other than commuting; and

(v) The employee required to use the vehicle for commuting is not a control employee of the employer (as defined in paragraphs (f) (5) and (6) of this section).

If the vehicle is a chauffeur-driven vehicle, the commuting valuation rule of this paragraph (f) may not be used to value the commuting use of any passenger who commutes in the vehicle. The rule may be used, however, to value the commuting use of the chauffeur. Personal use of a vehicle is all use of the vehicle by the employee that is not used

in the employee's trade or business of being an employee of the employer.

(2) *Special rules.* Notwithstanding anything in paragraph (f)(1) of this section to the contrary, the following special rules apply—

(i) *Written policy not required in 1985.* The policy described in paragraph (f)(1)(iii) of this section prohibiting personal use need not be written with respect to the commuting use which occurs prior to January 1, 1986;

(ii) *Commuting use during 1985.* For commuting use that occurs after December 31, 1984, but before January 1, 1986, the restrictions of paragraph (f)(1)(v) of this section shall be applied by substituting "an employee who is an officer or a five-percent owner of the employer" in lieu of "a control employee". For purposes of determining who is a five-percent owner, any individual who owns (or is considered as owning) five or more percent of the fair market value of an entity (the "owned entity") is considered a five-percent owner of all entities that would be aggregated with the owned entity under the rules of section 414 (b), (c), or (m). An employee who is an officer of an employer shall be treated as an officer of all entities treated as a single employer pursuant to section 414 (b), (c), or (m). The definitions provided in paragraphs (f)(5)(i) and (f)(6) of this section may be used to define an officer; and

(iii) *Control employee exception.* If the vehicle in which the employee is required to commute is not an automobile as defined in paragraph (d)(1)(ii) of this section, the restrictions of paragraph (f)(1)(v) of this section do not apply.

(3) *Commuting value*—(i) *$1.50 per one-way commute.* If the requirements of this paragraph (f) are satisfied, the value of the commuting use of an employer-provided vehicle is $1.50 per one-way commute (e.g., from home to work or from work to home).

(ii) *Value per employee.* If there is more than one employee who commutes in the vehicle, such as in the case of an employer-sponsored car pool, the amount includible in the income of each employee is $1.50 per one-way commute. Thus, the amount includible for each round-trip commute is $3.00 per employee.

(4) *Definition of vehicle.* For purposes of this paragraph (f), the term "vehicle" means any motorized wheeled vehicle manufactured primarily for use on public streets, roads, and highways. The term "vehicle" includes an automobile as defined in paragraph (d)(1)(ii) of this section.

(5) *Control employee defined—Non-government employer.* For purposes of this paragraph (f), a control employee of a non-government employer is any employee—

(i) Who is a Board- or shareholder-appointed, confirmed, or elected officer of the employer,

(ii) Who is a director of the employer, or

(iii) Who owns a one-percent or greater equity, capital, or profits interest in the employer.

For purposes of determining who is a one-percent owner under paragraph (f)(5)(iii) of this section, any individual who owns (or is considered as owning under section 318(a) or principles similar to section 318(a) for entities other than corporations) one percent or more of the fair market value of an entity (the "owned entity") is considered a one-percent owner of all entities which would be aggregated with the owned entity under the rules of section 414 (b), (c), or (m). An employee who is an officer of an employer shall be treated as an officer of all entities treated as a single employer pursuant to section 414 (b), (c) or (m).

(6) *Control employee defined—Government employer.* For purposes of this paragraph (f), a control employee of a government employer if any—

(i) Elected official,

(ii) Federal employee who is appointed by the President and confirmed by the Senate. In the case of commissioned officers of the United States Armed Forces, an officer is any individual with the rank of brigadier general or above or the rank of rear admiral (lower half) or above; or

(iii) State or local executive officer comparable to the individuals described in paragraph (f)(6) (i) and (ii) of this section.

For purposes of this paragraph (f), the term "government" includes any Federal, state, or local governmental unit, and any agency or instrumentality thereof.

(g) *Non-commercial flight valuation rule*—(1) *In general.* Under the non-commercial flight valuation rule of this paragraph (g), if an employee is provided with a flight on an employer-provided aircraft, the value of the flight is calculated using the aircraft valuation formula provided in paragraph (g)(5) of this section. Except as otherwise provided, for purposes of this paragraph (g), a flight provided to a person whose flight would be taxable to an employee as the recipient is referred to as provided to the employee, and a flight taken by such person is considered a flight taken by the employee.

(2) *Eligible flights and eligible aircraft.* The valuation rule of this paragraph (g) may be used to value flights on all employer-provided aircraft, including helicopters. The valuation rule of this paragraph (g) may be used to value international as well as domestic flights. The valuation rule of this paragraph (g) may not be used to value a flight on any commercial aircraft on which air transportation is sold to the public on a per-seat basis. For a special valuation rule relating to certain flights on commercial aircraft, see paragraph (h) of this section.

(3) *Definition of a flight*—(i) *General rule.* Except as otherwise provided in paragraph (g)(3)(iii) of this section (relating to intermediate stops), for purposes of this paragraph (g), an individual's flight is the distance (in statute miles) between the place at which the individual boards the aircraft and the place at which the individual deplanes.

(ii) *Valuation of each flight.* Under the valuation rule of this paragraph (g), value is determined separately for each flight. Thus, a round-trip is comprised of at least two flights. For example, an employee who takes a personal trip on an employer-provided aircraft from New York, New York to Denver, Colorado, Denver to Los Angeles, California, and Los Angeles to New York has taken three flights and must apply the aircraft valuation formula separately to each flight. The value of a flight must be determined on a passenger-by-passenger basis. For example, if an individual accompanies an employee and the flight taken by the individual would be taxed to the employee, the employee would be taxed on the special rule value of the flight by the employee and by the individual.

(iii) *Intermediate stop.* If the primary purpose of a landing is necessitated by weather conditions, by an emergency, for purposes of refueling or obtaining other services relating to the aircraft, or for purposes of the employer's business unrelated to the employee whose flight is being valued ("an intermediate stop"), the distance between the place at which the trip originates and the place at which the intermediate stop occurs is not considered a flight. For example, assume that an employee's trip originates in St. Louis, Missouri, on route to Seattle, Washington, but, because of weather conditions, the aircraft lands in Denver, Colorado, and the employee stays in Denver overnight. Assume further that the next day the aircraft flies to Seattle where the employee deplanes. The employee's flight is the distance between the airport

in St. Louis and the airport in Seattle. Assume that a trip originates in New York, New York, with five passengers and makes an intermediate stop in Chicago, Illinois, before going on to Los Angeles, California. If one of the five passengers deplanes in Chicago, the distance of that passenger's flight would be the distance between the airport in New York and the airport in Chicago. The intermediate stop is disregarded when measuring the flights taken by each of the other passengers. Their flights would be the distance between the airport in New York and the airport in Los Angeles.

(4) *Personal and non-personal flights*—(i) *In general.* The valuation rule of this paragraph (g) applies to personal flights on employer-provided aircraft. A personal flight is one the value of which is not excludable under another section of subtitle A, such as under section 132(d) (relating to a working condition fringe). However, solely for purposes of paragraphs (g)(4)(ii) and (g)(4)(iii) of this section, references to personal flights do not include flights a portion of which would not be excludable by reason of section 274(c).

(ii) *Trip primarily for employer's business.* If an employee combines, in one trip, personal and business flights on an employer-provided aircraft and the employee's trip is primarily for the employer's business (see § 1.162–2(b)(2)), the employee must include in income the excess of the value of all the flights that comprise the trip over the value of the flights that would have been taken had there been no personal flights but only business flights. For example, assume that an employee flies on an employer-provided aircraft from Chicago, Illinois to Miami, Florida, for the employer's business and that from Miami the employee flies on the employer-provided aircraft to Orlando, Florida, for personal purposes and then flies back to Chicago. Assume further that the primary purpose of the trip is for the employer's business. The amount includible in income is the excess of the value of the three flights (Chicago to Miami, Miami to Orlando, and Orlando to Chicago), over the value of the flights that would have been taken had there been no personal flights but only business flights (Chicago to Miami and Miami to Chicago).

(iii) *Primarily personal trip.* In an employee combines, in one trip, personal and business flights on an employer-provided aircraft and the aircraft's trip is primarily personal (see § 1.162–2(b)(2)), the amount includible in the employee's income is the value of the personal flights that would have been taken had there been no business flights but only personal flights. For example, assume that an employee flies on an employer-provided aircraft from San Francisco, California, to Los Angeles, California, for the employer's business and that from Los Angeles the employee flies on an employer-provided aircraft to Palm Springs, California, primarily for personal reasons and then flies back to San Francisco. Assume further that the primary purpose of the trip is personal. The amount includible in the employee's income is the value of personal flights that would have been taken had there been no business flights but only personal flights (San Francisco to Palm Springs and Palm Springs to San Francisco).

(iv) *Application of section 274(c).* The value of employer-provided travel outside the United States away from home may not be excluded from the employee's gross income as a working condition fringe, by either the employer or the employee, to the extent not deductible by reason of section 274(c). The valuation rule of this paragraph (g) applies to that portion of the value of any flight not excludable by reason of section 274(c). Such value must be included in income in addition to the amounts determined under paragraphs (g)(4)(ii) and (g)(4)(iii) of this section.

(v) *Flight by individuals who are not personal guests.* If an individual who is not an employee of the employer providing the aircraft is on a flight, and the individual is not the personal guest of any employee, the flight by the individual is not taxable to any employee of the employer providing the aircraft. The rule in the preceding sentence applies where the individual is provided the flight by the employer for noncompensatory business reasons of the employer. For example, assume that G, and employee of company Y, accompanies A, an employee of company X, on company X's aircraft for the purpose of inspecting land under consideration for purchase by company X from company Y. The flight by G is not taxable to A.

(5) *Aircraft valuation formula.* Under the valuation rule of this paragraph (g), the value of a flight is determined by multiplying the base aircraft valuation formula for the period during which the flight was taken by the appropriate aircraft multiple (as provided in paragraph (g)(7) of this section) and then adding the applicable terminal charge. The base aircraft valuation formula (also known as the Standard Industry Fare Level formula or SIFL) in effect on June 30, 1985, is as follows: ($.1402 per mile for the first 500 miles, $.1069 per mile for miles between 501 and 1500, and $.1028 per mile for miles over 1500). The terminal charge in effect on June 30, 1985, is $25.62. The SIFL cents-per-mile rates in the formula and the terminal charge are calculated by the Department of Transportation and are revised semi-annually.

(6) *SIFL formula in effect for a particular flight.* For purposes of this paragraph (g), in determining the value of a particular flight during the first six months of a calendar year, the SIFL formula (and terminal charge) in effect on December 31 of the preceding year applies, and in determining the value of a particular flight during the last six months of a calendar year, the SIFL formula (and terminal charge) in effect on June 30 of that year applies. The following is the SIFL formula in effect on December 31, 1984: ($.1480 per mile for the first 500 miles, $.1128 per mile for miles between 501 and 1500, and $.1085 per mile for miles over 1500). The terminal charge in effect on December 31, 1984, is $27.05.

(7) *Aircraft multiples*—(i) *In general.* The aircraft multiples are based on the maximum certified takeoff weight of the aircraft. For purposes of applying the aircraft valuation formula described in paragraph (g)(5) of this section, the aircraft multiples are as follows:

[In percent]

Maximum certified takeoff weight of the aircraft	Aircraft multiple for a—	
	Control employee	Non-control employee
6,000 lbs. or less	62.5	15.6
6,001 to 10,000 lbs	125.0	23.4
10,001 to 25,000 lbs	300.0	31.3
25,001 lbs. or more	400.0	31.3

(ii) *Flights treated as provided a to control employee.* Except as provided in paragraph (g)(10) of this section, any flight provided to an individual whose flight would be taxable to a control employee (as defined in paragraph (g)(8) and (9) of this section) as the recipient shall be valued as if such flight has been provided to that control employee. For example, assume that the chief executive officer of an employer, his spouse, and his two children fly on an employer-provided aircraft for personal purposes. Assume further that the maximum certified takeoff weight of the aircraft is 12,000 lbs. The amount includible in the employee's income is 4 x ((300 percent x base aircraft valuation formula) plus the applicable terminal charge).

(8) *Control employee defined—Nongovernment employer.* For purposes of this paragraph (g), a control employee of a non-government employer is any employee—

(i) Who is a Board- or shareholder-appointed, confirmed, or elected officer of the employer, limited to the lesser of (A) one-percent of all employees (increased to the next highest integer, if not an integer) or (B) ten employees;

(ii) Whose compensation equals or exceeds the compensation of the top one percent most highly-paid employees of the employer (increased to the next highest integer, if not an integer) limited to a maximum of 25 employees;

(iii) Who owns a ten-percent or greater equity, capital or profits interest in the employer; or

(iv) Who is a director of the employer.

For purposes of this paragraph (g), any employee who is a family member (within the meaning of section 267(c)(4)) of a control employee is also a control employee. Pursuant to this paragraph (g)(8), an employee may be a control employee under more than one of the requirements listed in paragraphs (g)(8)(i) through (iv) of this section. For example, an employee may be both an officer under paragraph (g)(8)(i) of this section and a highly-paid employee under paragraph (g)(8)(ii) of this section. In this case, for purposes of the officer limitation rule of paragraph (g)(8)(i) of this section and the highly-paid employee limitation rule of paragraph (g)(8)(ii) of this section, the employee would be counted as reducing both such limitation rules. In no event shall an employee whose compensation is less than $50,000 be a control employee under paragraph (g)(8)(ii) of this section. For purposes of determining who is a ten-percent owner under paragraph (g)(8)(iii) of this section, any individual who owns (or is considered as owning under section 318(a) or principles similar to section 318(a) for entities other than corporations) ten percent or more of the fair market value of an entity (the "owned entity") is considered a ten-percent owner of all entities which would be aggregated with the owned entity under the rules of section 414 (b), (c), or (m). For purposes of determining who is an officer under paragraph (g)(8)(i) of this section, notwithstanding anything in this section to the contrary, if the employer would be aggregated with other employers under the rules of section 414 (b), (c), or (m), the officer definition and the limitations are applied to each separate employer rather than to the aggregated employer. If applicable, the officer limitation rule of paragraph (g)(8)(i) of this section is applied to employees in descending order of their compensation. Thus, if an employer has 11 board-appointed officers, the employee with the least compensation of those officers would not be an officer under paragraph (g)(8)(i) of this section. For purposes of this paragraph (g), the term "compensation" means the amount reported on a Form W-2 as income for the prior calendar year. Compensation includes all amounts received from all entities treated as a single employer under section 414 (b), (c), or (m).

