

Doing As They Say or Saying As They Do:

Tax Policy and the (In)Effective and (In)Efficient Taxation of Credit Card Rewards

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Abstract:

In recent years, credit card reward programs have become a basic component of personal finance and, often, a basic perquisite for employees. Taxing rewards earned by an employee who charges an employer's expense on a personal credit card and is later reimbursed are problematic. Consequently, in 2002 the IRS stated that it would not assert a deficiency for in-kind rewards, e.g., frequent flyer miles, earned on business-related expenses, but that the "relief" provided does not apply to rewards converted to cash. This paper argues that, for various reasons, the IRS should also not assert a deficiency for cash rewards earned on business-related expenses. These arguments range from the practical (depending on perspective, the rewards can be classified in many different ways and valuation of in-kind rewards is ultimately not much more difficult than for cash) to the theoretical (enforcement would be an administrative nightmare, but failure to enforce the tax impairs transparency and equity). All arguments ultimately come out against using IRS resources to enforce a deficiency based on a cash business-related reward and, therefore, against maintaining the charade that such payments are taxable.

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In recent years, credit card reward programs have become a basic component of personal finance. Credit card issuers use them to entice consumers to spend more on a given card.¹ Consumers use them to earn a rebate on amounts spent or as an alternative to save for the next beach vacation. Generally, the value of the item or cash “earned” (the “Reward”) represents a small portion of the amount that must be charged to earn a rebate or “points” that are convertible to a selected item only when the cardholder reaches a specified threshold. Consequently, it can be difficult to classify, calculate the value of, and time the realization of the cardholder’s newly acquired wealth, especially if it is realized in a form other than cash. The situation only gets stickier when evaluating a Reward that a taxpayer earned on a personal credit card by charging a reimbursable business expense (a “business-related Reward”).² Ergo, the Service’s current position is that a business-related Reward earned on business or official travel that is cash or convertible to cash is taxable, but a similar business-related Reward that is an in-kind item or converted to an in-kind item, e.g., frequent flyer miles, is not taxable income.³

¹ Damon Darlin, *Gift Horses to Consider: Credit Cards That Reward*, N.Y. TIMES, Dec. 31, 2005, at C6.

² This article concerns only business-related expenses reimbursed by a third-party non-related employer or client. Other circumstances may lead to different complications. For example, if a cash method taxpayer takes a Section 162 deduction for non-reimbursed business expenses, the tax benefit rule requires inclusion of the value of a Reward in income. Brad Cripe & Katrina Mantzke, *Are Credit Card Rebates Taxable?*, 123 TAX NOTES 311, 312 (2009).

³ See I.R.S. Announcement 2002-18, 2002-1 C.B. 621 (announcing that the Service will not tax travel promotional benefits that are in-kind benefits earned on business or official travel and stating that the relief provided doesn’t apply to benefits converted to cash); I.R.S. Priv. Ltr. Rul. 93-40-007 (June 29, 1993) (noting that an employee’s receipt of cash earned through a frequent flyer mile program used on business travel constitutes a taxable fringe benefit); I.R.S. Priv. Ltr. Rul. 96-23-035 (June 7, 1996) (determining that a rebate earned on a personal credit card was not income and could be a charitable deduction if the cardholder chose to donate it to a specified charity).

Given the difficulty in determining realization of a business-related Reward, the question is why business-related Rewards are taxed in either situation. Rewards are a marketing gimmick used by profit-making companies – they are not a significant source of income to anyone. They are the thirteenth donut earned by buying a dozen or the taxi fare supplied by an employer after working late. Together they add up, but so do a lot of other small payments that are excluded from a taxpayer’s gross income either as fringe benefits or, indeed, as marketing promotions. In the meantime, taxpayers may not think to include a Reward in taxable income,⁴ viewing it as nothing more than a freebie in exchange for all the other charges made on a credit card. And from the Service’s perspective, the nature of business-related Rewards as related to an employment relationship on the one hand and a financing relationship on the other so complicates enforcement that the Service does not know if or when a taxpayer earns this type of benefit.⁵ Thus, the taxation of business-related Rewards is not simply about tax evasion, but rather whether the Service’s official position is consistent with tax policy goals.

This article argues that the Service should align its official position with policy and reality by stating that it does not consider any business-related Reward taxable income. In Part I, I narrow the issue and highlight some of the complications discussed by previous commentators. Most of the existing literature is dated and concerns primarily frequent flyer miles, but it presents adaptable frames of analysis and addresses some of the same problems inherent in taxing a cash Reward. Many of these issues are discussed in greater depth in Parts II and III of this article.

⁴ See *Charley v. Comm’r*, 91 F.3d 72, 75 (9th Cir. 1996) (deciding that at the time, there was nothing in the tax record indicating that a reasonable taxpayer would conclude that a conversion of frequent flyer miles would give rise to taxable income). Since the *Charley* case was decided, some additional literature on the topic and a handful of IRS publications have been published, but it is unlikely that taxpayer knowledge of the subject is much higher today than it was 13 years ago.

⁵ See discussion *supra* Part II.B.

In Part II, I present several arguments why cash Rewards should not be taxed. First, the process of valuating cash and in-kind Rewards is not sufficiently disparate to warrant taxing one and not the other. Although in-kind Rewards present valuation issues (one reason why they are not currently taxed), the problems are not insurmountable and can be pragmatically and economically addressed. Second, classification of Rewards is problematic. Although not crucial to recognition, classification is essential to determine if an exemption applies, what other taxes to impose, and what tax rate to assess. Without appropriate classification, a taxpayer is not fairly treated and the transparency of the tax system suffers. Third, taxing cash Rewards, even when appropriately classified, is problematic from a tax policy perspective. Administratively, it would be difficult to comply with or enforce such a tax and enforcement would yield proportionately small benefits. And, if the Service does not enforce the tax, the system becomes less transparent and less equitable.

In Part III, I address the tax avoidance issues related to any nonrecognition policy and argue that there are several reasons why Rewards will not become the next tax shelter. Additionally, I discuss a few current options to address such a situation, should it arise.

In Part IV, I present three proposals to reform the taxation of cash business-related Rewards. These proposals operate on the assumption that the Service's current position presents insurmountable policy problems. Each proposal has safeguards against the use of Rewards to avoid tax on wages; the latter two proposals proactively address such concerns by drawing on existing anti-avoidance methods.

Finally, in Part V, I conclude with a summary of the arguments presented.

I. What They Have Said: The Issue to Date.

Ubiquitous today, but unheard of thirty years ago, credit card Reward programs allow a cardholder to earn cash or other promotional benefits by charging expenses and either earning a percentage rebate or points convertible into goods, services, or cash (collectively, a “Reward”). Reward programs are a permutation of the frequent flyer bonus programs that American Airlines spearheaded in 1981 as a marketing tool to improve brand loyalty.⁶ In 1986, Discover created the first cash Reward program and soon learned that cardholders used the card more, thus increasing Discover’s receipts from merchants, a primary source of income for many issuers.⁷ Now, cardholders use a Reward card in approximately 70% of credit card transactions⁸ and card issuers pay out billions in incentives every year.⁹

Although Reward programs have proliferated rapidly, the commentary related to taxing those related to reimbursable business expense primarily concerns frequent flyer miles. Despite this narrow focus, the resulting literature is useful because many of the principles behind the question of taxing in-kind Rewards also apply to cash Rewards. Additionally, the commentary raises several pertinent questions about whether there are salient differences between in-kind and cash Rewards.

A. Earning points: What are Rewards and how are they taxed?

A Reward is the conferral of value on a cardholder by the Creditor that issued the pertinent credit card. At first blush, it appears to be an accretion to wealth, but this is not always true. A cardholder does not earn a Reward without incurring or paying a liability. Therefore, in

⁶ Lee S. Garsson, *Frequent Flyer Bonus Programs: To Tax, or Not to Tax – Is this the Only Question?*, 52 J. OF AIR L. & COM. 974, 973 (1986). Of course, many companies have offered incentive programs over the years. The S&H “green stamp” program and various programs operated by cigarette companies are similar to the Reward programs discussed herein. See the Wikipedia article on “green stamps” for a general explanation of the program. S&H Green Stamps, http://en.wikipedia.org/wiki/S&H_Green_Stamps (last visited June 11, 2009).

⁷ Darlin, *supra* note 1.

⁸ Nelly Torres, *When Reward Cards Are a Smart Option*, SEATTLE TIMES, Feb. 15, 2009, at C2.

⁹ Cripe & Matzkin, *supra* note 2, at 311

at least some situations, it is a return of capital and not an accretion to wealth at all.¹⁰ However, despite the terminology often used in the industry, a Reward is not a gift because, at the most basic level it is the product of a contractual relationship between a Creditor and a cardholder.¹¹ A Reward constitutes value in the form of a good or service, e.g., frequent flyer miles, in cash as a rebate or “kickback” paid directly to a cardholder or credited against future payments due to the Creditor, or as a point that can be converted to cash or in-kind goods or services. A cardholder¹² earns a Reward by charging certain types of expenses as defined by the agreement that the cardholder has with the pertinent Creditor. However, the cardholder may charge an expense for any reason, including for a business or employer. Consequently, a variety of Reward is defined in reference to the transactional relationships formed (personal or business-related) and the type of value that the Creditor confers by way of the Reward (cash or in-kind).

Judgments about the three basic principles of tax policy – efficiency, equity, and simplicity¹³ – determine which variety of Reward is excluded from a cardholder’s taxable income. The principles are interconnected – for example, a simplicity goal may affect the equity or economic efficiency of the tax system¹⁴ – but can be separated for definitional purposes.