(9) *Control employee defined—Government.* For purposes of this paragraph (g), a control employee of a government employer is any—

(i) Elected officials;

(ii) Federal employee who is appointed by the President and confirmed by the Senate. In the case of commissioned officers of the United States Armed Forces, an officer is any individual with the rank or brigadier general or above or the rank of rear admiral (lower half) or above; or

(iii) State or local executive officer comparable to the individuals in paragraph (g)(9)(i) and (ii) of this section.

For purposes of this paragraph (g), the term "government" includes any Federal, state, or local government unit, and any agency or instrumentality thereof.

(10) *Seating capacity rule*—(i) *In general.* Where 50 percent of more of the regular passenger seating capacity of an aircraft (as used by the employer) is occupied by individuals whose flights are primarily for the employer's business (and whose flights are excludable from income under section 132(d)), the value of a flight on that aircraft by any employee who is not flying primarily for the employer's business (or who is flying primarily for the employer's business but the value of whose flight is not excludable under section 132(d) by reason of section 274(c)) is deemed to be zero. See § 1.132-5T which limits the exclusion under section 132(d) to situations where the employee receives the flight in connection with the performance of services for the employer providing the aircraft. For purposes of this paragraph (g)(10), the term "employee" includes only employees and partners of the employer providing the aircraft and does not include independent contractors and directors of the employer.

For purposes of this paragraph (g)(10), the second sentence of paragraph (g)(1) of this section will not apply. Instead, a flight taken by an individual who is either treated as an employee pursuant to section 132(f)(1) or whose flight is treated as a flight taken by an employee pursuant to section 132(f)(2) is considered a flight taken by an employee. If (A) a flight is considered taken by an individual other than an employee (as defined in this paragraph (g)(10)), (B) the value of that individual's flight is not excludable under section 132(d), and (C) the seating capacity rule of this paragraph (g)(10) otherwise applies, then the value of the flight provided to such an individual is the value of a flight provided to a non-control employee (even if the individual who would be taxed on the value of such individual's flight is a control employee).

(ii) *Application of 50-percent test to multiple flights.* The seating capacity rule of this paragraph (g)(10) must be met both at the time the individual whose flight is being valued boards the aircraft and at the time the individual deplanes. For example, assume that employee A boards an employer-provided aircraft for personal purposes in New York, New York, and that at that time 80 percent of the regular passenger seating capacity of the aircraft is occupied by individuals whose flights are primarily for the employer's business (and whose flights are excludable from income under section 132(d)) ("the business passengers"). If the aircraft flies directly to Hartford, Connecticut where all of the passengers, including A, deplane, the requirements of the seating capacity rule of this paragraph (g)(10) have been satisfied. If instead, some of the passengers, including A, remain on the aircraft in Hartford and the aircraft continues on to Boston, Massachusetts, where they all deplane, the requirements of the seating capacity rule of this paragraph (g)(10) will not be satisfied unless at least 50 percent of the seats comprising the aircraft's regular passenger seating capacity were occupied by the business passengers at the time A deplanes in Boston.

(iii) *Regular passenger seating capacity.* The regular passenger seating capacity of an aircraft is the maximum number of seats that have at any time been on the aircraft (while owned or leased by the employer). Except to the extent excluded pursuant to paragraph (g)(10)(v) of this section, regular seating capacity includes all seats which may be occupied by members of the flight crew. It is irrelevant that on a particular flight, less than the maximum number of seats are available for use, because, for example, some of the seats are removed. When determining the maximum number of seats, those seats that cannot at any time be legally used during

takeoff and are not any time used during takeoff are not counted.

(iv) *Examples.* The rules of paragraph (g)(10)(iii) of this section are illustrated by the following examples:

Example (1). Employer A and employer B order the same aircraft, except that A orders it with 10 seats and B orders it with eight seats. A always uses its aircraft as a 10-seat aircraft; B always uses its aircraft as an eight-seat aircraft. The regular passenger seating capacity of A's aircraft is 10 and of B's aircraft is eight.

Example (2). Assume the same facts as in example (1), except that whenever A's chief executive officer and spouse use the aircraft eight seats are removed. Even if substantially all of the use of the aircraft is by the chief executive officer and spouse the regular passenger seating capacity of the aircraft is 10.

Example (3). Assume the same facts as in example (1), except that whenever more than eight people want to fly in B's aircraft, two extra seats are added. Even if substantially all of the use of the aircraft occurs with eight seats, the regular passenger seating capacity of the aircraft is 10.

(v) *Seats occupied by flight crew.* When determining the regular passenger seating capacity of an aircraft, any seat occupied by a member of the flight crew (whether or not such individual is an employee of the employer providing the aircraft) shall not be counted, unless the purpose of the flight by such individual is not primarily to serve as a member of the flight crew. If the seat occupied by a member of the flight crew is not counted as a passenger seat pursuant to the previous sentence, such member of the flight crew is disregarded in applying the 50 percent test described in the first sentence of paragraph (g)(10)(i) of this section. For example, assume that, prior to the application of this paragraph (g)(10)(v), the regular passenger seating capacity of an aircraft is two seats.

Assume further that an employee pilots the aircraft and that the employee's flight is not primarily for the employer's business. If the employee's spouse occupies the other seat for personal purposes, the seating capacity rule is not met and the value of both flights must be included in the employee's income. If, however, the employee's flight were primarily for the employer's business (unrelated to serving as a member of the flight crew), then the seating capacity rule is met and the value of the flight for the employee's spouse is deemed to be zero. If the employee's flight were primarily to serve as a member of the flight crew, then the seating capacity rule is not met and the value of a flight by any passenger for primarily personal reasons is not deemed to be zero.

(11) *Erroneous use of the non-commercial flight valuation rule*—(i) *In general.* If the non-commercial flight valuation rule of this paragraph (g) is used by an employer or a control employee, as the case may be, on a return as originally filed, on the grounds that either the control employee is not in fact a control employee, or that the aircraft is within a specific weight classification, and either position is subsequently determined to be erroneous, the valuation rule of this paragraph (g) (including paragraph (g)(13) of this section) is not available to value the flight taken by that control employee by the person or persons taking the erroneous position. With respect to the weight classifications, the previous sentence does not apply if the position taken is that the weight of the aircraft is greater than it is subsequently determined to be. If, with respect to a flight by a control employee, the seating capacity rule of paragraph (g)(10) of this section is used by an employer or the control employee, as the case may be, on a return as originally filed, and it is subsequently determined that the requirements of paragraph (g)(10) of this section were not met, the valuation rule of this paragraph (g) (including paragraph (g)(13) of this section) is not available to value the flight taken by that control employee by the person or persons taking the erroneous position.

(ii) *Value of flight excluded as a working condition fringe.* If either an employer or an employee, on a return as originally filed, excludes from the employee's income or wages the value of a flight on the grounds that the flight was excludable as a working condition fringe under section 132, and that position is subsequently determined to be erroneous, the valuation rule of this paragraph (g) (including paragraph (g)(13) of this section) is not available to value the flight taken by that employee by the person or persons taking the erroneous position.

(12) *Consistency rules*—(i) *Use by the employer.* Except as otherwise provided in paragraphs (g)(11) and (g)(13)(iv) of this section, if the non-commercial flight valuation rule of this paragraph (g) is used by an employer to value flights provided in a calendar year, the rule must be used to value all flights provided in the calendar year.

(ii) *Use by the employee.* Except as otherwise provided in paragraphs (g)(11) and (g)(13)(iv) of this section, if the non-commercial flight valuation rule of this paragraph (g) is used by an employee to value a flight taken in a calendar year, the rule must be used to value all flights taken in the calendar year.

(13) *Transitional valuation rule*—(i) *In general.* If the value of a flight determined under this paragraph (g)(13) is lower than the value of the flight otherwise determined under paragraph (g) of this section, the value of the flight is the lower amount. The transitional valuation rule of this paragraph (g)(13) is available only for flights provided after December 31, 1984, and before January 1, 1986.

(ii) *Transitional valuation rule aircraft multiples.* The appropriate aircraft multiples under the transitional valuation rule are as follows:

(A) 125 percent of the base aircraft valuation formula, plus the applicable terminal charge, for any flight by any employee who is not a key employee (as defined in paragraph (g)(13)(iii) of this section.)

(B) 125 percent of the base aircraft valuation formula, plus the applicable terminal charge, for a flight by a key employee if there is a primary business purpose of the trip by the aircraft. For purposes of this paragraph (g)(13)(ii) (B), entertaining an employee or other individual is not a business purpose.

(C) 600 percent of the base aircraft valuation formula, plus the applicable terminal charge, for a flight by a key employee if there is not primary business for the trip by the aircraft. Where there is no business purpose for the trip by the aircraft, the alternative valuation rule may not be used to value a flight by a key employee. For purposes of this section, compensating an employee is not a business purpose.

(iii) *Key employee defined.* A "key employee" is any employee who is a five-percent owner or an officer of the employer, or who, with respect to a particular trip by the aircraft, controls the use of the aircraft. For purposes of determining who is a five-percent owner, any individual who owns (or is considered as owning) five or more percent of the fair market value of an entity (the "owned entity") is considered a five-percent owner of all entities that would be aggregated with the owned entity under the rules of section 414(b), (c), or (m).

(iv) *Erroneous use of transitional valuation rule.* If the transitional valuation rule is used by an employer or a key employee, as the case may be, on a return as originally filed, on the grounds that—

(A) The key employee is not in fact a key employee,

(B) An aircraft trip had a primary business purpose, or

(C) An aircraft trip had some business purpose,

and such position is subsequently determined to be erroneous, neither the transitional valuation rule nor the non-commercial flight valuation rule of this paragraph (g) is available to value such flight taken by that key employee by the person or persons taking the erroneous position.

(h) *Commercial flight valuation rule*—(1) *In general.* Under the commercial flight valuation rule of this paragraph (h), the value of a space-available flight (as defined in paragraph (h)(2) of this section) on a commercial aircraft is 25 percent of the actual carrier's highest unrestricted coach fare in effect for the particular flight taken.

(2) *Space-available flight.* The commercial flight valuation rule of this paragraph (h) is available to value a space-available flight. The term "space-available flight" means a flight on a commercial aircraft (i) for which the airline (the acutal carrier) incurs no substantial additional cost (including forgone revenue) determined without regard to any amount paid for the flight and (ii) which is subject to the same types of restrictions customarily associated with flying on an employee "standby" or "space-available" basis. A flight may be a space-available flight even if the airline that is the actual carrier is not the employer of the employee.

(3) *Commercial aircraft.* If the actual carrier does not offer, in the ordinary course of its business, air transportation to customers on a per-seat basis, the commercial flight valuation rule of this paragraph (h) is not available. Thus, if, in the ordinary course of its line of business, the employer only offers air transportation to customers on a charter basis, the commerical flight valuation rule of this paragraph (h) may not be used to value a space-available flight on the employer's aircraft. Similarly, if, in the ordinary course of its line of business, an employer only offers air transportation to customers for the transport of cargo, the commercial flight valuation rule of this paragraph (h) may not be used to value a space-available flight on the employer's aircraft.

(4) *Timing of inclusion.* The date that the flight is taken is the relevant date for purposes of applying section 61(a)(1) and this section to a space-available flight on a commercial aircraft. The date of purchase or issuance of a pass or ticket is not relevant. Thus, this section applies to a flight taken on or after January 1, 1985, regardless of the date on which the pass or ticket for the flight was purchased or issued.

(5) *Consistency rules*—(i) *Use by employer.* If the commercial flight valuation rule of this paragraph (h) is used by an employer to value flights provided in a calendar year, the rule must be used to value all flights provided in the calendar year.

(ii) *Use by employee.* If the commercial flight valuation rule of this paragraph (h) is used by an employee to value a flight taken in a calendar year, the rule must be used to value all flights taken by such employee in the calendar year.

(i) [Reserved]

(j) *Valuation of meals provided at an employer-operated eating facility for employees*—(1) *In general.* The valuation rule of this paragraph (j) may be used to value a meal provided at an employer-operated eating facility for employees (as defined in § 1.132-7T). For rules relating to an exclusion for the value of meals provided at an employer-operated eating facility for employees, see § 1.132-7T.

(2) *Valuation formula*—(i) *In general.* The value of all meals provided at an employer-operated eating facility for employees during a calendar year is 150 percent of the direct operaitng costs of the eating facility ("total meal value"). For purposes of this paragraph (j), the definition of direct operating costs provided in § 1.132-7T applies. The taxable value of meals provided at an eating facility may be determined in two ways. The "individual meal subsidy" may be treated as the taxable value of a meal provided at the eating facility (see paragraph (j) (2) (ii) of this section). Alternatively, the employer may allocate the "total meal subsidy" among employees (see paragraph (j) (2) (iii) of this section).

(ii) *"Individual meal subsidy" defined.* The "individual meal subsidy" is determined by multiplying the price charged for a particular meal by a fraction, the numerator of which is the total meal value and the denominator of which is the gross receipts of the eating facility, and then subtracting the amount paid for the meal. The taxable value of meals provided to a particular employee during a calendar year, therefore, is the sum of the individual meal subsidies provided to the employee during the calendar year.

(iii) *Allocation of "total meal subsidy."* Instead of using the individual meal value method, the employer may allocate the "total meal subsidy" (total meal value less the gross receipts of the facility) among employees in any manner reasonable under the circumstances.

Par. 3. Section 1.132-1T is removed and a new § 1.132-1T is added in its place, as follows:

§ 1.132-1T Exclusion from gross income of certain fringe benefits (Temporary).

(a) *In general.* Gross income does not include any fringe benefit which qualifies as a—

(1) No-additional-cost service,

(2) Qualified employee discount,

(3) Working condition fringe, or

(4) De minimis fringe.

Special rules apply with respect to certain on-premises gyms and other athletic facilities (§ 1.132-1T (e)), demonstration use of employer-provided automobiles by full-time automobile salesmen (§ 1.132-1T (a)), parking provided to an employee on or near the business premises of the employer (§ 1.132-5T (o)), and on-premises eating facilities (§ 1.132-7T).

(b) *Definition of employee*—(1) *No-additional-cost services and qualified employee discounts.* For purposes of section 132 (a) (1) (relating to no-additional-cost services) and section 132 (a) (2) (relating to qualified employee discounts), the term "employee" (with respect to a line of business of an employer) means—

(i) Any individual who is currently employed by the employer in the line of business,

(ii) Any individual who was formerly employed by the employer in the line of business and who separated from service with the employer in the line of business by reason of retirement or disability, and

(iii) Any widow or widower of an individual who died while employed by the employer in the line of business or who separated from service with the employer in the line of business by reason of retirement or disability.

For purposes of this paragraph (b) (1), any partner who performs services for a partnership is considered employed by the partnership. In addition, any use by the spouse or dependent child (as defined in this paragraph (b)) of the employee will be treated as use by the employee.

(2) *Working condition fringes.* For purposes of section 132(a)(2) (relating to working condition fringes), the term "employee" means—

(i) Any individual who is currently employed by the employer,

(ii) Any partner who performs services for the partnership,

(iii) Any director of the employer, and

(iv) Any independent contractor who performs services for the employer.

Notwithstanding anything in this paragraph (b)(2) to the contrary, any independent contractor who performs services for the employer cannot exclude the value of parking or the use

of consumer goods provided pursuant to a product testing program under § 1.132–5T (n); in addition, any director of the employer cannot exclude the value of the use of consumer goods provided pursuant to a product testing program under § 1.132–5T (n).

(3) *De minimis fringe.* For purpose of section 132(a)(4) (relating to de minimis fringes), the term "employee" means any recipient of a fringe benefit.

(4) *Dependent child.* For purposes of this paragraph (b), the term "dependent child" means any son, stepson, daughter or stepdaughter of the employee who is a dependent of the employee, or both of whose parents are deceased. Any child to whom section 152(e) applies will be treated as the dependent of both parents.

(c) *Special rules for employers—Effect of section 414.* All employees treated as employed by a single employer under section 414(b), (c) or (m) will be treated as employed by a single employer for purposes of this section. Thus, employees of one corporation that is part of a controlled group of corporations may under certain circumstances be eligible to receive section 132 benefits from the other corporations that comprise the controlled group. However, the aggregation of employers described in this paragraph (c) does not change the other requirements for an exclusion, such as the line of business requirement. Thus, for example, if a controlled group of corporations consists of two corporations that operate in different lines of business, the corporations are not treated as operating in the same line of business even though the corporations are treated as one employer.

(d) *Customers not to include employees.* For purposes of section 132 and the regulations thereunder, the term "customer" means customers who are not employees. However, the preceding sentence does not apply to section 132(c)(2) (relating to the gross profit percentage for determining a qualified employee discount). Thus, an employer that provides employee discounts cannot exclude sales made to employees in determining the aggregate sales to customers.

(e) *Treatment of on-premises athletic facilities*—(1) *In general.* Gross income does not include the value of any on-premises athletic facility provided by the employer to its employees. For purposes of section 132 and this paragraph (e), the term "on-premises athletic facility" means any gym or other athletic facility (such as a pool, tennis court, or golf course)—

(i) Which is located on the premises of the employer,

(ii) Which is operated by the employer, and

(iii) Where substantially all of the use of which is, during the calendar year, by employees of the employer, their spouses, and their dependent children.

For purposes of this paragraph (e) (1) (iii), the term "dependent children" has the same meaning as the plural of the term "dependent child" in paragraph (b) (4) of this section. The exclusion of this paragraph (e) does not apply to any athletic facility if access to the facility is made available to the general public through the sale of memberships, the rental of the facility, etc.

(2) *Premises of the employer.* The athletic facility need not be located on the employer's business premises. However, the athletic facility must be located on premises of the employer. The exclusion provided in this paragraph (e) applies whether the premises are owned or leased by the employer; in addition, the exclusion is available even if the employer is not a named lesse on the lease so long as the employer pays reasonable rent. The exclusion provided in this paragraph (e) does not apply to any athletic facility that is a facility for residential use. Thus, for example, a resort with accompanying athletic facilities (such as tennis courts, pool, and gym) would not qualify for the exclusion provided in this paragraph (e).

(3) *Application of rules to membership in an athletic facility.* The exclusion provided in this paragraph (e) does not apply to any membership in an athletic facility (including health clubs or country clubs) unless the facility is owned (or leased) and operated by the employer and substantially all the use of the facility is by employees of the employer, their spouses, and their dependent children. Therefore, membership in health club or country club not meeting the rules provided in this paragraph (e) would not quality for the exclusion.

(4) *Operation by the employer.* An employer is considered to operate the athletic facility if the employer itself operates the facility through its own employees, or if the employer contracts out to another to operate the athletic facility. For example, if an employer hires an independent contractor to operate the athletic facility for the employer's employees, the facility is considered to be operated by the employer. In addition, if an athletic facility is operated by more than one employer, it is considered to be operated by each employer. For purposes of paragraph (e) (1) (iii) of this section, substantially all the use of a facility operated by more than one employer must be by employees of all of the employers, their spouses, and their dependent children. Where the facility is operated by more than one employer, an employer that either pays rent directly to the owner of the premises or pays rent to a named lessor of the premises is eligible for the exclusion.

(5) *Nonapplicability of nondiscrimination rules.* The nondiscrimination rules of section 132 and § 1.132–8T do not apply to on-premises athletic facilities.

(f) *Nonapplicability of section 132.* If the tax treatment of a particular fringe benefit is expressely provided for in another section of Chapter 1, section 132 and the applicable regulations (except for section 132 (e) and the regulations thereunder) do not apply to such fringe benefits. For example, since section 129 provides an exclusion from gross income for amounts paid or incurred by the employer for dependent care assistance for an employee, the exclusions under section 132 and this section do not apply to the provision by an employer to an employee of dependent care assistance.

Par. 4. The following new § 1.132–2T is added at the appropriate place:

§ 1.132-2T No-additional-cost service (Temporary).

(a) *In general*—(1) *Definition.* Gross income does not include the value of a no-additional-cost service. The term "no-additional-cost service" means any service provided by an employer to an employee for the employee's personal use if—

(i) The service is offered for sale to customers in the ordinary course of the line of business of the employer in which the employee performs substantial services, and

(ii) The employer incurs no substantial additional cost in providing the service to the employee (including forgone revenue and excluding any amount paid by or on behalf of the employee for the service).

For rules relating to the line of business limitation, see § 1.132–4T.

(2) *Examples.* Services that are eligible for treatment as no-additional-cost services are excess capacity services such as hotel accommodations; transportation by aircraft, train, bus, subway, or cruise line; and telephone services. Services that are not eligible for treatment as no-additonal-cost services are non-excess capacity services such as the facilitation by a stock brokerage firm of the purchase of stock. Employees who receive non-excess capacity services may, however,

be eligible for a qualified employee discount of up to 20 percent of the value of the service provided. See § 1.132-3T.

(3) *Cash rebates.* The exclusion for a no-additional-cost service applies whether the service is provided at no charge or at a reduced price. The exclusion also applies if the benefit is provided through a partial or total cash rebate of an amount paid for the service.

(4) *Applicability of nondiscrimination rules.* The exclusion for a no-additional-cost service applies to officers, owners, and highly compensated employees only if the service is available on substantially the same terms to each member of a group of employees that is defined under a reasonable classification set up by the employer that does not discriminate in favor of officers, owners, or highly compensated employees. See § 1.132-8T.

(5) *No substantial additional cost*—(i) *In general.* The exclusion for a non-additional-cost service applies only if the employer does not incur substantial additional cost in providing the service to the employee. For purposes of the preceding sentence, the term "cost" includes revenue that is forgone because the service is provided to an employee rather than a nonemployee. (For purposes of determining whether any revenue is forgone, it is assumed that the employee would not have purchased the service unless it were available to the employee at the actual price charged to the employee.) Whether an employer incurs substantial additional cost must be determined without regard to any amount paid by the employee for the service. Thus, any reimbursement by the employee for the cost of providing the service does not affect the determination of whether the employer incurs substantial additional cost.

(ii) *Labor intensive services.* An employer must include the cost of labor incurred in providing services to employees when determining whether the employer has incurred substantial additional cost. An employer has incurred substantial additional cost. An employer incurs substantial additional cost, whether or not non-labor costs are incurred, if a substantial amount of time is spent by the employer or its employees in providing the service to employees. This would be the result whether or not the time spent by the employer or its employees in providing the services would have been "idle", or if the services were provided outside normal business hours. An employer generally incurs no substantial additional cost, however, if the employee services provided are merely incidental to the primary service being provided by the employer. For example, the in-flight services of a flight attendant provided to airline employees traveling on a space-available basis are merely incidental to the primary service being provided (i.e., air transportation). In addition, the cost of in-flight meals provided to airline employees is not considered substantial in relation to the air transportation being provided.

(b) *Reciprocal agreements.* For purposes of the exclusion for a no-additional-cost service, any service provided by an employer to an employee of another employer shall be treated as provided by the employer of such employee if all of the following requirements are satisfied:

(1) The service is provided pursuant to a written reciprocal agreement between the employers under which a group of employees of each employer, all of whom perform substantial services in the same line of business, may receive no-additional-cost services from the other employer;

(2) The service provided pursuant to the agreement to the employees of both employers is the same type of service provided by the employers to customers both in the line of business in which the employees perform substantial services and the line of business in which the service is provided to customers; and

(3) Neither employer incurs substantial additional cost (including forgone revenue) in providing the service to the employees of the other employer or pursuant to the agreement. If one employer receives a substantial payment from the other employer with respect to the reciprocal agreement, the paying employer will be considered to have incurred a substantial additional cost pursuant to the agreement.

Par. 5. The following § 1.132-3T is added at the appropriate place:

§ 1.132-3T Qualified employee discount (Temporary).

(a) *In general*—(1) *Definition.* Gross income does not include the value of a qualified employee discount. The term "qualified employee discount" means any employee discount with respect to qualified property or services provided by an employer to an employee for the employee's personal use to the extent the discount does not exceed—

(i) The gross profit percentage of the price at which the property is offered to customers, for discounts on property, or

(ii) 20 percent of the price at which the services are offered to customers, for discounts on services.

(2) *Qualified property or services*—(i) *In general.* The term "qualified property or services" means any property or services that are offered for sale to customers in the ordinary course of the line of business of the employer in which the employee performs substantial services. For rules relating to the line of business limitation, see § 1.132-4T.

(ii) *Exception for certain property.* The term "qualified property" does not include real property and it does not include personal property (whether tangible or intangible) of a kind commonly held for investment. Thus, an employee may not exclude from gross income the amount of an employee discount provided on the purchase of either residential or commercial real estate, securities, commodities, or currency, whether or not the particular purchase is made for investment purposes.

(iii) *Property and services not offered in ordinary course of business.* The term "qualified property or services" does not include any property or services of a kind that is not offered for sale to customers in the ordinary course of the line of business of the employer. For example, employee discounts provided on property or services that are offered for sale only to employees and their families (such as merchandise sold at an employee store or through an employer-provided catalog service) may not be excluded from gross income.

(3) *No reciprocal agreement exception.* The exclusion for a qualified employee discount does not apply to property or services provided by another employer pursuant to a written reciprocal agreement that exists between employers to provide discounts on property and services to employees of the other employer.

(4) *Cash or third-party rebates*—(i) *Property or services provided without charge or at a reduced price.* The exclusion for a qualified employee discount applies whether the property or service is provided at no charge (in which case only part of the discount may be excludable as a qualified employee discount) or at a reduced price. The exclusion also applies if the benefit is provided through a partial or total cash rebate of an amount paid for the property or service.

(ii) *Property or services provided directly by the employer or indirectly through a third party.* A qualified employee discount may be provided either directly by the employer or indirectly through a third party. For example, an employee of an appliance manufacturer may receive a qualified employee discount on the manufacturer's appliances purchased at a retail store that offers such appliances for sale to customers. The employee may exclude the amount of the qualified

employee discount whether the employee is provided the appliance at no charge or purchases it at a reduced price, or whether the employee receives a partial or total cash rebate from either the employer-manufacturer or the retailer. If an employee receives additional rights associated with the property that are not provided by the employee's employer to customers in the ordinary course of the line of business in which the employee performs substantial services (such as the right to return or exchange the property or special warranty rights), the employee may only receive a qualified employee discount with respect to the property and not the additional rights. Receipt of such additional rights may occur, for example, when an employee of a manufacturer purchases property manufactured by the employee's employer at a retail outlet.

(5) *Applicability of nondiscrimination rules.* The exclusion for a qualified employee discount applies to officers, owners, and highly compensated employees only if the discount is available on substantially the same terms to each member of a group of employees that is defined under a reasonable classification set up by the employer that does not discriminate in favor of officers, owners, or highly compensated employees. See § 1.132-8T.

(b) *Employee discount*—(1) *Definition.* The term "employee discount" means the excess of—

(i) The price at which the property or service is being offered by the employer for sale to customers, over

(ii) The price at which the property or service is provided by the employer to an employee for use by the employee.

A transfer of property by an employee without consideration is considered use by the employee for purposes of this section. Thus, for example, if an employee receives a discount on property offered for sale by his employer to customers and the employee makes a gift of the property to his parent, the property will be considered to be provided for use by the employee, thus enabling the discount to be eligible for exclusion as a qualified employee discount.

(2) *Price to customers*—(i) *Determined at time of sale.* In determining the amount of an employee discount, the price at which the property or service is being offered to customers at the time of the employee's purchase is controlling. For example, assume that an employer offers a product to customers for $20 during the first six months of a calendar year but at the time the employee purchases the product at a discount, the price at which the product is being offered to customers is $25. In this case, the price from which the employee discount is measured is $25.

(ii) *Quantity discount not reflected.* The price referred to in paragraph (b)(2)(i) of this section cannot reflect any quantity discount unless the employee actually purchases the requisite quantity of the property or service.

(iii) *Customers of employee's employer controls.* In determining the amount of an employee discount, the price at which the property or service is offered to customers of the employee's employer is controlling. Thus, the price at which property is sold to the wholesale customers of a manufacturer will generally be lower than the price at which the same property is sold to the customers of a retailer. However, see paragraph (a)(4)(ii) of this section regarding the effect of a wholesaler providing to its employees additional rights not provided to customers of the wholesaler in the ordinary course of its business.

(iv) *Discounts to discrete customer or consumer groups.* In determining the amount of an employee discount, if an employer offers for sale property or services at one or more discounted prices to discrete customer or consumer groups, and sales at all such discounted prices comprise at least 35 percent of the employer's gross sales for a representative period, then the price at which property or service is being offered to customers is a discounted price. The applicable discounted price is the current undiscounted price, reduced by the percentage discount at which the greatest percentage of the employer's gross sales are made for such representative period. If sales at different percentage discounts equal the same percentage of the employer's gross sales, the price at which the property or service is being provided to customers may be reduced by the average of the two group discounts. For purposes of this section, a representative period is the taxable year of the employer immediately preceding the taxable year in which the property or service is provided to the employee at a discount. If more than one employer would be aggregated under section 414 (b), (c), or (m), and all of the employers do not have the same taxable year, the employers required to be aggregated must designate the 12-month period to be used in determining gross sales for a representative period.

(v) *Examples.* The rules provided in this paragraph (b)(2) are illustrated by the following examples:

Example (1). Assume that a wholesale employer offers property for sale to two discrete customer groups at differing prices. Assume further that during the prior taxable year of the employer, 70 percent of the employer's gross sales are made at a 15-percent discount and 30 percent at no discount. The current undiscounted price at which the property or service is being offered by the employer for sale to customers may be reduced by the 15-percent discount.