- Efficiency is primarily related to economic efficiency; that is, how much a given tax provision influences economic behavior (that would not otherwise change) and affects

¹⁰ Cripe & Matzkin, *supra* note 2, at 311-312.

¹¹ See *Comm’r v. Duberstein*, 363 U.S. 278 (1960) (holding that a car given to a business associate was not a gift and constituted remuneration for services rendered).

Any legal person may be a cardholder, but this article is solely concerned with cardholders who are natural persons.

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¹³ MICHAEL J. GRAETZ & DEBORAH H. SCHENK, *FEDERAL INCOME TAXATION: PRINCIPLES AND POLICIES* 27 (5th ed. 2005). The authors note that although these criteria are generally agreed upon for evaluating taxes, there is substantial disagreement about what the terms mean. For example, see Reuven Avi-Yonah, *The Three Goals of Taxation*, 60 TAX L. REV. 1 (2006) and, using slightly different terms, John A. LeDuc, *The Legislative Response of the 97th Congress to Tax Shelters, the Audit Lottery, and Other Forms of Intentional or Reckless Noncompliance*, 18 TAX NOTES 363 (1983).

¹⁴ JOEL SLEMROD & JON BAKIJA, *TAXING OURSELVES* 159 (4th ed. 2008).

the functioning of the economy.¹⁵ For example, in an income tax system, a consumer may substitute leisure for an additional week's work if that week will push her into a higher marginal tax bracket (the "substitution effect").¹⁶ Alternatively, if her demand for income is relatively inelastic or she views leisure as an inadequate substitute for income, she may work an additional week and a half to earn enough income to overcome the tax bracket change (the "income effect").¹⁷ When creating a tax provision, the government may have behavior modification as a direct or indirect goal or the modification may be an unintended consequence, but the attendant distortions should be evaluated for desirability in any event.¹⁸ In particular, the government should consider who will bear the incidence of the tax and whether (or how) it will be capitalized.¹⁹ The government should also be wary of modifying behavior such that a deadweight loss arises.²⁰

- Equity concerns who should pay taxes and is separable into vertical and horizontal categories.²¹ Vertical equity concerns the equity among taxpayers with different levels of "well-being" and currently relates to the distributive justice standard that the tax burden should weigh more heavily on those who have proportionately more income available for non-essential expenses and thus are more able to pay.²² Horizontal equity concerns the judgment that taxpayers situated in like circumstances should pay the same amount in

¹⁵ GRAETZ & SCHENK, *supra* note 10, at 28-29.

¹⁶ LAURIE L. MALMAN ET AL., *THE INDIVIDUAL TAX BASE* 9 (1st ed. 2002).

¹⁷ MALMAN ET AL., *supra* note 16, at 9.

¹⁸ GRAETZ & SCHENK, *supra* note 13, at 28-29.

¹⁹ MALMAN ET AL., *supra* note 16, at 9-11.

²⁰ MALMAN ET AL., *supra* note 16, at 11-12 (defining a deadweight loss as the "overall loss" that results when some taxpayers pay an imposed tax, but enough people avoid the tax by forgoing income or purchases that the government loses revenue and there is no transfer from one party to another, *viz.*, "individuals are worse off, but the public is no better off as a result").

²¹ GRAETZ & SCHENK, *supra* note 13, at 27-28.

²² SLEMRD & BAKIJA, *supra* note 14, at 59-60, 64-66.

taxes, but the definition of “like circumstances” is very much up for debate.²³ Taxpayer perception of the tax system as equitable or fair is seen as especially important for compliance, but the definition of fairness is very subjective.²⁴

- Simplicity is about implementation and compliance and is often broken down into three categories: rule, compliance and transactional complexity.²⁵ Rule simplicity is about how difficult it is for the Service to implement and enforce the tax law. Compliance simplicity pertains to how difficult it is for taxpayers to comply with the tax law.

Transactional simplicity concerns the transactional structures that taxpayers create to avoid aspects of the tax law or otherwise minimize tax liability. Simplicity strongly impacts efficiency and equity concerns because of the ability of taxpayers to understand and utilize the tax system and the time and resources necessary for taxpayers to comply with the Code and the Service to enforce compliance.²⁶ It is also strongly impacted by efficiency and equity because of Congress’ desire to increase the tax system’s equity without creating tax avoidance possibilities²⁷ and the Service’s efforts to close the tax gap by easing taxpayer compliance.²⁸

All three aspects of tax policy influence the Service’s current position, as far as it can be determined, on taxing each variety of Reward. A Reward earned on a personal purchase, i.e., a purchase involving only a cardholder, a merchant, and a Creditor, is generally²⁹ not considered

²³ GRAETZ & SCHENK, *supra* note 13, at 27-28; SLEMROD & BAKIJA, *supra* note 14, at 87-96.

²⁴ INTERNAL REVENUE SERV., U.S. DEPT. OF THE TREASURY, REDUCING THE FEDERAL TAX GAP: A REPORT ON IMPROVING VOLUNTARY COMPLIANCE 50-52 (2007); SLEMROD & BAKIJA, *supra* note 14, at 57-59.

²⁵ GRAETZ & SCHENK, *supra* note 13, at 29-31.

²⁶ GRAETZ & SCHENK, *supra* note 13, at 29; SLEMROD & BAKIJA, *supra* note 14, 160-164.

²⁷ SLEMROD & BAKIJA, *supra* note 14, at 165-67.

²⁸ INTERNAL REVENUE SERV., *supra* note 24, at 50-52.

²⁹ However, Cripe and Matzkin point out that if a personal expense is deductible, the tax benefit rule requires that the Reward reduce the deduction or be included in income if it occurs in a different taxable period. *Supra* note 2, at 312.

taxable income, regardless of whether the Reward is received in cash or in-kind.³⁰ Rather, the Reward is considered a purchase price reduction or rebate because some of the money paid to the Creditor has been repaid to the cardholder and the latter has therefore not truly had an accretion of wealth.³¹ Thus, it would be inequitable to include the rebate amount in taxable income.

Rewards earned in connection with a business expense are treated in a variety of ways. The Service will not tax an in-kind “promotional benefit,” e.g., frequent flyer miles or points converted to a toaster, “attributable to” a taxpayer’s business or official travel.³² Conversely, the Service currently claims to tax cash Rewards attributable to business travel expenses and in-kind Rewards converted to cash.³³ There is no current guidance on the taxation of in-kind Rewards “attributable to” general business expenses (not related to travel),³⁴ whether converted to cash or

³⁰ I.R.S. Priv. Ltr. Rul. 96-23-035 (June 7, 1996) (cash or charitable contribution); *see* I.R.S. Priv. Ltr. Rul. 93-40-007 (June 29, 1993) (noting that an individual who receives cash or an airline ticket as a result of personal flights taken with the airline has not realized gross income).

³¹ I.R.S. Priv. Ltr. Rul. 96-23-035 (June 7, 1996) (treating a reward donated to charity as a rebate), Cripe & Matzkin, *supra* note 2 at 311.

³² I.R.S. Announcement 2002-18, 2002-1 C.B. 621. The Announcement does not differentiate between “promotional benefits” earned by charging a business travel expense and those earned through an airline’s frequent flyer miles program.

³³ I.R.S. Announcement 2002-18, 2002-1 C.B. 621; *Charley*, 91 F.3d 72 (9th Cir. 1996) (holding that a conversion of frequent flyer miles to cash constituted either wages or a gain from the disposition of property). An in-kind Reward can be earned without using a personal credit card and then converted to cash. For example, some frequent flyer programs allow an individual to convert frequent flyer miles to dining gift cards, which are likely cash equivalents because they are “freely transferable,” “readily marketable,” and “immediately convertible to cash.” *See, e.g.*, Rev. Rul. 73-173, 1973-1 C.B. 40 (using this criteria to find that breeding rights in thoroughbred stallions were a cash equivalent); United Airlines, *Lettuce Entertain You*, <http://www.united.com/page/article/0,6722,52130,00.html> (last visited Apr. 16, 2009) (allowing a frequent flyer mile account holder to convert miles into dining certificates). Additionally, some individuals sell miles in the secondary market. Michelle Higgins, *Playing Markets That Trade Miles*, N.Y. TIMES, June 29, 2008, available at http://www.nytimes.com/2008/06/29/travel/29pracfflier.html?_r=1&scp=1&sq=playing%20markets%20that%20trade%20miles&st=cse. Cash equivalents earned in the former way is likely wage income and cash earned in the latter way is likely considered a gain from the sale of property. *See Charley*, 91 F.3d at 74 (holding that a conversion of frequent flyer miles to cash constituted either wages or a gain from the disposition of property). This article does not address Rewards earned through allegiance programs without charging a business expense on a personal credit card. Another issue for further study that is not analyzed here is the availability of deductions for donations of frequent flyer miles to charity. Since Announcement 2002-18 effectively exempts frequent flyer miles earned on business travel, a taxpayer is not taxed on the value of those miles. 2002-1 C.B. 621. Consequently, there is a question as to whether taxpayer-employee should also receive a deduction for a donation of those miles.

³⁴ In a typical large business an individual likely charges general business expenses only sporadically, but the opportunity exists to earn Rewards in this way using reimbursements under an employer’s accountable plan. I.R.C. § 62(a)(2)(A) (West 2009); *see also supra* Part II.B.1. Since these Rewards are also deductible is sufficiently attributable to business, they are included in the “business-related Rewards” category used herein.

in-kind benefits, but they should be treated similarly. The distinction between in-kind and cash Rewards reflects the Service's stated judgment that in-kind Rewards are more administratively and technically difficult to tax, including in relation to valuation, timing, and separation of basis attributable to benefits earned by personal or business use of a credit card.³⁵ Properly addressing this difficulty would increase the Service's administrative costs and taxpayers' and third party's compliance burdens. Therefore, the Service has effectively chosen to ignore in-kind Rewards. This presents the question of whether cash Rewards are sufficiently different to warrant the distinction and is discussed in Part II.B., *supra*.