Example (2). Assume that a retail employer offers a 20 percent discount to members of the American Bar Association, a 15 percent discount to members of the American Medical Association, and a ten percent discount to employees of the Federal Government. Assume further that during the prior taxable year of the employer, sales to American Bar Association members equal 15 percent of the employer's gross sales, sales to American Medical Association members equal 20 percent of the employer's gross sales, and sales to Federal Government employees equal 25 percent of the employer's gross sales. The current undiscounted price at which the property or service is being offered by the employer for sale to customers may be reduced by the ten percent Federal Government discount.

(3) *Damaged, distressed, or returned goods.* If an employee pays at least fair market value for damaged, distressed, or returned property, such employee will not have income attributable to such purchase.

(c) *Gross profit percentage*—(1) *In general*—(i) *General rule.* An exclusion from gross income for an employee discount on qualified property is limited to the price at which the property is being offered to customers in the ordinary course of the employer's line of business, multiplied by the employer's gross profit percentage. The term "gross profit percentage" means the excess of the aggregate sales price of the property sold by the employer to customers (including employees) over the employer's aggregate cost of the property, then divided by the aggregate sales price.

(ii) *Calculation of gross profit percentage.* The gross profit percentage must be calculated separately for each line of business based on the aggregate sales price and aggregate cost of property in that line of business for a representative period. For purposes of this section, a representative period is the taxable year of the employer immediately preceding the taxable year in which the discount is available. For example, if the aggregate sales of property in an employer's line of business for the prior taxable year were $800,000, and the aggregate cost of the property for the year were $600,000, the gross profit percentage would be 25 percent ($800,000 minus $600,000, then

divided by $800,000). If more than one employer would be aggregated under section 414 (b), (c), or (m), and all of the employers do not have the same taxable year, the employers required to be aggregated must designate the 12-month period to be used in determining the gross profit percentage. If an employee performs substantial services in more than one line of business, the gross profit percentage of the line of business in which the property is sold determines the amount of the excludable employee discount.

(iii) *Special rule for employers in their first year of existence.* An employer in its first year of existence may estimate the gross profit percentage of a line of business based on its mark-up from the cost. Alternatively, an employer in its first year of existence may determine the gross profit percentage by reference to an appropriate industry average.

(iv) *Redetermination of gross profit percentage.* If substantial changes in an employer's business indicate at any time that it is inappropriate for the prior years' gross profit percentage to be used for the current year, the employer must, within a reasonable period, redetermine the gross profit percentage for the remaining portion of the current year as if such portion of the year were the first year of the employer's existence.

(2) *Line of business.* In general, an employer must determine the gross profit percentage on the basis of all property offered to customers (including employees) in each separate line of business. An employer may instead select a classification of property that is narrower than the applicable line of business. However, such classification must be reasonable. For example, if an employer computes gross profit percentage according to the department in which products are sold, such classification is reasonable. Similarly, it is reasonable to compute gross profit percentage on the basis of the type of merchandise sold (such as high mark-up and low mark-up classifications). It is not reasonable, however, for an employer to classify certain low mark-up products preferred by certain employees (such as officers, owners, and highly compensated employees) with high mark-up products or to classify certain high mark-up products preferred by other employees with low mark-up products.

(3) *Generally accepted accounting principles.* In general, the aggregate sales price of property must be determined in accordance with generally accepted accounting principles. An employer must compute the aggregate cost of property in the same manner in which it is computed for the employer's Federal income tax liability, pursuant to the inventory rules in section 471 and the regulations thereunder.

(d) *Treatment of leased sections of department stores*—(1) *In general*—(i) *General rule.* For purposes of determining whether employees of a leased section of a department store may receive qualified employees discounts at the department store and whether employees of the department store may receive qualified employee discounts at the leased section of the department store, the leased section is treated as part of the line of business of the person operating the department store, and employees of the leased section are treated as employees of the person operating the department store as well as employees of their employer. The term "leased section of a department store" means a section of a department store where substantially all of the gross receipts of the leased section are over-the-counter sales of property made under a lease, license, or similar arrangement where it appears to the general public that individuals making such sales are employed by the department store. An example of a leased section of a department store is a cosmetics firm that leases floor space from a department store.

(ii) *Calculation of gross profit percentage.* When calculating the gross profit percentage of property and services sold at the department store under paragraph (c) of this section, sales of property and services sold at the department store, as well as sales of property and services sold at the leased section, are considered. The rule provided in the preceding sentence does not apply, however, if it is reasonable to calculate the gross profit percentage for the department store and leased section separately, or if it would be inappropriate to combine them (such as where either the department store or the leased section, but not both, provides employee discounts).

(2) *Employees of the leased section*—(i) *Definition.* For purposes of this paragraph (d), "employees of the leased section" means all employees who perform substantial services at the leased section regardless of whether the employees engage in over-the-counter sales of property or services. The term "employee" has the same meaning as in section 133(f).

(iii) *Discounts offered to either department store employees or employees of the leased section.* If the requirements of this paragraph (d) are satisfied, employees of the leased section may receive qualified employee discounts at the department store regardless of whether employees of the department store are offered discounts at the leased section. Similarly, regardless of whether employees of the leased section are offered discounts at the department store, employees of the department store may receive qualified employee discounts at the leased section.

(e) *Excess discounts.* Unless excludable under a statutory provision other than section 132(a)(2), an employee discount provided on property is excludable to the extent of the gross profit percentage multiplied by the price at which the property is being offered for sale to customers. If an employee discount exceeds the gross profit percentage, the excess discount is includible in the employee's income. For example, if the discount on property is 30 percent and the employer's gross profit percentage for the period in the relevant line of business is 25 percent, then 5 percent of the price at which the property is being offered for sale to customers is includible in the emloyee's income. With respect to services, an employee discount of up to 20 percent may be excludable. If an employee discount exceeds 20 percent, the excess discount is includible in the employee's income.

Par. 6. The following § 1.132–4T is added at the appropriate place:

§ 1.132–4T Line of business limitation (Temporary).

(a) *In general*—(1) *Applicability*—(i) *General rule.* A no-additional-cost service or qualified employee discount provided to an employee must be for property or services that are offered for sale to customers in the ordinary course of the same line of business in which the employee receiving the property or service performs substantial services. Thus, an employee who does not perform substantial services in a particular line of business of the employer may not exclude the value of services or employee discounts received on property or services in that line of business.

(ii) *Property and services sold to employees rather than customers.* Since the property or services must be offered for sale to customers in the ordinary course of the same line of business in which the employee performs substantial services, the line of business limitation is not satisfied if the employer's products or services are sold to employees of the employer, rather than to customers. Thus, for example, an employer in the banking line of business is not considered in the variety store line of business if the employer

establishes an employee store that offers variety store items for sale to the employer's employees.

(iii) *Performance of substantial services in more than one line of business.* An employee who performs services in more than one of the employer's lines of business may only exclude no-additional-cost services and qualified employee discounts in the lines of business in which the employee performs substantial services.

(iv) *Performance of services that directly benefit more than one line of business*—(A) *In general.* An employee who performs substantial services that directly benefit more than one line of business of an employer is treated as performing substantial services in all such lines of business. For example, an employee who maintains accounting records for an employer's three lines of business may receive qualified employee discounts in all three lines of business.

(B) *Significantly interrelated minor line of business.* The employees of a minor line of business of an employer that is significantly interrelated with a major line of business of the employer who perform substantial services that directly benefit both the major and the minor lines of business are treated as employees of both the major and the minor lines of business. Employees of the minor line of business who do not perform substantial services which directly benefit the major line of business are not treated as employees of the major line of business. A minor line of business is significantly interrelated with a major line of business when, for example, the activity of the minor line of business is directly related to but is a minor part of the major line of business (such as laundry services provided at a hospital).

(C) *Examples.* The rules provided in this paragraph are illustrated in the following examples:

Example (1). Assume that employees of units of an employer provide repair or financing services, or sell by catalog, with respect to retail merchandise sold by the employer. Such employees may be considered as employees of the retail merchandise line of business under this paragraph (a)(1)(iv).

Example (2). Assume that an employer operates a hospital and a laundry service. Assume further that some of the gross receipts of the laundry service line of business are from laundry services sold to customers other than the hospital employer. Only the employees of the laundry service who perform substantial services which directly benefit the hospital line of business (through the provision of laundry services to the hospital) will be treated as employees of the hospital line of business. Other employees of the laundry service line of business will not be treated as employees of the hospital line of business.

Example (3). Assume the same facts as in example (2), except that the minor line of business also operates a chain of dry cleaning stores. Employees who perform substantial services which directly benefit the dry cleaning stores but who do not perform substantial services that directly benefit the hospital line of business will not be treated as employees of the hospital line of business.

(2) *Definition*—(i) *In general.* An employer's line of business is determined by reference to the Enterprise Standard Industrial Classification Manual (ESIC Manual) prepared by the Statistical Policy Division of the U.S. Office of Management and Budget. An employer is considered to have more than one line of business if the employer offers for sale to customers property or services in more than one two-digit code classification referred to in the ESIC Manual.

(ii) *Examples.* Examples of two-digit classifications are general retail merchandise stores; hotels and other lodging places; auto repair, services, and garages; and food stores.

(3) *Aggregation of two-digit classifications.* If, pursuant to paragraph (a)(2) of this section, an employer has more than one line of business, such lines of business will be treated as a single line of business where and to the extent that one or more of the following aggregation rules apply:

(i) If it is uncommon in the industry of the employer for any of the separate lines of business of the employer to be operated without the others, the separate lines of business are treated as one line of business.

(ii) If it is common for a substantial number of employees (other than those employees who work at the headquarters or main office of the employer) to perform substantial services for more than one line of business of the employer, so that determination of which employees perform substantial services for which line of business would be difficult, then the separate lines of business of the employer in which such employees perform substantial services are treated as one line of business. For example, assume that an employer operates a delicatessen with an attached service counter at which food is sold for consumption on the premises. Assume further that most but not all employees work both at the delicatessen and at the service counter. The delicatessen and the service counter are treated as one line of business.

(iii) If the retail operations of an employer that are located on the same premises are in separate lines of business but would be considered to be within one line of business under paragraph (a)(2) of this section if the merchandise offered for sale in such lines of business were offered for sale at a department store, then the operations are treated as one line of business. For example, assume that on the same premises an employer sells both women's apparel and jewelry. Since, if sold together at a department store, the operations would be part of the same line of business, the operations are treated as one line of business.

(b) *Grandfather rule for certain retail stores*—(1) *In general.* The line of business limitation may be relaxed under a special grandfather rule. If—

(i) On October 5, 1983, 85 percent of the employees of one member of an affiliated group (as defined in section 1504 without regard to subsections (b)(2) and (b)(4) thereof) were entitled to employee discounts at retail department stores operated by another member of the affiliated group, and

(ii) More than 50 percent of the current year's sales of the affiliated group are attributable to the operation of retail department stores,

then for purposes of the exclusion from gross income of a qualified employee discount, the first member is treated as engaged in the same line of business as the second member (the operator of the retail department stores). Therefore, employees of the first member of the affiliated group may exclude qualified employee discounts received at the retail department stores operated by the second member. However, employees of the second member of the affiliated group may not exclude any discounts received on property or services offered for sale to customers by the first member of the affiliated group.

(2) *Taxable year of affiliated group.* If all of the members do not have the same taxable year, the affiliated group must designate the 12-month period to be used in determining the "current year's sales" (as referred to in this paragraph (b)). The 12-month period designated, however, must be used consistently.

(3) *Definition of "sales".* For purposes of this paragraph (b), the term "sales" means the gross receipts of the affiliated group, based upon the accounting methods used by its members.

(4) *Retired and disabled employees.* For purposes of this paragraph (b), an employee includes any individual who was, or whose spouse was, formerly employed by the first member of the affiliated group and who separated from

service with the member by reason of retirement or disability if the second member of the group provided employee discounts to such individuals on October 5, 1983.

(5) *Increase of employee discount.* If, after October 5, 1983, the employee discount described in this paragraph (b) is increased, the grandfather rule of this paragraph (b) does not apply to the amount of the increase. For example, if on January 1, 1985, the employee discount is increased from 10 percent to 15 percent, the grandfather rule will not apply to the additional five percent discount.

(c) *Relaxation of line of business requirement.* The line of business requirement may be relaxed under an elective grandfather rule provided in section 4977. For rules relating to the section 4977 election, see § 54.4977-1.

Par. 7. The following § 1.132-5T is added at the appropriate place:

§ 1.132-5T Working condition fringe (Temporary).

(a) *In general*—(1) *Definition.* Gross income does not include the value of a working condition fringe. The term "working condition fringe" means any property or service provided to an employee of an employer to the extent that, if the employee paid for the property or service, the amount paid would be allowable as a deduction under section 162 or 167. If, under section 274 or any other section, certain substantiation requirements must be met in order for a deduction under section 162 or 167 to be allowable, those substantiation requirements apply to the determination of a working condition fringe. An amount that would be deductible by the employee under, for example, section 212 is not a working condition fringe.

(2) *Trade or business of the employee.* If the hypothetical payment for the property or service would be allowable as a deduction with respect to a trade or business of the employee other than the employee's trade or business of being an employee of the employer, it cannot be taken into account for purposes of determining the amount, if any, of the working condition fringe. For example, assume that, unrelated to company X's trade or business and unrelated to company X's employee's trade or business of being an employee of company X, the employee is a member of the board of directors of company Y. Assume further that company X provides the employee with air transportation to a company Y board of director's meeting. The employee may not exclude the value of the air transportation to the meeting as a working condition fringe. The employee may, however, deduct such amount under section 162 if the section 162 requirements are satisfied. The result would be the same whether the air transportation was provided in the form of a flight on a commercial airline or a seat on a company X airplane.

(b) *Vehicle allocation rules*—(1) *In general*—(i) *General rule.* In general, with respect to an employer-provided vehicle, the amount excludable as a working condition fringe is the amount that would be allowable as a deduction under section 162 or 167 if the employee paid for the availability of the vehicle. For example, assume that the value of the availability of an employer-provided vehicle for a full year is $2,000, without regard to any working condition fringe (i.e., assuming all personal use). Assume further that the employee drives the vehicle 6,000 miles for his employer's business and 2,000 miles for reasons other than the employer's business. In this situation, the value of the working condition fringe is $2,000 multiplied by a fraction, the numerator of which is the business-use mileage (6,000 miles) and the denominator of which is the total mileage (8,000 miles). Thus, the value of the working condition fringe is $1,500. The total amount includable in the employee's gross income on account of the availability of the vehicle is $500. For purposes of this section, the term "vehicle" has the same meaning given the term in § 1.61-2T(e)(2). Generally, when determining the amount of an employee's working condition fringe, miles accumulated on the vehicle by all employees of the employer during the period in which the vehicle is available to the employee must be considered. For example, assume that an employee of the employer is provided the availability of an automobile for one year. Assume further that during the year, the automobile is regularly used in the employer's business by other employees. All miles accumulated on the automobile by all employees of the employer during the year must be considered. If, however, substantially all the use of the automobile by other employees in the employer's business is permitted during a certain period, such as the last three months of the year, the miles driven by the other employees during that period would not be considered when determining the employee's working condition fringe exclusion.