Another oddity about the Service's official position regarding taxing a cash business-related Reward is that even within that category, only certain types of Rewards are effectively taxable. As discussed below in Part II.C.1., a per diem expense allowance reasonably calculated to cover an employee's reimbursable travel expense is deemed a substantiated expense and thus excluded from income. Although the Regulations require an employee to report excess per diem,³⁶ in the pertinent Revenue Procedure the Service only requires an employee to report certain types of excess per diem.³⁷ Consequently, any Reward earned on such expenses is effectively not taxed. Additionally, the field of Reward-earning opportunities is practically limited to reimbursed business expenses under Section 162. An employee may exclude a reimbursement from an employer to the extent that the underlying expense would be otherwise deductible under one of Sections 161 through 199.³⁸ However, most of the expenses otherwise

³⁵ I.R.S. Announcement 2002-18, 2002-1 C.B. 621.

³⁶ Treas. Reg. § 1.274-5(g) (as amended in 2003).

³⁷ The Service does not require an employee to include in income the excess, if any, of the substantiated per diem amount over the amount actually spent on business expenses if the employee satisfies the given substantiation rules. Treas. Reg. § 1.274-5(g) (as amended in 2003); Rev. Proc. 2008-59, 2008-41 I.R.B. 857 ¶ 7.03. The substantiated per diem amount is the lesser of the federal per diem rate for a locality or the per diem paid. Rev. Proc. 2008-59, 2008-41 I.R.B. 857 ¶ 4.01.

³⁸ See I.R.C. § 62(a)(2)(A) (West 2009).

deductible as an employee reimbursement likely would not give rise to a Reward.³⁹

Consequently, the primary category of Reward-earning opportunities is limited to those deductions available under Section 162.

B. Drawing parallels: Contributions from the literature on frequent flyer miles.

Most of the sparse literature related to the issue of Rewards addresses frequent flyer miles before the 2002 Announcement, but it provides some insight into the issue at hand. First, commentators have repeatedly demonstrated that a Reward earned on a reimbursable business expense is realized income,⁴⁰ but they have not fully explored the issues attendant on that conclusion. For example, a few commentators have discussed the timing problems inherent in the realization of Rewards.⁴¹ As discussed below in Part II.B., there may be a significant lag between when the taxpayer makes a charge that leads to a Reward and when that Reward is realized. Additionally, a taxpayer who has “earned” a Reward may never be able to convert it to cash, goods, or services due to contractual restrictions that may arise at any time under some cardholder agreements.⁴² These conditions may constitute a substantial restriction⁴³ and therefore the Reward should not be considered constructively received until the restrictions have

³⁹ For example, a personal credit card has no place in accounting for a business’ bad debts under Section 166. And, while a credit card could be used to pay interest expenses and taxes under Sections 163 and 164, respectively, such method would likely only be used in very small companies. Additionally, a credit card could be used to purchase depreciable equipment, but much of such equipment is impractical or too expensive singly (e.g., screen-printing equipment) or in the aggregate (e.g., 10 laptops) to purchase for even a small business with a personal credit card.

⁴⁰ Dominic L. Daher, *The Proposed Federal Taxation of Frequent Flyer Miles Received From Employers: Good Tax Policy But Bad Politics*, 16 AKRON TAX J. 1, 4 (2001); Sharon Alice Pouzar, *Frequent Flyer Awards as Taxable Income: Time to Pay the Taxman*, 5 TEX. WESLEYAN L. REV. 55, 60-61 (1998); Darrell L. Oliveira, *The Taxability of Frequent Flyer Credits Earned by Employees: Why the IRS Has Remained Silent on the Issue*, 4 U. PA. J. LAB. & EMP. L. 643, 646-47 (2002).

⁴¹ Oliveira, *supra* note 40, at 660-663; Pouzar, *supra* note 40, at 77.

⁴² Restrictions on the American Express Membership Rewards program. www.membershiprewards.com/terms (last visited Apr. 9, 2009).

⁴³ For example, the Second Circuit once held that required permission from a co-executor of an estate to release stock and cash was a substantial restriction and, therefore, the constructive receipt doctrine did not apply. *Wolder v. Comm’r*, 493 F.2d 608, 613 (1974); *see generally* BORIS I. BITTKER & LAWRENCE LOKKEN, FEDERAL TAXATION OF INCOME, ESTATES, AND GIFTS ¶ 5.9 (3d ed. 2001).

lapsed.⁴⁴ Additionally, some Reward programs limit the transfer or assignment of Rewards,⁴⁵ thereby rendering the cash equivalency doctrine inapplicable.⁴⁶ Nonetheless, these commentators have not fully discussed how timing affects the second major topic in the existing literature: classification. Classification is primarily important because of the possibility of excluding economic income from taxable income and, thus, is essential when determining if an employee should be taxed on Rewards earned using a personal credit card and how. Commentators have suggested several classification possibilities, including a purchase price adjustment,⁴⁷ a prize,⁴⁸ a taxable fringe benefit,⁴⁹ employment compensation,⁵⁰ and, simply, non-deductible income.⁵¹ However, as discussed below in Part II.B., none of these possibilities is free from doubt or complications. And, ultimately, none of the commentators are sufficiently precise to clearly assess the problem.

The available literature also leaves lingering issues, two of which are very important. First, although some have argued that the difficulties of valuation weigh in favor of exempting in-kind Rewards,⁵² other commentators have offered plausible, even practical, valuation methods.⁵³ Consequently, the argument that an in-kind business-related Reward is specially qualified for a formal policy of non-enforcement while a cash business-related Reward is not is more tenuous than it seems. This is discussed at length in Part II.A. Second, previous authors have also failed to appreciate the tax policy issue of effectively enforcing a tax on cash Rewards.

⁴⁴ Treas. Reg. § 1.451-2(a) (as amended in 1979).

⁴⁵ See, e.g., Restrictions on the American Express Membership Rewards program, www.membershiprewards.com/terms (last visited Apr. 9, 2009) (noting in paragraph titled “Point Accrual” that points are not the property of the cardholder and not transferable).

⁴⁶ *Cowden v. Comm’r*, 289 F.2d 20 (5th Cir. 1961).

⁴⁷ Kathy Krawczyk & Lorraine Wright, *How Should Frequent Flyer Miles Be Taxed?*, 79 TAX NOTES 1029 (1998).

⁴⁸ Jennifer A. Cunningham, *Are Frequent Flyer Benefits Really Benefits?: An Analysis of the Frequent Flyer Tax Debate and a New Theory of Taxability for Frequent Flyer Benefits*, 47 CLEV. ST. L. REV. 281 (1999).

⁴⁹ Daher, *supra* note 40, at 7-10.

⁵⁰ *Id.* at 4-7.

⁵¹ Pouzar, *supra* note 40, at 59-71.

⁵² Oliveira, *supra* note 40, at 656-658.

⁵³ Pouzar, *supra* note 40, at 75-77.

That is, by the basic tenets of tax policy analysis, a tax should be efficient, equitable, and relatively simple.⁵⁴ Each of these components is interlinked; thus, when one fails, the others suffer as well. Of course, many taxes exist that are not easily administrable from the Service's perspective or that create compliance costs from the taxpayer's or a third party's perspective. The question is whether the cost (financial and political) of enforcing any one tax (or failing to exempt it) outweighs the benefits (financial and political) of enforcement. This issue is also discussed in more detail below in Part II.C.

II. Reading Between the Lines: Why the Service Should Not Tax Cash Business-related Rewards

Taxing cash business-related Rewards is a losing battle for many reasons. First, although valuation difficulties are typically cited as the reason why in-kind business-related Rewards are not taxed, the asserted difficulties are not insurmountable and can be addressed using several different methods. Therefore, the major reason to distinguish between cash and in-kind Rewards quickly disintegrates and the question becomes why tax Rewards at all. Second, the best option to classify business-related Rewards is as an excess reimbursement under Section 62. However, because this classification is the result of two relationships (between the taxpayer and each of an employer and a Creditor), it is very difficult to determine the amount of potential income and who receives it. Thus, third, classifying the Rewards as an excess reimbursement opens a Pandora's box of policy problems because enforcing the tax is administratively cumbersome and burdensome, but not enforcing the tax is inequitable, opaque, and erodes the legitimacy of the tax system. Consequently, for policy and pragmatic reasons, the Service should exclude all business-related Rewards from taxable income.

⁵⁴ GRAETZ & SCHENK, *supra* note 13, at 27-31; U.S. GOV'T ACCOUNTABILITY OFFICE, PUB. NO. 05-1009SP UNDERSTANDING THE TAX REFORM DEBATE: BACKGROUND, CRITERIA, AND QUESTIONS 24 (2005).

A. Looking at the price tag: why the distinction between valuating cash and in-kind Rewards is not sufficiently significant to warrant different treatment.

Although the traditional rule is to tax all accretions of wealth unless specifically exempted,⁵⁵ income realized as goods or services is sometimes treated differently than income realized as cash, often because of valuation and its attendant problems. Valuation of goods or services can be difficult because there are several reference points for valuation – prevailing market price, price normally charged by the taxpayer and taken as the fair market value,⁵⁶ etc. – and no single point may be perfect in a given situation. Additionally, each method has its own attendant problems, *viz.*, even using fair market value requires identification of the appropriate market. A taxpayer does not generally face these problems when she receives cash because cash only has a face value.⁵⁷ It follows that valuation is less of a problem with cash Rewards than with in-kind Rewards, but, is valuation really a significant problem with in-kind Rewards or is the Service laboring under a false assumption?