(ii) *Use by an individual other than the employee.* For purposes of this section, if the availability of a vehicle to an individual would be taxed to an employee, use of the vehicle by the individual is included in references to use by the employee.

(iii) *Provision of an expensive vehicle for personal use.* Assume an employer provides an employee with an expensive vehicle that an employee may use in part for personal purposes. Even though the decision to provide an expensive rather than an inexpensive vehicle is made by the employer for bona fide noncompensatory business reasons, there is no working condition fringe exclusion with respect to the personal miles driven by the employee. If the employee paid for the availability of the vehicle, he would not be entitled to deduct any part of the payment attributable to personal miles.

(2) *Use of different employer-provided automobiles.* The working condition fringe exclusion must be applied on an automobile by automobile basis. For example, assume that automobile Y is available to employee D for 3 days in January and for 5 days in March, and automobile Z is available to D for a week in July. Assume further that the Daily Lease Value, as defined in § 1.61-2T, of each automobile is $50. For the eight days of availability of Y in January and March, D uses Y 90 percent for business (by mileage). During July, D uses Z 60 percent for business (by mileage). The value of the working condition fringe is determined separately for each automobile. Therefore, the working condition fringe for Y is $360 ($400 x .90) leaving an income inclusion of $40. The working condition fringe for Z is $210 ($350 x .60) leaving an income inclusion of $140. If the value of the availability of an automobile is determined under the Annual Lease Value rule for one period and Daily Lease Value rule for a second period (see § 1.61-2T), the working condition fringe exclusion must be calculated separately for the two periods.

(c) *Applicability of sections 162 and 274(d)*—(1) *In general.* The value of property or services provided to an employee may not be excluded from the employee's gross income as a working condition fringe, by either the employer or the employee, unless the applicable substantiation requirements of either section 274(d) or section 162 (whichever is applicable) and the regulations thereunder are satisfied. With respect to listed property, the substantiation requirements of section 274(d) and the regulations thereunder do not apply to the determination of an employee's working condition fringe exclusion prior to the date that those requirements apply to the first taxable year of the employer beginning after December 31,

1985. For example, if an employer's first taxable year beginning after December 31, 1985, begins on July 1, 1986, with respect to listed property, the substantiation requirements of section 274(d) apply as of that date. The substantiation requirements of section 274(d) apply to an employee even if the requirements of section 274 do not apply to the employee's employer for deduction purposes (such as when the employer is a tax-exempt organization or a governmental unit); in these cases, the requirements of section 274(d) apply to the employee as of January 1, 1986.

(2) *Section 274(d) requirements.* The substantiation requirements of section 274(d) are satisfied by "adequate records or sufficient evidence corroborating the [employee's] own statement". Therefore, such records or evidence provided by the employee, and relied upon by the employer to the extent permitted by the regulations promulgated under section 274(d), will be sufficient to substantiate a working condition fringe exclusion.

(d) *Safe harbor rules*—(1) *In general.* Section 1.274–6T provides that the substantiation requirements of section 274(d) and the regulations thereunder may be satisfied, in certain circumstances, by using one or more of the safe harbor rules prescribed in § 1.274–6T. If the employer uses one of the safe harbor rules prescribed in § 1.274–6T during a period with respect to a vehicle (as defined in § 1.61–2T), that rule must be used by the employer to substantiate a working condition fringe exclusion with respect to that vehicle during the period. An employer that is exempt from Federal income tax may still use one of the safe harbor rules (if the requirements of that section are otherwise met during a period) to substantiate a working condition fringe exclusion with respect to a vehicle during the period. If the employer uses one of the methods prescribed in § 1.274–6T during a period with respect to an employer-provided vehicle, that method may be used by an employee to substantiate a working condition fringe exclusion with respect to the same vehicle during the period, as long as the employee includes in gross income the amount allocated to the employee pursuant to § 1.274–6T and this section. (See § 1.61–2T(c)(2)(i) for other rules concerning when an employee must include in income the amount determined by the employer.) If, however, the employer uses the safe harbor rule prescribed in § 1.274–6T(a)(2) or (3) and the employee without the employer's knowledge uses the vehicle for purposes other than de minimis personal use (in the case of the rule prescribed in § 1.274–6T(a)(2)), or for purposes other than de minimis personal use and commuting (in the case of the rule prescribed in § 1.274–6T(a)(3)), then the employee must include additional income for the unauthorized use of the vehicle.

(2) *Period for use of safe harbor rules.* The rules prescribed in this paragraph (d) assume that the safe harbor rules prescribed in § 1.274–6T are used for a one-year period. Accordingly, references to the value of the availability of a vehicle, amounts excluded as a working condition fringe, etc., are based on a one-year period. If the safe harbor rules prescribed in § 1.274–6T are used for a period of less than a year, the amounts referenced in the previous sentence must be adjusted accordingly. For purposes of this section, the term "personal use" has the same meaning as prescribed in § 1.274–6T(e)(5).

(e) *Vehicles not available to employees for personal use.* For a vehicle described in § 1.274–6T(a)(2) (relating to certain vehicles not used for personal purposes), the working condition fringe exclusion is equal to the value of the availability of the vehicle if the employer uses the method prescribed in § 1.274–6T(a)(2).

(f) *Vehicles not available to employees for personal use other than commuting.* For a vehicle described in § 1.274–6T(a)(3) (relating to certain vehicles not used for personal purposes other than commuting), the working condition fringe exclusion is equal to the value of the availability of the vehicle for purposes other than commuting if the employer uses the method prescribed in § 1.274–6T(a)(3). This rule applies only if the special rule for valuing commuting use, as prescribed in § 1.61–2T, is used and the amount determined under the special rule is either included in the employee's income or reimbursed by the employee.

(g) *Vehicles used in connection with the business of farming that are available to employees for personal use*—(1) *In general.* For a vehicle described in § 1.274–6T(b) (relating to certain vehicles used in connection with the business of farming), the working condition fringe exclusion is calculated by multiplying the value of the availability of the vehicle by 75 percent.

(2) *Vehicles available to more than one individual.* If the vehicle is available to more than one individual, the employer must allocate the gross income attributable to the vehicle (25 percent of the value of the availability of the vehicle) among the employees (and other individuals whose use would not be attributed to an employee) to whom the vehicle was available. This allocation must be done in a reasonable manner to reflect the personal use of the vehicle by the individuals. An amount that would be allocated to a sole proprietor reduces the amounts that may be allocated to employees but are otherwise to be disregarded for purposes of this paragraph (g). For purposes of this paragraph (g), the value of the availability of a vehicle may be calculated as if the vehicle were available to only one employee continuously and without regard to any working condition fringe exclusion.

(3) *Examples.* The following examples illustrate a reasonable allocation of gross income with respect to an employer-provided vehicle between two employees:

Example (1). Assume that two farm employees share the use of a vehicle which for a calendar year is regularly used directly in connection with the business of farming and qualifies for use of the rule in § 1.274–6T (b). Employee A uses the vehicle in the morning directly in connection with the business of farming and employee B uses the vehicle in the afternoon directly in connection with the business of farming. Assume further that employee B takes the vehicle home in the evenings and on weekends. The employer should allocate all the income attributable to the availability of the vehicle to employee B.

Example (2). Assume that for a calendar year, farm employees C and D share the use of a vehicle that is regularly used directly in connection with the business of farming and qualifies for use of the rule in § 1.274–6T (b). Assume further that the employees alternate taking the vehicle home in the evening and alternate the availability of the vehicle for personal purposes on weekends. The employer should allocate the income attributable to the availability of the vehicle for personal use (25 percent of the value of the availability of the vehicle) equally between the two employees.

Example (3). Assume the same facts as in example (2) except that C is the sole proprietor of the farm. Based on these facts, C should allocate the same amount of income to D as was allocated to D in example (2). No other income attributable to the availability of the vehicle for personal use should be allocated.

(h) *Qualified non-personal use vehicles.* Effective January 1, 1985, 100 percent of the value of the use of a qualified nonpersonal use vehicle (as described in § 1.274–5T (k)) is excluded from gross income as a working condition fringe, provided that, in the case of a vehicle described in paragraph (k) (3) through (7) of that section, the use of the vehicles conforms to the requirements of that paragraph.

(i) [Reserved].

(j) *Application of section 280F.* In determining the amount, if any, of an employee's working condition fringe, section 280F and the regulations thereunder do not apply. For example, assume that an employee has available for a calendar year an employer-provided automobile with a fair market value of $28,000. Assume further that the special rule provided in § 1.61-2T is used and that the Annual Lease Value, as defined in § 1.61-2T, is $7,750, and that all of the employee's use of the automobile is in the employer's business. The employee would be entitled to exclude the entire Annual Lease Value as a working condition fringe, despite the fact that if the employee paid for the availability of the automobile, an income inclusion would be required under § 1.280F-5T(d)(1). This paragraph (j) does not affect the applicability of section 280F to the employer with respect to such employer-provided automobile, nor does it affect the applicability of section 274. For rules concerning substantiation of an employee's working condition fringe, see paragraph (c) of this section.

(k) *Aircraft allocation rule.* In general, with respect to a flight on an employer-provided aircraft, the amount excludable as a working condition fringe is the amount that would be allowable as a deduction under section 162 or 167 if the employee paid for the flight on the aircraft. For example, if employee P flies on P's employer's airplane primarily for business reasons of P's employer, the value of P's flight is excludable as a working condition fringe. However, if P's spouse and children accompany P on such airplane trip primarily for personal reasons, the value of the flights by P's spouse and children are includable in P's gross income. See § 1.61-2T(g) for special rules for valuing personal flights.

(l) [Reserved].

(m) *Employer-provided transportation for security concerns*—(1) *In general.* The amount of a working condition fringe exclusion with respect to employer-provided transportation is the amount that would be allowable as a deduction under section 162 or 167 if the employee paid for the transportation. Generally, if an employee pays for transportation taken for primarily personal purposes, the employee may not deduct any part of the amount paid. Thus, the employee may not generally exclude the value of employer-provided transportation as a working condition fringe if such transportation is primarily personal. If, however, for bona fide business-oriented security concerns, the employee purchases transportation that provides him or her with additional security, the employee may generally deduct the excess of the amount paid for the transportation over the lesser amount the employee would have paid for the same mode of transportation absent the bona fide business-oriented security concerns. With respect to a vehicle, the phrase "the same mode of transportation" means use of the same vehicle without the additional security aspects, such as bulletproof glass. With respect to air transportation, the phrase "the same mode of transportation" means comparable air transportation. These same rules apply to the determination of an employee's working condition fringe exclusion. For example, if an employer provides an employee with an automobile for commuting and, for bona fide business-oriented security concerns, the automobile is specially designed for security, then the employee may exclude the value of the special security design as a working condition fringe if the employee's automobile would not have had such security design but for the bona fide business-oriented security concerns. The employee may not exclude the value of the commuting from income as a working condition fringe because commuting is a nondeductible personal expense. Similarly, if an employee travels on a personal trip in an employer-provided aircraft for bona fide business-oriented security concerns, the employee may exclude the excess, if any, of the value of the flight over the amount the employee would have paid for comparable air transportation, but for the bona fide business-oriented security concerns. Because personal travel is a nondeductible expense, the employee may not exclude the total value of the trip as a working condition fringe.

(2) *Demonstration of bona fide business-oriented security concerns*—(i) *In general.* For purposes of this paragraph (m), the existence of a bona fide business-oriented security concern for the furnishing of a specific form of transportation to an employee is determined on the basis of all the facts and circumstances within the following guidelines:

(A) *Services performed outside the United States.* With respect to an employee performing services for an employer in a geographic area other than the United States, a factor indicating a bona fide business-oriented security concern is a recent history of violent terrorist activity in such geographic area (such as bombings or abductions for ransom), unless such activity is focused on a group of individuals which does not include the employee or a similarly situated employee or on a section of the geographic area which does not incude the employee.

(B) *Services performed in the United States.* With respect to an employee performing services for an employer in the United States, a factor indicating a bona fide business-oriented security concern is threats on the life of the employee or on the life of a similarly situafed employee because of the employee's status as an employee of the employer.

(ii) *Establishment of overall security program.* Notwithstanding anything in paragraph (m)(2)(i) of this section to the contrary, *no* bona fide business-oriented security concern will be deemed to exist unless the employee's employer establishes an overall security program with respect to the employee involved.

(iii) *Overall security program*—(A) *Definition.* An overall security program is one in which security is provided to protect the employee on a 24-hour basis. The employee must be protected while at the employee's residence, while commuting to and from the employee's workplace, and while at the employee's workplace. In addition, the employee must be protected while traveling, whether for business or personal purposes. An overall security program would include the provision of a bodyguard/driver who is trained in evasive driving techniques; and automobile specially equipped for security; guards, metal detectors, alarms, or similar methods of controling access to the employee's workplace and residence; and, in appropriate cases, flights on the employer's aircraft for business and personal reasons.

(B) *Application.* There is no overall security program when, for example, security is provided at the employee's workplace but not at the employee's residence. In addition, the fact that an employer requires an employee to travel on the employer's aircraft, or in an employer-provided vehicle that contains special security features, does not alone constitute an overall security program. The preceding sentence applies regardless of the existence of a corporate or other resolution requiring the employee to travel in the employer's airplane or vehicle for personal as well as business reasons. Similarly, the existence of an independent security study particular to the employer and its employees, or to the employee involved, does not alone constitute an overall security program.

(iv) *Effect of an independent security study.* An overall security program with respect to an employee is deemed to exist even though security is not

provided to an employee on a 24-hour basis if the conditions of this paragraph (m)(2)(iv) are satisfied:

(A) A security study is performed with respect to the employer and the employee (or a similarly situated employee) by an independent security consultant;

(B) The security study is based on an objective assessment of all the facts and circumstances;

(C) The recommendation of the security study is that an overall security program (as defined in paragraph (m)(2)(iii) of this section) is not necessary and such recommendation is reasonable under the circumstances; and

(D) The employer applies the specific security recommendations contained in the security study to the employee on a consistent basis.

The value of the security provided pursuant to a security study that meets the requirements of this paragraph (m)(2)(iv) may be excluded from income, if the security study conclusions are reasonable and, but for the bona fide business-oriented security concerns, the employee would not have had such security. No exclusion from income applies to security provided by the employer that is not recommended in the security study. Security study conclusions may be reasonable even if, for example, it is recommended that security be limited to certain geographic areas, as in the case where air travel security is provided only in certain foreign countries.

(v) *Application of security rules to spouses and dependents.* The availability of a working condition fringe exclusion based on the existence of a bona fide business-oriented security concern with respect to the spouse and dependents of an employee is determined separately for such spouse and dependents under the rules established in this paragraph (m).

(vi) *Working condition safe harbor.* Under the special rule of this paragraph (m)(2)(vi), if, for a bona fide business-oriented security concern, the employer requires that the employee travel on an employer-provided aircraft for a personal trip, the employer and the employee may exclude, as a working condition fringe, the excess value of the trip over comparable first-class airfare without having to show that but for the bona fide business-oriented security concerns, the employee would have flown first-class on a commercial aircraft. If the special valuation rule provided in § 1.61–2T is used, the excess over the amount determined by multiplying an aircraft multiple of 200-percent by the base aircraft valuation formula may be excluded as a working condition fringe.

(3) *Examples.* The provisions of this paragraph (m) may be illustrated by the following examples:

Example (1). Assume that in response to several death threats on the life of A, the president of a multinational company (company X), company X establishes an overall security program for A, including an alarm system at A's home and guards at A's workplace, the use of a vehicle that is specially equipped with alarms, bulletproof glass, and armor plating and a bodyguard/driver who is trained in evasive driving techniques. Assume further that A is driven for both personal and business reasons in the vehicle. Also, assume that but for the bona fide business-oriented security concerns, no part of the overall suecurity program would been provided to A. With respect to the transportation provided for security reasons, A may exclude as a working condition fringe the value of the special security features of the vehicle and the value attributable to the bodyguard/driver. Thus, if the value of the specially equipped vehicle is $40,000, and the value of the vehicle without the security features is $25,000, A may determine A's income attributable to the vehicle as if the vehicle were worth $25,000. A must include in income the value of the availability of the vehicle for personal use.

Example (2). Assume that B is the chief executive officer of a multinational corporation (company Y). Assume further that there have been kidnapping attempts and other terrorist activities in the foreign countries in which B performs services and that at least some of such activities have been directed against B or similarly situated employees. In response to these activities, company Y provides B with an overall security program, including an alarm system at B's home and bodyguards at B's workplace, a bodyguard/driver who is trained in evasive driving techniques, and a vehicle specially designed for security during B's overseas travels. In addition, assume that company Y requires B to travel in company Y's airplane for business and personal trips taken to, from, and within these foreign countries. Also, assume that but for bona fide business-oriented security concerns, no part of the overall sucurity program would have been provided to B. B may exclude as a working condition fringe the value of the special security features of the automobile and the value attributable to the bodyguards and the bodyguard/driver. B may also exclude as a working condition fringe the excess, if any, of the value of personal flights in the company Y airplane over first-class airfare (as determined under the special valuation rule provided in § 1.61–2T if the safe harbor described in paragraph (m)(2)(vi) of this section is used). B must include in income the value of the availability of the vehicle for personal use and the lesser of the value of first-class airfare or the value of the flight determined under § 1.61–2T for each personal flight taken by B in company Y's airplane.

Example (3). Assume the same facts as in example (2) except that company Y also requires B to travel in company Y's airplane within the United States, and provides B with a chauffeur-driven limousine for business and personal travel in the United States. Assume further that company Y also requires B's spouse and dependents to travel in company Y's airplane for personal flights in the United States. If no bona fide business-oriented security concern exists with respect to travel in the United States, B may not exclude any portion of the value of the availability of the driver or limousine for personal use in the United States. Thus, B must include in income the value of the availability of the vehicle and driver for personal use. In addition, B may not exclude any portion of the value attributable to personal flights by B or B's spouse and dependents on company Y's airplane. Thus, B must include in income the value attributable to the personal use of company Y's airplane. See § 1.61–2T for rules relating to the valuation of personal flights on employer-provided airplanes.

Example (4). Assume that company Z retains an independent security consultant to perform a security study with respect to its chief executive officer. Assume further that, based on an objective assessment of the facts and circumstances, the security consultant reasonably recommends that the employee be provided security at his workplace and for ground transportation, but not for air transportation. If company Z follows the recommendations on a consistent basis, an overall security program will be deemed to exist with respect to the workplace and ground transportation security only.

Example (5). Assume the same facts as in example (4) except that company Z only provides the employee security while commuting to and from work, but not for any other ground transportation. Since the recommendations of the independent security study are not applied on a consistent basis, an overall security program will not be deemed to exist.

(n) *Product testing*—(1) *In general.* The fair market value of the use of consumer goods, which are manufactured for sale to nonemployees, for product testing and evaluation by an employee outside the employer's workplace is excludable as a working condition fringe if—

(i) Consumer testing and evaluation of the product is an ordinary and necessary business expense of the employer,

(ii) Business reasons necessitate that the testing and evaluation of the product be performed off the employer's business premises by employees (i.e., the testing and evaluation cannot be carried out adequately in the employer's office or in laboratory testing facilities),

(iii) The product is furnished to the employee for purposes of testing and evaluation,

(iv) The product is made available to the employee for no longer than

necessary to test and evaluate its performance and must be returned to the employer at completion of the testing and evaluation period,

(v) The employer imposes limitations of the employee's use of the product which significantly reduce the value of any personal benefit to the employee, and

(vi) The employee must submit detailed reports to the employer on the testing and evaluation.

The length of the testing and evaluation period must be reasonable in relation to the product being tested.

(2) *Employer-imposed limitations.* The requirement of paragraph (n)(1)(v) of this section is satisfied if—

(i) The employer places limitations on the employee's ability to select among different models or varieties of the consumer product that is furnished for testing and evaluation purposes,

(ii) The employer's policy provides for the employee, in appropriate cases, to purchase or lease at his or her own expense the same type of product as that being tested (so that personal use by the employee's family will be limited), and

(iii) The employer generally prohibits use of the product by members of the employee's family.

(3) *Discriminating classifications.* If an employer furnishes products under a testing and evaluation program only to officers, owners, or highly compensated employees, this fact may be considered in a determination of whether the products are furnished for testing and evaluation purposes or for compensation purposes, unless the employer can show a business reason for the classification of employees to whom the products are furnished (e.g., that automobiles are furnished for testing and evaluation by an automobile manufacturer to its design engineers and supervisory mechanics).

(4) *Factors that negate the existence of a product testing program.* If an employer fails to tabulate and examine the results of the detailed reports within a reasonable period of time after expiration of the testing period, the program will not be considered a product testing program. Existence of one or more of the following factors may also establish that the program is not a bona fide product testing program:

(i) The program is in essence a leasing program under which employees lease the consumer goods from the employer for a fee;

(ii) The nature of the product and other considerations are insufficient to justify the testing program; or

(iii) The expense of the program outweighs the benefits to be gained from testing and evaluation.

(5) *Failure to meet the requirements of this paragraph (n).* The fair market value of the use of property for product testing and evaluation by an employee outside the employee's workplace, under a product testing program that does not meet all of the requirements of this paragraph (n), is not excludable as a working condition fringe.

(6) *Example.* Assume that an employer that manufactures automobiles establishes a product testing program under which 50 of its 5,000 employees test and evaluate the automobiles for 30 days. Assume further that the 50 employees represent a fair cross section of all of the employees of the employer, such employees submit detailed reports to the employer on the testing and evaluation, the employer tabulates and examines the test results within a reasonable time, and the use of the automobiles is restricted to the employees. If the rules of paragraph (n)(2) of this section are also met, the employees may exclude the value of the use of the automobile during the testing and evaluation period.

(o) *Qualified automobile demonstration use*—(1) *In general.* The value of qualified automobile demonstration use is excludable from gross income as a working condition fringe. The term "qualified automobile demonstration use" means any use of a demonstration automobile by a full-time automobile salesman in the sales area in which the automobile dealer's sales office is located if—

(i) Such use is provided primarily to facilitate the salesman's performance of services for the employer, and

(ii) There are substantial restrictions on the personal use of the automobile by the salesman.

(2) *Full-time automobile salesman*—(i) *Definition.* The term "full-time automobile salesman" means any individual who—

(A) Is employed by an automobile dealer,

(B) Customarily spends substantially all of a normal business day on the sales floor selling automobiles to customers of the automobile dealership,

(C) Customarily works a number of hours considered full-time in the industry (but at a rate not less than 1,000 hours per year), and

(D) Derives at least 85 percent of his or her gross income from the automobile dealership directly as a result of such automobile sales activities.

An individual, such as the general manager of an automobile dealership, who receives a sales commission on the sale of an automobile is not a full-time automobile salesman unless the requirements of this paragraph (o)(2)(i) are met. The exclusion provided in this paragraph (o) is available to an individual who meets the definition of this paragraph (o)(2)(i) regardless of whether the individual performs services in addition to those described in this paragraph (o)(2)(i). For example, an individual who is an owner of the automobile dealership but who otherwise meets the requirements of this paragraph (o)(2)(i) may exclude from gross income the value of qualified automobile demonstration use.

(ii) *Use by an individual other than a full-time automobile salesman.* Personal use of a demonstration automobile by an individual other than a full-time automobile salesman is not treated as a working condition fringe. Therefore, any personal use, including commuting use, of a demonstration automobile by a part-time salesman, automobile mechanic, manager, or other individual is not "qualified automobile demonstration use" and thus not excludable from gross income.

(3) *Demonstration Automobile.* The exclusion provided in this paragraph (o) applies only to qualified use of a demonstration automobile. A demonstration automobile is an automobile that is—

(i) Currently in the inventory of the automobile dealership, and

(ii) Available for test drives by customers during the normal business hours of the employee.

(4) *Substantial restrictions on personal use.* Substantial restrictions on the personal use of demonstration automobiles exist when all of the following conditions are satisfied:

(i) Use by individuals other than the full-time automobile salesmen (e.g., the salesman's family) is prohibited,

(ii) Use for personal vacation trips is prohibited,

(iii) The storage of personal possessions in the automobile is prohibited, and

(iv) The total use by mileage of the automobile by the salesman outside the salesman's normal working hours is limited.

(5) *Sales area*—(i) *In general.* Qualified automobile demonstration use must be use in the sales area in which the automobile dealer's sales office is located. The sales area is the geographic area surrounding the automobile dealer's sales office from which the office regularly derives customers.

(ii) *Sales area safe harbor.* With respect to a particular full-time salesman, the automobile dealer's sales area may be treated as the larger of the area within a 75 mile radius of the dealer's sales office, or the on-way

commuting distance (in miles) of the particular salesman.

(p) *Parking*—(1) *In general.* The value of parking provided to an employee on or near the business premises of the employer is excludable from gross income as a working condition fringe. The working condition fringe exclusion applies whether the employer owns or rents the parking facility or parking space.

(2) *Reimbursement of parking expenses.* Any reimbursement to the employee of the ordinary and necessary expenses of renting a parking space on or near the business premises of the employer is excludable as a working condition fringe. The preceding sentence does not apply, however, to cash payments that are not actually used for renting a parking space. Thus, that part of a general transportation allowance that is not used for parking is not excludable as a working condition fringe under this paragraph (p).

(3) *Parking on residential property.* With respect to an employee, this paragraph (p) does not apply to any parking facility or space located on property owned or leased for residential purposes by the employee.

(q) *Nonapplicability of nondiscrimination rules.* Except to the extent provided in paragraph (n)(3) of this section, the nondiscrimination rules of section 132(h)(1) and § 1.132-8T do not apply in determining the amount, if any, of a working condition fringe.

Par. 8. The following § 1.132-6T is added at the appropriate place:

§ 1.132-6T De minimis fringe (Temporary).

(a) *In general.* Gross income does not include the value of a de minimis fringe provided to an employee. The term "de minimis fringe" means any property or service the value of which is (after taking into account the frequency with which similar fringes are provided by the employer to the employer's employees) so small as to make accounting for it unreasonable or administratively impracticable.

(b) *Frequency.* Generally, the frequency with which similar fringes are provided by the employer to the employer's employees is determined by reference to the frequency with which the employer provides the fringe to each individual employee. For example, if an employer provides a free meal to one employee on a daily basis, but not to any other employee, the value of the meals is not de minimis with respect to that one employee even though with respect to the employer's entire workforce the meals are provided "infrequently." However, where it would be administratively difficult to determine frequency with respect to individual employees, the frequency with which similar fringes are provided by the employer to the employer's employees is determined by reference to the frequency with which the employer provides the fringes to the employees and not the frequency with which individual employees receive them. In these cases, if an employer occasionally provides a fringe benefit of de minimis value to the employer's employees, the de minimis fringe exclusion may apply even though a particular employee receives the benefit frequently. For example, if an employer exercises sufficient control and imposes significant restrictions on the personal use of a company copying machine so that at least 85 percent of the use of the machine is for business purposes, any personal use the copying machine by particular employees is considered to be a de minimis fringe.

(c) *Administrability.* Unless excluded by a statutory provision other than section 132(a)(4), the value of any fringe benefit that would not be unreasonable or administratively impracticable to account for must be included in the employee's gross income. Thus, except as otherwise provided in this section, the provision of any cash fringe benefit (or any fringe benefit provided to an employee through the use of a charge or credit card) is not excludable as a de minimis fringe. For example, the provision of cash to an employee for personal entertainment is not excludable as a de minimis fringe.

(d) *Special rules*—(1) *Transit passes.* A transit pass provided to an employee at a discount not exceeding $15 per month may be excluded as a de minimis fringe. The exclusion provided in this paragraph (d) also applies to the provision of $15 in tokens or fare cards that enable an individual to travel on the transit system. The exclusion provided in this paragraph (d) does not apply to any provision of cash or other benefit to defray transit expenses incurred for personal travel.

(2) *Occasional meal money or local transportation fare.* Occasional meal money or local transportation fare provided to an employee because overtime work necessitates an extension of the employee's normal workday is excluded as a de minimis fringe.

(3) *Use of special rules to establish a general rule.* The special rules provided in this paragraph (d) may not be used to establish any general rule. For example, the fact that $180 ($15 per month for 12 months) worth of transit passes can be excluded in a year does not mean that any fringe benefit with a value equal to or less than $180 may be excluded as a de minimis fringe.

(4) *Benefits exceeding value and frequency limitations.* If the benefit provided to an employee is not de minimis because either the value or frequency exceeds a limit provided in this paragraph (d), no amount of the benefit is considered to be de minimis. For example, if an employer provides a $20 monthly transit pass, the entire $20 must be included in income, not just the excess value over $15.