Traditionally, the crux of the issue has been price fluctuation, an obvious conundrum when valuing airline tickets received as rewards, but not necessarily as onerous when contemplating the valuation of other in-kind goods, e.g., toasters, coffee makers, and even hotel lodgings. But, since much of the literature focuses on frequent flyer miles, and because they still account for a large portion of in-kind Rewards earned, valuation has been and still is an important issue in this debate. Thus, congressional representatives have focused on the fluctuating nature of value of airline tickets in several failed attempts to change the taxation of frequent flyer miles.⁵⁸ Nonetheless, commentators have suggested several valuation methods,

⁵⁵ I.R.C. § 61 (West 2009); *Comm'r v. Glenshaw Glass*, 348 U.S. 426, 430 (1955).

⁵⁶ Treas. Reg. § 1.61-2(d)(1) (as amended in 2003); Rev. Rul. 80-52, 1980-1 C.B. 100 (bartering).

⁵⁷ I.R.C. § 1001(b) (West 2009).

⁵⁸ *See, e.g.*, H.R. 3111, 104th Cong. (1996), H.R. 533, 105th Cong. (1997); HR 1139, 108th Cong. (2003).

most of which have pitfalls, but all of which have some redeeming features,⁵⁹ indicating that valuation is not as hard a nut to crack as the Service seems to think it is. Of the methods proposed, using the Creditor's determination of fair market value of a good or service obtained using points is the best solution. The Creditor will likely already know this amount and will have correlated the value of points accordingly. Thus, even products with highly variable fair market values, e.g., airline tickets, can be valued efficiently and with reasonable accuracy.

Arbitrary Value. As Dominic Daher proposed in 1999⁶⁰ and Lee Garsson discussed in 1986,⁶¹ the Service or the Congress could simply set an arbitrary value for reward points. Setting an arbitrary value for reward points is a reasonable proposition – there are many current examples of apparently arbitrary limits, including those used to value employee flights on employer-provided aircraft.⁶² An arbitrary value would also be easy to enforce. This type of method should be keyed to a reliable measure of pertinent price changes, e.g., the consumer price index, but there will still be a risk that the values would become irrelevant over time as the market for air travel services and overall economic climate change.

Secondary Market Value. The secondary market value of reward points, vouchers, or in-kind goods is the amount of money (or value of goods or services) that the seller receives in exchange.⁶³ There is currently a market for the sale of at least some frequent flyer miles⁶⁴ and any other type of good or voucher for services can easily be sold in the broader market. Thus, the theory is that value can be determined by reference to the prevailing market price. Oliveira

⁵⁹ Pouzar, *supra* note 40, at 71-75; Oliveira, *supra* note 40, at 651-658.

⁶⁰ Daher, *supra* note 40, at 18.

⁶¹ Garsson, *supra* note 6, at 989-992 (discussing the “commercial flight valuation” and “non-commercial flight valuation” rules in the Regulations).

⁶² Treas. Reg. § 1.61-21(g) (as amended in 1992). For additional examples, see Announcement 2008-63 on optional standard mileage rates, Section 368(c), defining “control” as 80% in corporate reorganizations, and Section 195, allowing an election to deduct start-up costs limited to \$5,000 or less in first year.

⁶³ Oliveira, *supra* note 40, at 654.

⁶⁴ Higgins, *supra* note 35. Some frequent flyer mile programs do not allow participants to transfer miles, however.

argues that the secondary market will always undervalue the reward points and therefore a holder of frequent flyer miles will be taxed on far less value than they have received.⁶⁵ This may be true – or not. Thus, the question is really whether the “secondary market price” should equate to liquidation or replacement value. But, even this issue could be solved by instead looking to the amount that frequent flyer programs charge consumers to purchase miles.⁶⁶ From there, it is possible to extrapolate the value of other in-kind items available in the same or similar programs. Or, the amount assessed as consistent with value on a secondary market could be a method of establishing basis, leaving open the question of later assessing more tax upon use or sale. This admittedly overcomplicates matters, but would ensure at least some taxation of in-kind Rewards.

Comparison value. Oliveira raises the issue of valuation by comparison, i.e., comparing the number of Reward points needed for an airline ticket with the number needed for some other in-kind gift.⁶⁷ But, he complicates matters by arguing that this method is inapt because the Creditor may require more or fewer points than are consistent with the item’s fair market value. Yet, this observation is not fatal so long as the conversion is reasonable, i.e., a willing consumer would pay that price and a willing seller would sell it for that price.⁶⁸ Additionally, a manufacturer’s suggested retail price or a service-provider’s usual price can be used to establish a fair comparison value. And, just as a taxpayer can decline a prize to avoid taxation in excess of

⁶⁵ Oliveira, *supra* note 40, at 654. The Ninth Circuit held in the *Charley* decision that if the taxpayer’s frequent flyer miles were considered property, then he had no basis in them. *Charley*, 91 F.3d at 74 (9th Cir. 1996). This could drive down the value of Reward points in the secondary market, but also may not affect the market price at all.

⁶⁶ For example, Delta recently sold miles for \$.0275 per mile, plus the federal excise tax. Delta SkyMiles, Buy Miles, http://www.delta.com/skymiles/buy_transfer/buy_miles/index.jsp (last visited Apr. 16, 2009).

⁶⁷ Oliveira, *supra* note 40 at 655.

⁶⁸ This is logical in light of the Regulatory definition of fair market value: “the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts.” Treas. Reg. § 1.170A-1(c)(2) (as amended in 2008). Thus, if a taxpayer is willing to pay less at WalMart to purchase an item also available at Macy’s, the taxpayer who accepts a prize of the same item should be taxed at the normal retail price at the pertinent retailer.

what the prize is worth to her,⁶⁹ a cardholder can either redeem points for an item or purchase it elsewhere if she thinks that she is not getting the best value for her points.

*Fair market value determined by the Creditor.*⁷⁰ Fair market value can also be determined by requiring a Creditor (or the party that operates a reward fulfillment service) to report to the cardholder and the Service the retail value⁷¹ of the item “purchased” with points or the conversion value of the points themselves. Reward card issuers likely already have this information for in-kind Rewards⁷² - it is in their interest to correlate point value with the value of an item and to publish such correlation in order to encourage participation in the program. Some issuers also use a maximum value categorization, e.g., a plane ticket in the lower forty-eight is worth twenty-five thousand points earned by using one of Capital One’s Reward cards. However, those twenty-five thousand points convert to a plane ticket worth up to \$250.00.⁷³ This maximum value categorization could also be used as a somewhat arbitrary measure of fair market value, especially when the increments are relatively small.

Relying on Creditor determinations of value may create a perceived inequity because the value of some in-kind products, e.g., airline tickets, fluctuate very quickly and the points necessary to “purchase” such product may not adjust correspondingly.⁷⁴ However, purchasing with points and purchasing with cash are inherently different transactions and, in the context of airline tickets especially, the seat that can be purchased with cash may not be available to

⁶⁹ Rev. Rul. 57-374, 1957-2 CB 69.

⁷⁰ See Pouzar, *supra* note 40, at 75-77 (concluding that using airline company conversion rates to value frequent flyer miles is ideal in a system that taxes Rewards attributable to business-related frequent flyer miles).

⁷¹ Many in-kind Rewards are commonly available consumer goods and travel and entertainment services. Thus, the retail price of these goods is the best measure of how much the taxpayer would otherwise spend to obtain such good or service.

⁷² Pouzar, *supra* note 40, at 74-75 (noting that in at least two cases involving frequent flyer miles, the airlines involved had a fixed value for frequent flyer miles).

⁷³ Capital One No Hassle Points Reward Card,

http://www.capitalone.com/creditcards/products/points/?linkid=WWW_0608_CARD_TGUNS01_CCPC_H3_03_TCCPP (last visited Apr. 9, 2009).

⁷⁴ See Oliveira, *supra* note 40, at 652-654.

purchase with points. Thus, a comparison of the two will never be anything more than an estimate of fair market value. Moreover, considering the variation in airline ticket prices from seat to seat based on time of purchase, time of flight, discount categories, and other variables,⁷⁵ comparing the value of one seat to another is somewhat artificial anyway. Consequently, using the Creditor's valuation of an in-kind Reward may be the best measure of fair market value.

In light of these viable options for valuing in-kind Rewards, the argument that they should be treated differently from cash Rewards begins to falter. If the Service truly wanted to tax in-kind Rewards, it could simply require Companies to report cash values for Reward points or provide notice to cardholders of the fair market value of the in-kind Reward redeemed.⁷⁶ Thus, the argument is reduced to the appropriateness of taxing Rewards at all.

B. The name game: issues related to classifying Rewards.

The inability to classify income is not an impediment to recognition,⁷⁷ but classification is essential to determine if an exception to recognition or a deduction applies⁷⁸ and how to characterize the income. Classification of income may also reveal some of the inherent problems in taxing an income source. Thus, it is important to classify what kind of income Rewards are, especially when an individual taxpayer earns them as a result of charging an employer's expenses on the taxpayer's personal credit card.

1. Labeling: proper classification of a cash business-related Reward earned on a reimbursable expense as an excess reimbursement

⁷⁵ Notably, some frequent flyer programs change the number of points needed to "purchase" a seat based on price variation within their own system, which presumably reflects broader market fluctuations.

⁷⁶ Pouzar argues for the latter, but as discussed below in Part II.C., relying on self-reporting is unlikely to solve the problem. *Supra*, note 30, at 77.

⁷⁷ See *Glenshaw Glass*, 348 U.S. at 430 (1955) (holding that any accretion to wealth is taxable income unless exempted).

⁷⁸ For example, deductions under provisions Sections 212 and 168 and nonrecognition provisions such as Section 119 require classification of some underlying factor, e.g., the activity for which the expense arises, the nature of the item and how it is used, or the taxpayer and how they benefit.

Proper classification of Rewards depends on how the points were earned and the identity of the parties involved and their relationships to each other. A Reward usually arises when an individual uses a credit card to pay a merchant for goods or services and thereby agrees to instead transfer money to the credit card issuer, i.e., the Creditor, in payment for the goods or services and not the third party directly. The individual is always liable to pay to the Creditor the full amount charged, but as a consequence may receive a Reward point or cash rebate. As discussed above in Part I.A., in some cases, the Service has defined cash received in a Reward program as a rebate, but only when the Reward arises from a personal expense.⁷⁹ Although the Service has not similarly defined a business-related Reward as a rebate, it should.

Classifying a Reward as a rebate makes sense, but requires a few steps and focus on the roles of each party involved. In a 1996 private letter ruling, the Service decided that an amount paid by a retailer to a credit card company and then donated on behalf of a cardholder to a charity was a rebate.⁸⁰ In this scenario, the amount paid by the retailer was a percentage of the purchase price of whatever item the cardholder purchased and is therefore easy to label a rebate. However, the Tax Court has found that an amount paid by a third party to a purchaser without involving the seller reduced the basis in the property purchased (and therefore was effectively a rebate).⁸¹ In *Freedom Newspapers*, the seller's agent agreed to pay the purchaser of several newspapers a flat amount to induce the purchaser to buy an additional newspaper, which the agent was required to sell in order to earn a commission from the seller. The court held that the inducement reduced the purchaser's basis in the properties and was not current income because

⁷⁹ I.R.S. Priv. Ltr. Rul. 96-23-035 (June 7, 1996).

⁸⁰ I.R.S. Priv. Ltr. Rul. 96-23-035 (June 7, 1996).

⁸¹ *Freedom Newspapers v. Comm'r*, 36 T.C.M. (CCH) 1755 (1977). See also Priv. Ltr. Rul. 2007-43-003, 11-12 (July 25, 2007) (citing *Freedom Newspapers* and stating that the key issues were that the second transaction clearly related back to the original purchase, the agreements were contemporaneous, and the taxpayer would not have otherwise made the purchase.)

the agreement that produced the inducement could not be separated from the agreement to purchase the properties.⁸² The court reasoned that the two transactions were inseparable because the purchaser was otherwise reluctant to buy the property, the agreements were made on two consecutive days, and the agent intended to induce the purchaser to buy the property.⁸³

The scenario in *Freedom Newspapers* can be analogized to the payment of a Reward to a cardholder who uses a credit card to purchase goods or services from a merchant. In a credit card transaction, the Creditor is the third party in a transaction otherwise between a merchant and a purchaser. The Creditor pays a Reward to induce a cardholder to purchase something, which transaction gives rise to a payment from the merchant to the Creditor, much like the commission in *Freedom Newspapers*. The direct relationship between the sale and the rebate is similar to the direct relationship between the sale and the payment in *Freedom Newspapers*. And, although the cardholder may have many reasons for using a particular credit card, it is reasonable to infer that she would not use a given credit card if it did not pay a Reward. Consequently, the logic of *Freedom Newspapers* could be applied to classify a Reward as a purchase price reduction or rebate.

When an individual uses a credit card to charge a reimbursable business expense, another relationship is established. In this relationship, the individual as an employee purchases something in her employer's stead and may deduct the expense from her taxable income, but only as an itemized deduction.⁸⁴ Alternatively, if the employer reimburses the employee for the expense, the expense is deducted in full from the employee's taxable income.⁸⁵ However, for the

⁸² *Freedom Newspapers*, 36 T.C.M. (CCH) at 1757 (citing *Arrowsmith v. Comm'r*, 344 U.S. 6 (1952) and *Federal Bulk Carriers, Inc. v. Comm'r*, 66 T.C. 283 (1976) for the proposition that losses that are intimately related to an earlier sale should be characterized in reference to the sale).

⁸³ *Freedom Newspapers*, 36 T.C.M. (CCH) at 1756 (drawing parallels to *Brown v. Comm'r*, 10 B.T.A. 1036, 1054-55 (1928)).

⁸⁴ I.R.C. § 162(a) (West 2009).

⁸⁵ I.R.C. § 62(a)(2)(A) (West 2009).

employee to receive this treatment, the employer must maintain an “accountable plan” that requires an employee to return any amounts reimbursed in excess of the substantiated expense.⁸⁶ The employee may choose to not return any excess amount, but such excess will fail to qualify for Section 62(a)(2)(A) treatment.

The problem with cash Rewards lies in the interaction between these two relationships (as depicted in Figure 1, below). If the Creditor and employer relationships are separate, then the employer is reimbursing the employee for the full expense and the Reward is an additional amount received from the Creditor. The problem is that since a cash Reward is essentially a rebate,⁸⁷ the employee appears to have improperly received a benefit.⁸⁸ This benefit is “other income” because the relationship between the Creditor and the employee and the employer and employee are separate. But, since the charge that generated the Reward would not have occurred but for the employment relationship, the Reward should be considered a rebate on the reimbursable expense. This correlates with the current treatment of Rewards earned on personal expenses and since there is no relationship between the employer and the Creditor a business-related Reward is also fundamentally a rebate on the purchase. Consequently, the employee has received a reimbursement that exceeds the expenses actually paid or incurred. This excess amount is not matched by a deduction under Section 162(a) and therefore, not deductible under Section 62(a)(2)(A). Rather, it is wage income.⁸⁹

⁸⁶ Treas. Reg. § 1.62-2 (as amended in 2003). In a technical advice memorandum concerning frequent flyer miles, the Service held that a company policy allowing employees to retain frequent flyer plan benefits rendered the company’s reimbursement policy not an accountable plan. I.R.S. Tech. Adv. Mem. 95-47-001 (July 11, 1995). Therefore, the expenses paid by employees were only itemized deductions under Section 162. *Id.* However, the memorandum provoked such strong outcries from the tax community, that the Service quickly stated that it had no official policy regarding frequent flyer mile programs. Sheryl Stratton & Ryan J. Donmoyer, *Don’t Ask, Don’t Tell: The IRS’s Frequent Flyer Policy*, 69 TAX NOTES 1159 (1995).

⁸⁷ See discussion *supra* pp. 17-18.

⁸⁸ Cunningham, *supra* note 48, at 288-289.

⁸⁹ The excess is treated as not made under an accountable plan, but rather as under an unaccountable plan. Treas. Reg. § 1.62-2(c)(2)(ii), (c)(3)(ii) (as amended in 2003). Consequently, the excess amount is included in the

Reward from wage income and avoid the issue of taxing an employer who may have no idea that an employee has earned a cash Reward. However, another commentator was equally imprecise when he declared that frequent flyer miles are general wages or even taxable fringe benefits.⁹³ While these classifications are true in a rough and ready sort of way, they are unsuitable for a probing analysis of the issues or for devising a solution to the tax policy problem.

Alternatively, and not mentioned in the literature, the Reward could be interest income. Looking again at the structure of the two transactions, a reimbursable expense paid by the employee resembles a short-term loan from the employee to the employer (regardless of the payment method). When the employee additionally earns a Reward, the total reimbursement exceeds the amount actually loaned. Thus, the Reward is similar to original issue discount (“OID”),⁹⁴ but the employer likely pays the redemption price long before the Creditor’s payment of a Reward to the taxpayer has reduced the issue price and “interest” has arisen (without the employer’s knowledge or participation). There is also additional OID because no stated interest was paid on the “loan” and the issue price must be imputed.⁹⁵ In other words, the relationships among the parties render classification of the Reward as interest income bizarre (and ultimately unnecessary because of Regulation 1.62-2).

Finally, the Reward could also be construed as a reduction in the cost of credit, i.e., annual fees or interest payments to a Creditor. This formulation is appealing because the Creditor has direct control over the cost of credit and, therefore, the link between the merchant and the Creditor is no longer an issue. However, the characterization as a reduction in the cost of credit is difficult when one looks at the composition of a cardholder’s cost of credit. A Reward cannot be attributable to an annual fee because that is levied regardless of use. Additionally,

⁹³ Daher, *supra* note 40, at 4-5, 7.

⁹⁴ See I.R.C. § 1273 (West 2009) (defining OID).

⁹⁵ I.R.C. § 1274(a)(2) (West 2009).

Rewards are generally not awarded based on fees or interest paid to the Creditor.⁹⁶ Therefore, it does not make sense to say that a Reward is a reduction in the cost of credit when it has no relationship with any component of a cardholder's cost of credit. Additionally, the relationship between the cardholder and her employer still complicates matters. Since the cost of credit (even on a personal card⁹⁷) could be an ordinary and necessary business expense under Section 162, there is a possibility that it could also be a reimbursable business expense under Section 62. If properly attributable to a reimbursable business expense, then the cost of credit is reduced, but probably not reimbursed by the employer. Consequently, taxable income only arises when the value of the Reward exceeds the cardholder's cost of credit. In that case, the Reward is income paid by the Creditor and is still deductible under Section 162, but the relationship between the employer and the employee means that the Reward could still be construed as an excess reimbursement under Section 62(a)(2)(A) even though paid by a third party. Thus, the Reward is still characterized as employment income in at least some scenarios.