(e) *Nonapplicability of nondiscrimination rules.* Except to the extent provided in § 1.132-7T, the nondiscrimination rules of section 132(h)(1) and § 1.132-8T do not apply. Thus, for example, a fringe benefit may be a de minimis fringe even if the benefit is provided exclusively to officers of the employer.

(f) *Examples*—(1) *Benefits excludable from income.* Examples of de minimis fringe benefits are occasional typing of personal letters by a company secretary; occasional personal use of an employer's copying machine, provided that the employer exercises sufficient control and imposes significant restrictions on the personal use of the machine so that at least 85 percent of the use of the machine is for business purposes; occasional cocktail parties or picnics for employees and their guests; traditional holiday gifts of property (not cash) with a low fair market value; occasional theatre or sporting event tickets; and coffee and doughnuts.

(2) *Benefits not excludable as de minimis fringes.* Examples of fringe benefits that are not excludable from income as de minimis fringes are: season tickets to sporting or theatrical events; the commuting use of an employer-provided automobile or other vehicle more than once a month; membership in a private country club or athletic facility, regardless of the frequency with which the employee uses the facility; and use of employer-owned or leased facilities (such as an apartment, hunting lodge, boat, etc.) for a weekend. Some amount of the value of these fringe benefits may be excluded under other statutory provisions, such as the exclusion for working condition fringes. See § 1.132-5T.

Par. 9. The following § 1.132-7T is added at the appropriate place:

§ 1.132-7T Treatment of employer-operated eating facilities (Temporary).

(a) *In general*—(1) *General rule.* The value of meals provided to employees at an employer-operated eating facility for employees is excludable from gross income as a de minimis fringe only if—

(i) On an annual basis, the revenue from the facility equals or exceeds the direct operating costs of the facility, and

(ii) With respect to any officer, owner or highly compensated employee, access to the facility is available on substantially the same terms to each member of a group of employees that is defined under a reasonable classification set up by the employer that does not discriminate in favor of officers, owners, and highly compensated employees. See § 1.132–8T.

(2) *Employer-operated eating facility for employees.* An employer-operated eating facility for employees is a facility that meets all of the following conditions—

(i) The facility is owned or leased by the employer,

(ii) The facility is operated by the employer,

(iii) The facility is located on or near the business premises of the employer,

(iv) Substantially all of the use of the facility is by employees of the employer operating the facility, and

(v) The meals furnished at the facility are provided during, or immediately before or after, the employee's workday.

For purposes of this section, the term "meals" means food, beverages, and related services provided at the facility. If an employer can determine the number of employees who receive meals that are excludable from income under section 119, the employer may, in determining whether the requirement of paragraph (a)(1)(i) of this section is satisfied, disregard all costs and revenues attributable to such meals provided to such employees. For purposes of this section, each dining room or cafeteria in which meals are served is treated as a separate eating facility, regardless of whether each such dining room or cafeteria has its own kitchen or other food-preparation area.

(3) *Operation by the employer.* If an employer contracts with another to operate an eating facility for its employees, the facility is considered to be operated by the employer for purposes of this section. If an eating facility is operated by more than one employer, it is considered to be operated by each employer.

(b) *Direct operating costs.* The direct operating costs test must be applied separately for each dining room or cafeteria. For purpose of this section, the direct operating costs of an eating facilities are: (1) The cost of food and beverages and (2) the cost of labor for personnel whose services relating to the facility are performed primarily on the premises of the eating facility. Direct operating costs do not include the cost of labor for personnel whose services relating to the facility are not performed primarily on the premises of the eating facility. Thus, for example, the labor cost for cooks, waiters, and waitresses is included in direct operating costs, but the labor cost for a manager of an eating facility whose services relating to the facility are not primarily performed on the premises of the eating facility is not included in direct operating costs. If an employee perfoms services both on and off the premises of the eating facility, only the applicable percentage of the total labor cost of the employee that bears the same proportion as time spent on the premises bears to total time is included in direct operating costs. For example, assume that 60 percent of the services of the cooks in the above example are not related to the eating facility. Only 40 percent of the total labor cost of the cooks is includible in direct operating costs. For purposes of this section, labor costs include all compensation required to be reported on a Form W–2 for income tax purposes and related employment taxes paid by the employer.

(c) *Valuation of non-excluded meals provided at an employer-operated eating facility for employees.* If the exclusion for meals provided at an employer-operated eating facility for employees is not available, the recipient of meals provided at such facility must include in income the amount by which the fair market value of the meals provided exceeds the sume of: (1) The amount, if any, paid for the meals, and (2) the amount, if any, specifically excluded by another section of the Code. For special valuation rules relating to such meals see § 1.61–2T (j).

Par. 10. The following § 1.132–8T is added at the appropriate place:

§ 1.132–8T Nondiscrimination rules (Temporary).

(a) *Application of nondiscrimination rules*—(1) *General rule.* To qualify under section 132 for the exclusions for non-additional-cost services, qualified employee discounts, or meals provided at employer-operated eating facilities for employees, the fringe benefit must be available on substantially the same terms to each member of a group of employees which is defined under a reasonable classification set up by the employer that does not discriminate in favor of officers, owners, or highly compensated employees (the "prohibited group employees").

(2) *Consequences of discrimination.* If the availability of or the provision of the fringe benefit does not satisfy the nondiscrimination rules provided in this section, the exclusion applies only to those employees (if any) who receive the benefit and who are not prohibited group employees. For example, if an employer offers a 20 percent discount (which otherwise satisfies the requirements for a qualified employee discount) to all nonprohibited group employees and a 35 percent discount to all prohibited group employees, the entire value of the 35 percent discount (not just the excess over 20 percent) is includible in the gross income and wages of the prohibited group employees who make purchases at a discount.

(3) *Scope of the nondiscrimination rules provided in this section.* The nondiscrimination rules provided in this section apply only to fringe benefits provided pursuant to section 132 (a)(1), (a)(2), and (e)(2). These rules have no application to any other employee benefit that may be subject to nondiscrimination requirements under any other section of the Code.

(b) *Coverage requirement*—(1) *Section 132 (a)(1) and (2).* For purposes of the exclusions for no-additional-cost services and qualified employee discounts, the nondiscrimination rules of this section are applied by aggregating the employees of all related employers (as defined in § 1.132–1T (c)), but without aggregating employees in different lines of business (as defined in § 1.132–4T). Employees in different lines of business will be aggregated, however, if the line of business limitation has been relaxed pursuant to either section 1.132–4T (b) or (c). Except as provided in paragraph (e) of this section, the nondiscrimination rules of this section are generally applied separately to each fringe benefit program of an employer.

(2) *Section 132(e)(2).* For purposes of the exclusion for meals provided at employer-operated eating facilities for employees, the nondiscrimination rules of this section are applied by aggregating the employees of all related employers, without regard to different lines of business, who regularly work at or near the premises on which the eating facility is located. The nondiscrimination rules of this section are applied separately to each eating facility. Each dining room or cafeteria in which meals are served is treated as a separate eating facility, regardless of whether each such dining room or cafeteria has its own kitchen or other food-preparation area.

(3) *Classes of employees who may be excluded.* Except as otherwise provided in this section, for purposes of applying the nondiscrimination rules of this section to a particular fringe benefit program, there may be excluded from

consideration the following classes of employees provided that, with respect to each class (other than the class described in paragraph (b)(3)(iii) of this section), all employees in the class are excluded from participating in the particular fringe benefit program—

(i) All part-time or seasonal employees who are (or who are reasonably expected to be) credited with less than 1,000 hours (or such lesser number required for the program) of service during a calendar year;

(ii) All employees who are included in a unit of employees covered by an agreement with the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and one or more employers, if there is evidence that the particular fringe benefit program was the subject of good faith bargaining between such employee representatives and such employer or employers (and if, after March 31, 1984, the additional condition of section 7701(a)(46) is satisfied);

(iii) All employees who are nonresident aliens and who receive no earned income (within the meaning of section 911(d)(2)) from the employer which constitutes income from services within the United States (within the meaning of section 861(a)(3));

(iv) All employees who have not completed at least one year (or such lesser period required for the program) of service with the employer;

(v) All employees who have separated from the service of the employer in a year prior to the current year (regardless of the reason for the separation);

(vi) All employees who have separated from the service of the employer in a year prior to the current year except for retired and/or disabled employees (either with or without a time limit based on a set number of years since separation from the service of the employer); and

(vii) All employees of a leased section of a department store.

(c) *Classification requirement*—(1) *General rule.* The determination of whether a particular classification established by an employer discriminates in favor of the prohibited group will depend on the facts and circumstances involved, based on principles similar to those applied in the qualified plan area (see section 410(b)(1)(B) and the regulations thereunder). In general, except as otherwise provided in this section, a classification that would be determined to be nondiscriminatory pursuant to the application of the nondiscrimination standards that are applied in the qualified plan area shall be deemed to be nondiscriminatory for purposes of section 132.

(2) *Classifications that are per se discriminatory.* A classification that, on its face, makes fringe benefits available only to prohibited group employees is per se discriminatory, and no exclusion from gross income is available to any prohibited group employee under section 132. In addition, a classification that is based on either an amount or rate of compensation is per se discriminatory if it favors those with the higher amount or rate of compensation. On the other hand, a classification that is based on factors such as seniority, full-time vs. part-time employment, or job description is not per se discriminatory but may be discriminatory as applied to the workforce of a particular employer.

(3) *Former employees.* When determining whether a classification is discriminatory, former employees shall not be considered together with other employees of the employer. Therefore, a classification is not discriminatory if the employer does not make the fringe benefits available to any former employee. Whether a classification of former employees discriminates in favor of prohibited group employees will depend on the facts and circumstances. The rules of this section shall apply separately to the former employee classification.

(4) *Employer-operated eating facilities for employees*—(i) *General rule.* If access to an employer-operated eating facility for employees is available to a classification of employees that discriminates in favor of highly compensated employees, the classification will not be treated as discriminating in favor of the prohibited group employees unless the facility is used, more than a de minimis amount, by any executive group employee.

(ii) *Executive group employees.* For purposes of this paragraph (c)(4), the term "executive group employees" has the same meaning as the term "prohibited group employees" (as defined in paragraph (g) of this section), except that for purposes of identifying highly compensated employees—

(A) The exception provided in paragraph (g)(1)(i)(A) of this section does not apply, and

(B) The phrase "highest-paid one percent of all employees of an employer" is substituted for the phrase "highest-paid ten percent of all employees of an employer" in paragraph (g)(1)(ii)(A) of this section.

(d) *Substantially-the-same-terms requirement*—(1) *General rule.* Fringe benefits available to a particular classification of employees must be available to each employee in the classification on substantially the same terms. The determination of whether this requirement is met shall depend on the facts and circumstances involved. For example, if a department store provides a 20 percent qualified employee discount to its employees on all merchandise, the substantially-the-same-terms requirement will be satisfied. Similarly, if the discount provided to all employees is 30 percent on certain merchandise (such as apparel), and 20 percent on all other merchandise, the substantially-the-same-terms requirement will be satisfied. However, if the discount provided is 20 percent on all merchandise for hourly employees and 30 percent on all merchandise for salaried employees, the substantially-the-same-terms requirement will not be satisfied. In addition, if the percentage discount varies depending on either an employee's amount or rate of compensation, or volume of purchases, the substantially-the-same-terms requirement will not be satisfied. In order to determine whether such a discount program satisfies the nondiscrimination requirements of section 132, each group of employees that does receive fringe benefits on substantially the same terms must be treated as a separate classification. However, subject to the rules of paragraph (e) (2) of this section, an employer may divide a fringe benefit program into two programs for purposes of aggregating groups of employees. See Example (1) of paragraph (d) (3) of this section.

(2) *Terms relating to priority.* Certain fringe benefits made available to employees are available only in limited quantities that may be insufficient to meet employee demand. This may occur either because of employer policy (such as where an employer determines that only a certain number of units of a specific product will be made available to employees each year) or because of the nature of the fringe benefit (such as where an employer provides a no-additional-cost transportation service that is limited to the number of seats available just before departure). Under these circumstances, an employer may find it necessary to establish some method of allocating the limited fringe benefits among the employees eligible to receive the fringe benefits. An allocation among employees on a "first-come, first-served" basis will not violate the substantially-the-same-terms requirement provided that such an allocation is not discriminatory in practice. In addition, an allocation among employees on a lottery basis will

not violate the substantially-the-same-terms requirement provided that such an allocation is nondiscriminatory in practice. For example, assume that an employer has a limited number of a particular benefit to offer to its employees. Assume further that the employees interested in receiving the benefit submit their names to the employer who then selects a number of names, at random, equal to the number of fringe benefits available. This lottery system would not violate the substantially-the-same-terms requirement. An allocation among employees on other than a "first-come, first-served", lottery, or similar basis will violate the substantially-the-same-terms requirement. Therefore, an allocation based on seniority, full-time vs. part-time employment, or job description will violate the substantially-the-same-terms requirement. In order to determine whether such a fringe benefit program satisfies the nondiscrimination requirements of section 132, each group of employees that does receive fringe benefits on substantially the same terms must be treated as a separate classification. For purposes of this rule, the last two sentences of paragraph (d)(1) of this section apply.

(3) *Examples.* The followings examples illustrate the provisions of this paragraph (d):

Example 1. Assume that with respect to a benefit available in limited quantities an employer provides priority to employees based on seniority. Assume further that all non-prohibited group employees have ten years of seniority and all prohibited group employees have nine years seniority. If each of these groups were tested separately, the benefits offered to prohibited group employees would be discriminatory under this section. In this case, the employer could divide the fringe benefit program provided to non-prohibited group employees into two parts: one relating to nine years of seniority and one relating to an additional year of seniority. As restructured in this manner, all employees receive the benefit relating to nine years seniority and only non-prohibited group employees receive the benefit relating to an additional year of seniority. Both groups (all employees and all non-prohibited group employees) are nondiscriminatory groups.

Example 2. Assume that prices charged to prohibited group employees at an employer-operated eating facility for employees are lower than prices charged to non-prohibited group employees. The substantially-the-same requirement is not satisfied.

(4) *Disproportionate use of eating facility.* If access to an employer-operated eating facility for employees is technically available on substantially-the-same-terms (to (i) all employees who regularly work at or near the premises on which the eating facility is located (the employee group), or (ii) a nondiscriminatory classification of the employee group, but in practice a highly disproportionate number of the prohibited group employees in the employee group, compared to the non-prohibited group employees in the employee group, use the facility, the substantially-the-same-terms requirement will not be satisfied unless no member of the executive group eats there more than a de minimis amount.

(e) *Aggregation of separate fringe benefit programs*—(1) *General rule.* If an employer maintains more than one fringe benefit program, i.e., two or more classifications of employees providing either identical or different fringe benefits, the nondiscrimination requirements of section 132 will generally be applied separately to each such program. Thus, a determination that one fringe benefit program discriminates in favor of prohibited group employees generally will not cause other fringe benefit programs covering the same prohibited group employees to be treated as discriminatory.