2. The Ripple Effect: why classifying cash business-related Rewards as an excess reimbursement is problematic.

Although it is the most logical conclusion, classifying a cash Reward as wage income presents numerous problems, most of which refer back to why classification as a rebate is appealing. First, the timing is problematic. Either kind of Reward usually cannot be realized

⁹⁶ See, e.g., Restrictions on the American Express Membership Rewards program. www.membershiprewards.com/terms (last visited Apr. 9, 2009) (noting in paragraph titled "Point Accrual" that points will not be earned on payments of, among other things, annual fees, finance fees, and delinquency fees); Capital One No Hassle Rewards Credit Card, http://www.capitalone.com/creditcards/products/cash/?linkid=WWW_0608_CARD_TGUNS01_CCMAIN_C2_07_T_CCPC (last visited June 16, 2009) (noting that points are not earned on payments of, among other things, finance charges and fees of any kind).

⁹⁷ If the cardholder can separate personal and business charges and the corresponding cost of credit, then she should claim a deduction for the cost of credit if it arises from an otherwise deductible expense and it was incurred for an ordinary and necessary reason. This is consistent with the concept of an ordinary and necessary business expense. See BITTKER & LOKKEN, *supra* note 43, at ¶ 20.3.2.

until the Reward points are converted to a good, service, or cash equivalent.⁹⁸ A Reward is generally contingent on multiple factors, e.g., payment of a minimum balance⁹⁹ or the total amount due, timely use,¹⁰⁰ and keeping a credit line open.¹⁰¹ Additionally, a Creditor generally reserves the right to deny Reward points.¹⁰² Therefore, the employee has not realized a Reward until it has been converted to a good, service, or cash equivalent,¹⁰³ i.e., when she has redeemed Reward points or sold them to a third party, perhaps months after the charge was made.

Additionally, if the Reward is a wage, then the employer must pay appropriate taxes on it and therefore must somehow track the employee's receipt of a Reward. This imposes a heavy burden on a party that has no direct control over a Reward and may not know that an employee has received it. Since the Reward may be received long after the expense was paid or incurred (or after the employment relationship was terminated), the excess reimbursement may not arise within a "reasonable period" and the taxpayer will be unable to return it within the appropriate time period.¹⁰⁴ An obvious solution is for an employer to refuse to reimburse expenses charged on personal Reward credit cards, which would effectively eliminate all Rewards earned on business expenses. While this would close the loophole, employers know that allowing employees to use a personal credit card is a valuable (and effectively free) perquisite thus

⁹⁸ See discussion on constructive receipt *supra* p. 10. However, barring other restrictions that substantially restrict the taxpayer's use of the Reward, a transferable Reward is likely constructively received when earned. *Cowden v. Comm'r*, 289 F.2d 20 (5th Cir. 1961).

⁹⁹ A restriction on the Discover More Rewards program. Discover More, <http://www.discovercard.com/more/faqs.html> (last visited Apr. 9, 2009).

¹⁰⁰ Reward points earned on the Citi Professionalsm Card with Thank You[®] Network expire after time period unspecified in the materials available on the internet. Citi Professional Card with Thank You[®] Network, https://www.citicards.com/cards/wv/cardDetail.do?screenID=913&origincontentId=CC_TY_REWARDS&CONTENT_TYPE=card_category_detail (last visited Apr. 9, 2009).

¹⁰¹ Restrictions on the American Express Membership Rewards program. www.membershiprewards.com/terms (last visited Apr. 9, 2009).

¹⁰² For example, see the "General Rewards and Point Redemption Information" section of the American Express Membership Rewards terms and conditions document at www.membershiprewards.com/terms. (last visited Apr. 9, 2009).

¹⁰³ Pouzar, *supra* note 40, at 77; Garsson, *supra* note 6, at 993.

¹⁰⁴ Treas. Reg. § 1.62-2(f), (g) (as amended in 2003).

making effective enforcement another matter, as discussed in Part II.C., *supra*. And, barring the use of a company card, the employer would have no way to insure that an employee does not use a personal Reward card.

C. Shoulda, coulda, woulda: Tax policy issues.

Taxing cash Rewards is problematic from a policy perspective primarily because of the impossibility of effective enforcement. The problem is that although the Service maintains that it will enforce the rule that a cash business-related Reward is taxable income,¹⁰⁵ reality is probably much different because the Service must rely on self-reporting, the least effective method of tax collection.¹⁰⁶ Additionally, since cash Rewards are otherwise treated as a rebate paid by the Creditor, it is counterintuitive for many taxpayers to think of a cash Reward as income, especially when the taxable Reward arises on a personal card used for personal purchases as well as business purchases. Pertinent information on the taxation of cash business-related Rewards is also not readily available to the average taxpayer.¹⁰⁷ Thus, the Service has a conundrum: try to enforce the tax or simply ignore it.

Either choice is complicated and unsatisfactory for policy reasons. On the one hand, the administrative and compliance costs of enforcement are likely substantial and would probably outweigh the benefit of enforcement. On the other, having a tax and not enforcing it is inequitable and impairs the transparency of the tax system. Thus, Congress and the Service must evaluate the policy behind each choice to determine which is better, i.e., to tax, to merely say that

¹⁰⁵ I.R.S. Announcement 2002-18, 2002-1 C.B. 621.

¹⁰⁶ Self-reporting famously equates to non-reporting in many circumstances. *See* INTERNAL REVENUE SERV., NEWS RELEASE IR-2006-28, I.R.S. STUDY UPDATES TAX GAP ESTIMATES (2006) (noting that compliance is highest when third-party reporting or withholding occurs).

¹⁰⁷ For example, in a recent search of the IRS website, the author did not find any information on Rewards using numerous synonyms, e.g., “reward”, “rebate”, “cashback”, and “kickback.”

it will tax and therefore exclude, or to positively exclude.¹⁰⁸ These choices often relate to the operability of the system in light of fundamental policy goals.¹⁰⁹ As discussed above, tax policy concerns efficiency, vertical and horizontal equity, and simplicity.¹¹⁰ Of these goals, equity and simplicity are most directly pertinent to the issue herein, but efficiency and other issues such as privacy and transparency pervade the questions related to simplicity. Since the policy issues vary based on the type of enforcement used, they will be evaluated as they arise in the context of enforcement solely through self-reporting and enforcement with third-party information reporting.

1. Honest Abe? “Enforcement” through self-reporting

Currently, the Service implements its policy of taxing cash business-related Rewards by relying on self-reporting. Even though an employer is required to report an excess reimbursement,¹¹¹ because the employer is not required to determine if an employee uses a cash Rewards card to charge business expenses, it cannot account for a Reward received as an excess reimbursement. Since a Creditor is also not required to file an information return on payment of a Reward to a cardholder,¹¹² the result is that the Service must rely on the taxpayer to self-report. This is troublesome because while it is true that a taxpayer is under a legal duty to report income, it is also well documented that compliance is low when only an income recipient reports income to the Service.¹¹³ Consequently, while the Service says that it will tax cash business-related Rewards, in reality it is not equipped to so do.

¹⁰⁸ See Patricia D. White, *Realization, Recognition, Reconciliation, Rationality and the Structure of the Federal Income Tax System*, 88 MICH. L. REV. 2034, 2042 (1990) (discussing the policy choices attendant on deciding to tax income currently, exclude income, or defer taxation).

¹⁰⁹ *Id.* at 2043.

¹¹⁰ See *supra* Part I.A.

¹¹¹ Treas. Reg. § 31.3121(a)-3(b)(1) (1990).

¹¹² I.R.S. Priv. Ltr. Rul. 93-40-007 (June 29, 1993).

¹¹³ INTERNAL REVENUE SERV., *supra* note 106. Low compliance may result from evasion, avoidance, or simply lack of knowledge. Either way, the Service is not collecting revenue.

As an initial problem, requiring self-reporting without the threat of probable repercussions causes low compliance, which impairs the equity of the tax system. The horizontal equity of the tax system is impaired because some taxpayers report the income while many other taxpayers do not either because they do not know to so do or because they know that they will not be caught.¹¹⁴ Over time, the number of taxpayers who do report cash business-related Rewards (if, indeed, there are any currently) will dwindle as they realize that they are at slight risk of incurring a tax liability even while they are subsidizing free-riders.¹¹⁵ At the same time, taxpayer confidence in the system will suffer, possibly leading to additional evasion. Additionally, failing to enforce a tax such as the one at hand may result in vertical inequity because the people who earn cash business-related Rewards are likely those in more prestigious positions at an organization and, thus, at higher income levels.¹¹⁶

Additionally, self-reporting of cash business-related Rewards in particular would impose high compliance costs on both the employee and the employer. Both parties must account for reimbursed expenses charged on a personal credit card and then account for the cash Reward the employee realized in order to pay the appropriate tax. When such expense is an itemized reimbursement, e.g., the cost of a plane ticket, the employee could likely obtain reimbursement records from the employer,¹¹⁷ but must still link each expense with the corresponding cash Reward, if the employee realizes one. This detailed and time-consuming work to account for what is likely a small amount of money imposes large compliance costs on the taxpayer, which could affect her compliance generally. In many cases, these costs are unwarranted because the

¹¹⁴ John L. Mikesell, *Administration and the Public Revenue System: A View of Tax Administration*, 34 PUB. ADMIN. REV. 615, 620 (1974).

¹¹⁵ SLEMROD & BAKUA, *supra* note 14, at 174-175.

¹¹⁶ See Oliveira, *supra* note 40, at 664 (noting the concern that higher-income individuals are more likely to earn business-related frequent flyer miles).

¹¹⁷ The employer must record all such reimbursements and retain the records for use in audits unless the Service has prescribed rules to the contrary. Treas. Reg. § 1.62-2(e)(1) (as amended in 2003); Temp. Treas. Reg. § 1.274-5T(c)(2)(iv) (as amended in 2003).

annual Rewards earned by any one taxpayer on business-related expenses are likely relatively small.¹¹⁸ Conversely, if the expenses are paid as a per diem allowance,¹¹⁹ the employer is not required to record each item reimbursed, but still satisfies the substantiation requirement for reimbursable business expenses provided that the per diem amount is reasonably calculated to not exceed the employee's expenses.¹²⁰ And, any amounts that the employee does not spend may be excluded from her gross income.¹²¹ Therefore, an employee will likely also not be taxed at all on cash Rewards attributable to a per diem expense because it is similar to the extra per diem received but saved through an employee's careful use of the allowance. This result appears to arise from the administrative difficulty of discovering if an employee has excess per diem, a reason that should also apply to (not) taxing the Reward. This raises the question whether there is even sufficient revenue to be gained from administering the tax since an informed company

¹¹⁸ This assertion is based on a confluence of data regarding consumer credit card usage and the Rewards available on consumer bank type and American Express credit cards. In 2007, consumers utilized \$939.5 billion of revolving credit (seasonally adjusted). FED. RESERVE BD., FED. RESERVE STATISTICAL RELEASE, CONSUMER CREDIT G.19 (Apr. 7, 2009), available at <http://www.federalreserve.gov/releases/g19/current/g19.htm>. According to the Federal Reserve Bank, most revolving credit consists of credit card debt. BD. OF GOVERNORS OF THE FED. RESERVE SYS., REPORT TO THE CONGRESS ON PRACTICES OF THE CONSUMER CREDIT INDUSTRY IN SOLICITING AND EXTENDING CREDIT AND THEIR EFFECTS ON CONSUMER DEBT AND INSOLVENCY 5 n.1 (2006). However, the value of Reward points earned is likely significantly less than this figure. First, of course, not all credit cards are Reward cards. See e.g., Darlin, *supra* note 1 (noting that in 2005, approximately two-thirds of credit cards in use had a Reward feature); Torres, *supra* note 8 (noting that a recent industry survey showed that Reward cards were used in 70% of card transactions). Additionally, some Creditors allow a cardholder to earn Rewards only on amounts paid to the Creditor. Yet, in 2007, 46.1% of the families surveyed by the Federal Reserve carried a credit card debt with a mean balance of \$7,300 and median balance of \$3,000. Brian K. Bucks et al., *Changes in U.S. Family Finances from 2004 to 2007: Evidence from the Survey of Consumer Finances*, 95 FED. RESERVE BULLETIN A1, A45 (2009). Cardholders also earn variable Rewards depending on what they purchase and some purchases may not give rise to Rewards at all. See *infra* Appendix 1. Furthermore, every year Creditors cancel many Rewards earned for various reasons. Jane J. Kim, *How to Lose (Reward) Points*, WALL ST. J., <http://blogs.wsj.com/wallet/2009/01/14/how-to-lose-reward-points/> (last visited Apr. 9, 2009). Consequently, in 2005, Discover reported to the New York Times, that it had paid \$500 million in Rewards, or approximately .053% of the total revolving credit in 2004. Darlin, *supra* note 1. While Discover is a relatively small player in the credit card markets, more credit card charges are likely made for personal expenses than for business expenses. Thus, the true value of cash business-related Rewards is likely relatively small and, thus, the amount of revenue to be gained is even smaller.

¹¹⁹ Although the per diem method is limited to travel expenses, it likely accounts for many of the reimbursements made to employees, as discussed in more detail below.

¹²⁰ Treas. Reg. § 1.62-2(f)(2) (as amended in 2003); Rev. Proc. 2008-59, 2008-41 I.R.B. 857.

¹²¹ See discussion *supra* p. 9.

would pay a per diem allowance within legal limits and its employees therefore escape taxation in any event.

Finally, enforcing the tax on cash business-related Rewards will impair economic efficiency as well. Although in the reimbursable business expense scenario at issue here the incidence will fall on the employee as intended, other taxpayers may shift the increased cost to their own customers. Some taxpayers will substitute other payment methods for business expenses, perhaps losing benefits that they would otherwise obtain by using a cash Reward card and skewing the market toward less efficient payment methods. This substitution effect may cause the Service to spend money on enforcement without gaining tax revenue, consequently producing nothing but a deadweight loss.

2. Proliferating 1099s: enforcement using increased third party information reporting

While it would improve compliance, imposing a reporting burden for all cash business-related Rewards on a third party is problematic because it imposes large compliance costs on the third party and could impair the efficiency of the tax system. For example, the Service could increase the employer's reporting requirements¹²² on reimbursements by requiring it to flag reimbursements where an employee used a personal cash Rewards card or require that the Creditor report all cash Reward payments. Or, the Service could do both.

Although both Creditors and employers likely already maintain the pertinent records and the additional cost of preparing them may be marginal because of automated accounting systems,¹²³ a tailored reporting process would create much higher expenses for several parties.

¹²² An employer is already generally required to submit an information report regarding reimbursements paid to employees. I.R.C. § 6041 (West 2009); Treas. Reg. §§ 1.62-2(l) (as amended in 2003), 1.6041-3(k) (as amended in 2006).

¹²³ Jay A. Soled, *Homage to Information Returns*, 27 VA. TAX REV. 371, 389 (2007).

First, the employer and the Creditor must specifically calculate and report the pertinent information to the Service and the individual taxpayer. Then, the Service must match all of the pertinent data in order to determine that the taxpayer is reporting the correct amount of income. Although this process would also likely be automated, it would require equipment and at least some personnel time currently used for other tasks. And, because of the timing difficulties attendant on the realization of Rewards,¹²⁴ the taxpayer may not realize income until much later. This against raises the question whether the increased equity justifies the increased administrative and compliance cost.¹²⁵ If not, then the question is whether the level of equity is tolerably high or whether enforcing the tax should be formally abandoned.

However, efficiency is also implicated by heaping additional costs on Creditors and employers. Rather than comply with the reporting requirements, a Creditor may discontinue cash Reward programs, preferring instead to spend money on other marketing efforts that may not be as effective.¹²⁶ An employer could require that employees return any Rewards to the employer, as indeed it must require an employee to return an excess reimbursement in an accountable plan.¹²⁷ Or, the employer could avoid the Rewards problem altogether by requiring employees to use in-kind Reward cards or direct bill some expenses and only give the employee per diem for other expenses. However, these methods would likely result in still more untaxed income to employees and diminish any returns from effective enforcement. And, since employees will forego something of value to them – cash – a substantial deadweight loss may

¹²⁴ See *supra*, Part II.B.2.

¹²⁵ RICHARD A. MUSGRAVE & PEGGY B. MUSGRAVE, PUBLIC FINANCE IN THEORY AND PRACTICE 290 (4th ed. 1984).

¹²⁶ Darlin, *supra* note 1 (noting that cash Rewards in particular lead to improved cardholder loyalty to a particular card and thus higher revenue for the Creditor).

¹²⁷ Treas. Reg. § 1.62-2(f) (as amended in 2003).

result. Additionally, fewer enforcement dollars will be directed at other enforcement efforts, thus indirectly encouraging other evasion schemes.

Additionally, Creditor reporting of all cash Rewards implicates privacy concerns because many (if not most) of the Reward payments made likely result from personal purchases, which are not currently considered taxable income. Thus, the Service would obtain information that it has no reasonable need to have.

III. The elephant in the room: tax avoidance and why it will not be a problem

The dangers of tax shelters and tax avoidance are often invoked when Congress, the Treasury, or the Service reviews a tax provision. That is, despite the principle that “[a]ny one may so arrange his affairs that his taxes shall be as low as possible,”¹²⁸ there is always a possibility that a taxpayer will push a clear exception beyond the situation in which it was intended to operate. The inherent danger is in the difficulty to detect such avoidance tactics. The concern with cash business-related Rewards is that an employee and an employer will conspire for an employee to charge an unreasonable amount of company expenses and thus use cash Rewards to increase her wages. Thus, both the employee and employer will avoid employment taxes and the employee will avoid state and federal income tax. The Service will be hard-pressed to detect such avoidance strategies because some of the expenses may be valid and, failing an in-depth audit or constant supervision, the Service may not know that others are not.

However, cash Rewards are not the typical tax avoidance rabbit hole. Rewards are subject to several types of pragmatic limits and, in those extreme cases when they might be used for tax avoidance goals, can be controlled by using variations of existing anti-abuse methods. First, Rewards are generally subject to one or more limits imposed by the sponsoring Creditor,

¹²⁸ *Helvering v. Gregory*, 69 F.2d 809, 810 (2d Cir. 1934), *aff'd*, 293 U.S. 465 (1935) (Judge Learned Hand).

e.g., limits on the number of points that can be earned, value of points that can be redeemed in a calendar year, or a credit limit.¹²⁹ These provisions will necessarily limit the amount of tax revenue that can be earned on a Reward card. Second, businesses have an interest in limiting the amount of business expenses that employees charge on personal credit cards. Third, even if some taxpayers abuse the system, there are adequate basic principles to address abuse without creating undue administrative obstacles for other taxpayers and financial institutions.

A. Not in my back yard: Self-interest limits

Several parties are involved in generating a business-related Reward; two of them have significant countervailing interests. While a Creditor has much to gain from giving cardholders a cash Reward for using a credit card, it still has a bottom line and must account for default rates and other business risks. Additionally, while an employer has certain incentives to allow an employee to use a Reward card for business expenses, excessive use of such cards can create business risks or inefficiencies for the employer. Consequently, cash business-related Rewards are inherently limited by the Creditor's and the employer's self-interest.

1. Limits imposed by a Creditor

Creditors do not have Reward programs to enrich their cardholders; they use Reward programs out of self-interest to maintain brand loyalty.¹³⁰ Ergo, a Creditor only gives a cardholder enough to prompt the latter to charge more and imposes restrictions on a cardholder's ability to earn Rewards,¹³¹ thus necessarily limiting the number of reward points that can be converted into cash in any taxable year. Reward programs generally pay a cash Reward as a percentage of amounts charged in various categories of purchases, the highest earning of which

¹²⁹ For examples, see Appendix 1.