(2) *Exception*—(i) *Related fringe benefit programs.* If one of a group of fringe benefit programs discriminates in favor of prohibited group employees, no related fringe benefit provided to such prohibited group employees under any other fringe benefit program may be excluded from the gross income of such prohibited group employees. For example, assume a department store provides a 20 percent merchandise discount to all employees under one fringe benefit program. Assume further that under a second fringe benefit program, the department store provides an additional 15 percent merchandise discount to a group of employees defined under a classification which discriminates in favor of the prohibited group. Because the second fringe benefit program is discriminatory, the 15 percent merchandise discount provided to the prohibited group employees is not a qualified employee discount. In addition, because the 20 percent merchandise discount provided under the first fringe benefit program is related to the fringe benefit provided under the second fringe benefit program, the 20 percent merchandise discount provided the prohibited group employees is not a qualified employee discount. Thus, the entire 35 percent merchandise discount provided to the prohibited group employees is includible in such employees' gross incomes.

(ii) *Employer-operated eating facilities for employees.* For purposes of paragraph (e)(2)(i) of this section, meals at different employer-operated eating facilities for employees are not related fringe benefits, so that a prohibited group employee may exclude the value of a meal at a nondiscriminatory facility even though any meals provided to him or her at the discriminatory facility cannot be excluded.

(f) *Cash bonuses or rebates.* A cash bonus or rebate provided to an employee by an employer that is determined pursuant to the value of employer-provided property or services purchased by the employee, is treated as an equivalent employee discount. For example, assume a department store provides a 20 percent merchandise discount to all employees under a fringe benefit program. In addition, assume that the department store provides cash bonuses to a group of employees defined under a classification which discriminates in favor of the prohibited group. Assume further that such cash bonuses equal 15 percent of the value of merchandise purchased by each employee. This arrangement is substantively identical to the example described in paragraph (e)(2) of this section. Thus, both the 20 percent merchandise discount and the 15 percent cash bonus provided to the prohibited group employees are includible in such employees' gross incomes.

(g) *Prohibited group employees*—(1) *Highly compensated*—(i) *General rule.* Except as otherwise provided in this paragraph (g)(1)(i), any employee of an employer who has (or is reasonably expected to have) compensation during a calendar year equal to or greater than the employer's base compensation amount is highly compensated. There are two exceptions to this rule:

(A) Any employee who has (or is reasonably expected to have) compensation during a calendar year equal to or greater than $50,000 is highly compensated, regardless of whether such compensation is in excess of the base compensation amount, and

(B) Any employee who is reasonably expected to have compensation during a calendar year equal to or less than $20,000 is not highly compensated, unless no employee of the employer is reasonably expected to have compensation equal to or greater than $35,000.

The determination of whether an employee is a highly compensated employee will be determined based on the entire employee workforce of all employers aggregated pursuant to the rules of section 414 (b), (c), or (m) without regard to the regular workplace of the employees.

(ii) *Base compensation amount*—(A) *General rule.* The term "base compensation amount" is defined as that amount corresponding to the lowest annual compensation amount received by the highest-paid ten percent of all employees of an employer (the number of employees in the top ten percent will be increased to the next highest integer if necessary), determined on the basis of the preceding calendar year. For purposes of this paragraph (g) (1) (ii), the term "employer" includes all entities that would be aggregated pursuant to the rules of section 414 (b), (c), or (m).

(B) *Employees that are excluded.* For purposes of determining the base compensation amount with respect to a fringe benefit program, employees described in paragraph (b)(3) of this section are excluded whether or not they are covered under the fringe benefit program, except that: (*1*) Employees described in paragraph (b)(3)(ii) of this section are taken into account with respect to the program even if they are excluded under paragraph (b)(3), and (*2*) employees described in paragraph (b)(3) (i) and (iv) of this section are taken into account with respect to the program unless they are excluded under paragraph (b)(3).

(C) *Exception to preceding calendar year rule.* In the case of an employer's first year of operation, or where an employer's business has changed significantly from the prior calendar year (e.g., due to an acquisition or merger), the employer must make a good faith attempt to either determine or adjust the base compensation amount for the current year based on reasonable estimates of current year compensation.

(iii) *Compensation.* The term "compensation" is defined as the amount reportable on a Form W–2 as income. Amounts that would be excluded from income but for section 132(h)(1) are not included in compensation for purposes of this paragraph (g)(1). Compensation includes amounts received from all entities which would be treated as a single employer under section 414 (b), (c), or (m) and is not restricted to amounts received with respect to any one line of business.

(iv) *Employee.* Generally, for purposes of determining whether an employee is highly compensated under this paragraph (g)(1), the term "employee" does not include any individual who does not perform services for the employer as an employee during the calendar year. For example, if an employer has active employees, retired or disabled employees, and widows or widowers who are "employees" under section 132(f)(1)(B), the general rule (described in paragraph (g)(1)(i) of this section) applies only to the active employees.

(2) *Owner*—(i) *General rule.* For purposes of this section, the term "owner" means any employee who owns a one percent or greater interest in either the employer or in any entity that would be aggregated with the employer pursuant to the rules of section 414 (b), (c), or (m). In addition, such an employee shall be treated as an owner of all entities that would be aggregated with the employer pursuant to the rules of section 414 (b), (c), or (m).

(ii) *Determining ownership.* Ownership in a corporation shall be determined pursuant to the rules of section 318(a). For purposes of determining ownership in an entity other than a corporation, the rules of section 318(a) shall apply in a manner similar to the way in which they apply for purposes of determining ownership in a corporation. For non-corporate interests, capital or profits interest must be substituted for stock.

(3) *Officer.*—(i) *Non-government.* For purposes of this section, an officer of a non-government employer is any employee who is appointed, confirmed, or elected by the Board or shareholders of the employer. An employee who is an officer of an employer shall be treated as an officer of all entities treated as a single employer pursuant to section 414 (b), (c), or (m). The number of officers is not to exceed one-percent of the total number of employees of all entities treated as a single employer pursuant to section 414 (b), (c), or (m) (increased to the next highest integer, if necessary). If the number of officers exceeds one-percent of all employees, then the limitation is to be applied to employees in descending order of compensation (as defined in paragraph (g)(1)(iii) of this section). Thus, if an employer with 1,000 employees has 11 board-appointed officers, the employee with the least compensation of those officers would not be an officer under this paragraph (g)(3)(i). In determining the total number of employees with respect to a fringe benefit program, employees described in paragraph (b)(3) of this section are excluded whether or not they are covered under the fringe benefit program, except that (A) employees described in paragraph (b)(3)(ii) of this section are taken into account with respect to the program even if they are excluded under paragraph (b)(3), and (B) employees described in paragraph (b)(3) (i) and (iv) of this section are taken into account with respect to the program unless they are excluded under paragraph (b)(3).

(ii) *Government.* For purposes of this section, an officer of a government employer is any—

(A) Elected official,

(B) Federal employee appointed by the President and confirmed by the Senate. However, in the case of any commissioned officer of the United States Armed Forces, an officer is any employee with the rank of brigadier general or rear admiral (lower half) or above, and

(C) State or local executive officer comparable to individuals described in paragraphs (g)(3)(ii) (A) and (B) of this section.

For purposes of this paragraph (g)(3)(ii), the term "government" includes any Federal, state, or local governmental unit, and any agency or instrumentality thereof.

(4) *Former employees.* [Reserved]

§ 1.162–25T [Amended]

Par. 11. Paragraph (b) of § 1.162–25T is amended by removing the words "(as defined in § 1.61–2T Q/A–20)" and adding in their place the words "(as defined in § 1.61–2T(e)(2))".

§ 1.274–5T [Amended]

Par. 12. Section 1.274–5T is amended as follows:

1. Paragraph (e)(1)(ii) is amended by removing the words "(as defined in § 1.61–2T Q/A–20)" and adding in their place the words "(as defined in § 1.61–2T(e)(2))".

2. The first sentence of paragraph (l) is revised to read as follows: "For purposes of section 274(d) and this section, the terms "automobile" and "vehicle" have the same meanings as prescribed in § 1.61–2T(d)(1)(ii) and § 1.61–2T(e)(2), respectively.".

3. The third sentence of paragraph (m) is amended by removing the words "except as provided in § 1.132–1T Q/A–4b" and adding in their place the words "except as provided in § 1.132–5T(h)".

§ 1.274–6T [Amended]

Par. 13. Section 1.274–6T is amended as follows:

1. Paragraph (a)(3)(i)(E) is revised to read as follows: "The employee required to use the vehicle for commuting is not a control employee (as defined in § 1.61–2T(f) (5) and (6)) required to use an automobile (as defined in § 1.61–2T(d)(1)(ii)), and".

2. Paragraph (a)(3)(i)(F) is amended by removing the citation "§ 1.61–2T Q/A–21" and adding in its place the citation § 1.61–2T(f)(3)".

3. Paragraph (a)(3)(ii) is amended by removing from the introductory text the

citation "§ 1.61-2T Q/A-21" and adding in its place the citation "§ 1.61-2T(f)(3)".

4. Paragraph (a)(3)(ii)(E) is revised to read as follows: "The employee required to use the vehicle for commuting is not a control employee (as defined in § 1.61-2T(f) (5) and (6) required to use an automobile (as defined in § 1.61-2T(d)(1)(ii)), and".

5. Paragraph (a)(3)(ii)(F) is amended by removing the citation "§ 1.61-2T Q/A-21" and adding in its place the citation "§ 1.61-2T(f)(3)".

6. Paragraph (b)(1) is amended by removing from the last sentence the citation "§ 1.132-1T Q/A-4a(f)" and adding in its place the citation "§ 1.132-5T(g)".

7. Paragraph (b)(3) is amended by removing from the last sentence the citation "§ 1.132-1T Q/A-4a(f)" and adding in its place the citation "§ 1.132-5T(g)(3)".

8. Paragraph (e)(3) is amended by removing the citation "§ 1.61-2T Q/A-11" and adding in its place the citation "§ 1.61-2T(d)(1)(ii)".

9. Paragraph (e)(4) is amended by removing the citation "§ 1.61-2T Q/A-20" and adding in its place the citation "§ 1.61-2T(e)(2)".

PART 602—[AMENDED]

Par. 14. The authority for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

§ 602.101 [Amended]

Par. 15. Section 602.101(c) is amended by inserting in the appropriate place in the table § 1.61-2T . . . 1545-0771; 1.132-2T . . . 1545-0771; and § 1.132-5T . . . 1545-0771".

Roscoe L. Egger, Jr.,

Commissioner of Internal Revenue.

Approved: December 11, 1985.

Ronald A. Pearlman,

Assistant Secretary of the Treasury.

[FR Doc. 85-30161 Filed 12-18-85; 11:08 am]

BILLING CODE 4830-01-M

---

26 CFR Parts 1 and 602

[T.D. 8064]

Income Tax; Information Returns Relating To Sales or Exchanges of Certain Partnership Interests

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document provides temporary regulations relating to information returns, statements, and notifications required where there is a sale or exchange of certain partnership interests. The text of the temporary regulations set forth in this document also serves as the text of the proposed regulations cross-referenced in the notice of proposed rulemaking in the Proposed Rules Section of this issue of the **Federal Register.** The temporary regulations reflect changes to the applicable tax law made by section 149 of the Tax Reform Act of 1984 and provide guidance on the manner of filing and contents of required information returns, statements, and notifications under section 6050K of the Internal Revenue Code of 1954.

DATE: The regulations contained in this document are effective with respect to sales or exchanges of partnership interests made after December 31, 1984.

FOR FURTHER INFORMATION CONTACT: Robert E. Shaw of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC 20224 (Attention: CC:LR:T LR-129-85). Telephone, 202-566-3297 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

Explanation of Provisions

Under section 6050K (a) and § 1.6050K-1T a partnership must file a return on Form 8308 when there is a sale or exchange described in section 751 (a) (a "section 751 (a) exchange") of any interest in that partnership during any calendar year after 1984. A section 751 (a) exchange occurs when any portion of any money or other property received by a transferor partner in exchange for all or a part of his or her interest in the partnership is attributable to section 751 property (unrealized receivables and substantially appreciated inventory items as defined in seciton 751 (c) and (d)). Generally, a sale or exchange of an interest in a partnership (or a portion thereof) at a time when the partnership has any section 751 property will constitute a section 751(a) exchange.

A return on Form 8308 must be filed with respect to each sale or exchange. Section 1.6050K-1T (a) (2), however, provides that the Commissioner may, at a future date, authorize the use of a single document which includes all of the partnership's returns for a calendar year, or of a composite document, by partnerships that are required to file 25 or more separate returns in any calendar year. The information to be supplied on Form 8308 includes the names, addresses, and taxpayer identification numbers of the transferee and transferor in the exchange and of the partnership, the date of the exchange, and such other information as may be required by Form 8308 or its instructions. Form 8308 shall contain a printed notice that the information on the Form has been supplied to the Internal Revenue Service, that the transferor is required to treat a portion of the gain realized from the section 751 (a) exchange as ordinary income, and that the transferor in a section 751 (a) exchange is required under § 1.751-1 (a) (3) to attach a statement relating to the exchange to his or her income tax return for the taxable year in which the exchange occurred. The partnership return on Form 8308 is to be filed as an attachment to the partnership's Form 1065 for its taxable year in which the calendar year in which the section 751 (a) exchange occurred ends.

Under section 6050K (b) and the temporary regulations all partnerships that are required to file returns under section 6050K (a) must furnish a statement to each person whose name appears on the partnership's Form 8308 showing the name and address of the partnership in addition to the information shown on the Form 8308 with respect to that person. A copy of Form 8308 is to be used as the statement. The statement must be furnished on or before January 31 following the calendar year in which the section 751 (a) exchange occurred (or, if later, 30 days after the partnership has notice of the exchange). Thus, under the statute the partnership must generally prepare Form 8308 prior to the time it must be filed so as to allow the timely furnishing of statements to the transferor and transferee.

Section 6050K (c)(1) and the temporary regulations require the transferor of a partnership interest in a section 751 (a) exchange to notify the partnership of the exchange, in writing, on or before the thirtieth day after the date of the exchange (or, if earlier, January 15 of the calendar year following the calendar year in which the exchange occurred). The written notification from the transferor must include the names and addresses of the transferor and transferee, the date of the exchange, and the taxpayer identification numbers of the transferor and, if known, of the transferee.

Under section 6050K (c) (2) and the temporary regulations the partnership is not required to file a return or furnish statements under section 6050K until the partnership has notice of the section 751 (a) exchange. Section 1.6050K-1T (e) clarifies that a partnership has notice of a section 751 (a) exchange when either (1) the partnership receives the written