¹³⁰ Jane J. Kim, *Banks Make Reward Plans Less Rewarding*, WALL ST. J., Jan. 19, 2009, available at <http://online.wsj.com/article/SB123180989113175857.html>. Darlin, *supra* note 1.

¹³¹ See *supra* Part II.B.2.; see also *infra* Appendix 1.

are usually earned through selected retailers or on routine expenses such as groceries or gas.¹³² Additionally, the value of rewards that an individual may possibly earn in any one year is limited based on the amount of credit available to the cardholder annually, i.e., the cardholder's credit limit multiplied by twelve.

These limits are not particularly strong. A cardholder can use multiple credit cards in order to increase the potential to earn Rewards. Additionally, some individuals have very high (or no pre-set¹³³) credit limits. And, some cards now pay higher Rewards for restaurant¹³⁴ expenses, a likely expense category for many individuals charging business-related expenses. However, they are real limits that strongly influence the value of cash business-related Rewards.

2. Limits imposed by an employer

Ultimately, employer-imposed limits are the strongest non-tax limit on cash business-related Rewards. Closely held businesses aside, most businesses treat employees at arms length and do not confer value on them in excess of what the employee is worth to the company, if for no other reason than because, *ceteris paribus*, the employer can take a deduction for wages paid under Section 162(a). Additionally, the company can save money by using Rewards earned on a card in the company name to benefit the company or its employees indirectly.¹³⁵ However, allowing an employee to charge business expenses on a personal reward credit card¹³⁶ offers an employer an essentially free way¹³⁷ to provide additional compensation to an employee, a very

¹³² For example, the Citi Professional Cash Card. Citi Professional Cash Card, <https://www.citicards.com/cards/wv/copy.do?screenID=1542> (last visited Apr. 9, 2009).

¹³³ For example, the current line of American Express Premium Rewards cards. See *infra* Appendix 1.

¹³⁴ For example, American Express' Blue Cash card. American Express Blue Cash, <http://www201.americanexpress.com/getthecard/learn-about/BlueCash> (last visited Apr. 9, 2009).

¹³⁵ Terrence Belford, *Using Points to Attract Clients, Reward Staff*, THE STAR, Apr. 9, 2009, available at <http://www.thestar.com/Travel/article/615270>.

¹³⁶ The personal card may be a corporate card with a designated creditor that is taken out in the employee's own name to prevent fraud.

¹³⁷ The employer will still deduct the expense if it is an ordinary and necessary business expense, but will not pay payroll taxes on amounts that are not classified as wages. I.R.C. §§ 162(a), 3111, 3301 (West 2009). This is also a

dangerous situation indeed.¹³⁸ But, since doing so is not always in the employer's best interest, reimbursements are generally made for the convenience of the employer, e.g., to prevent employee fraud,¹³⁹ and not to enrich employees without paying payroll taxes.

The cost to an employer of reimbursing an employee is hidden on multiple levels. First, both the pertinent employee and administrative staff use company time to process reimbursements and maintain records of substantiated expenses.¹⁴⁰ Second, a business may be able to obtain better rates on commonly purchased goods and services if it contracts with and pays suppliers directly. Maintaining accounts with suppliers directly is also preferable for accurate record keeping and provides a payment schedule that is more predictable and probably longer than that obtained by reimbursing employees. Third, reimbursements deprive a business of cash (used to repay employees), thus potentially skewing its debt to equity ratio. Since reasonable borrowing to fund investments is widely held to improve a business' financial efficiency and profit margins,¹⁴¹ purchasing goods and services on a business' short-term credit may improve a business' ability to borrow at favorable rates and allow a business to put cash into more profitable endeavors. Of course, this argument cuts both ways because using an employee's credit to pay company expenses may also maximize the company's return because it

problem with the current Service policy of not taxing in-kind Rewards earned on business purchases because, technically, wages include non-cash compensation. I.R.C. §§ 3121(a), 3301(b) (West 2009). By excluding in-kind Rewards from employee taxable income, the Service is essentially declaring that such Rewards do not constitute compensation.

¹³⁸ See Ray A. Knight and Lee G. Knight, *Substance Over Form: the Cornerstone of Our Tax System or a Lethal Weapon in the IRS's Arsenal?*, 8 AKRON TAX J. 91, 98-99 (1991) (discussing how an employer may be tempted to facilitate an employee's avoidance behavior if the employer does not stand to lose anything).

¹³⁹ As a colleague noted to the author, fraud could include an employee buying a car on the corporate account, and then leaving the country.

¹⁴⁰ A taxpayer must substantiate business travel expenses to completely exclude a corresponding reimbursement from taxable income. Temp. Treas. Reg. § 1.274-5T (as amended in 2003). Similar requirements exist to exclude non-travel expense reimbursements. Treas. Reg. § 1.62-2(e)(3) (as amended in 2003).

¹⁴¹ See RICHARD A. BREALEY ET AL., *PRINCIPLES OF CORPORATE FINANCE* 480-482 (9th ed. 2008) (discussing Miller and Modigliani's Principle 2).

does not immediately pay in cash. However, that is a messy and expensive way to improve a company's debt to equity ratio.

Employer self-interest also extends to its own tax situation, specifically the inherent limits in the definition of an excludable reimbursement. To avoid classification of an expense reimbursement as wages, the payment must be to reimburse an employee for an expense incurred "in connection with the performance by him of services as an employee" that would otherwise be deductible under Part VI of Subchapter B.¹⁴² Pertinent Tax Court and Service rulings addressing the definition of "in connection with the performance [] of services as an employee" indicate that the employee must have incurred the expense in order to perform a specific job for the business and that such expense be incurred on behalf of the business.¹⁴³ Thus, the exclusion clearly extends to purchases necessary to perform specific duties, e.g., an airline ticket required to go to Seattle on an employer's business. However, it may not apply to expenses incurred for the employer that an employee would not normally incur to perform her duties, e.g., purchasing office supplies for the entire office. If such payments are recharacterized as wages, the employer will incur employment tax on such reimbursements, thus increasing its tax burden and the cost of the pertinent item or service.

B. Using what they have: Of loopholes and anti-abuse provisions

Although formally not taxing cash Rewards presents some opportunity for tax avoidance, methods that already exist can be used or easily adjusted to close that loophole should it arise. For example, the substance over form doctrine provides a general method of limiting tax avoidance activities that have no connection to economic reality, e.g., misuse of employer

¹⁴² I.R.C. § 62(a)(2)(A) (West 2009).

¹⁴³ *Biehl v. Comm'r*, 118 T.C. 467, 478-485 (2002) (noting that the language in Regulation 1.62-1(d) indicates that an expense must be "in connection with" the performance of the regular services for which the employee is employed).

reimbursements. Additionally, several other existing methods can be adapted to address taxpayer temptations to use cash business-related Rewards as a tax avoidance method.

Substance over form. As a tool to recharacterize transactions undertaken solely for tax purposes, the substance over form doctrine can act as an effective general measure to limit avoidance activities.¹⁴⁴ The doctrine requires that the parties to a transaction must have a legitimate non-tax business reason for the form of a transaction and the agreement must have non-tax related economic effect, i.e., the parties' economic interests must have changed in ways unrelated to or unmotivated by tax savings.¹⁴⁵ While the doctrine is most useful in a related party context, e.g., regarding reimbursements made to an employee/shareholder of a closely-held corporation, it does apply to transactions made at arms' length.¹⁴⁶ In the context of the cash Rewards debate, if a reimbursement is for a widely recognized employer convenience, then the substance over form doctrine should not apply because there is a legitimate non-tax business reason for the form of the transaction. Conversely, if the reimbursement is not for a recognized employer convenience, e.g., an employee routinely charging large quantities of office supplies to a personal credit card, and the purpose of the charge is to pay the employee more without paying employment taxes,¹⁴⁷ the substance over form doctrine should apply.

De minimis provisions. Some provisions set a limit on the amount of income from a given source that a taxpayer may receive without being taxed. Many of these provisions are apparently designed for administrative efficiency because they account for relatively small

¹⁴⁴ Knight & Knight, *supra* note 138, at 107.

¹⁴⁵ *Newman v. Comm'r*, 894 F.2d 560 (2d Cir. 1990) (delineating factors from the Supreme Court decision in *Frank Lyon Co. v. United States*, 435 U.S. 561 (1978)).

¹⁴⁶ Knight & Knight, *supra* note 138, at 97-98; BITTKER & LOKKEN, *supra* note 43, at ¶ 4.3.3.

¹⁴⁷ See Knight & Knight, *supra* note 138, at 98-99 (discussing that differing tax interests often indicate that there is substance to a transaction, but that the substance may be illusory when one party stands to gain and the other will experience no net loss)

amounts of money, e.g., some of the fringe benefits exceptions and the per diem exception.¹⁴⁸

Although none of the currently applicable *de minimis* provisions apply in this situation, one of these provisions could be extended or adapted to cover cash business-related Rewards. In this way, the bulk of the problem of tracking such Rewards is avoided, but a limitation on tax avoidance possibilities remains.

Information returns. Since it is impossible to apply a *de minimis* provision directly to a cash business-related Reward except through self-reporting, proxy methods can be used in conjunction with information reporting by a creditor or employer. In this way, a *de minimis* provision could be applied as an assumption that reimbursements made to an employee known to use a cash Reward card satisfy Section 62(a)(2)(A) requirements if they do not exceed a defined amount. If that type of reimbursement exceeds a defined level, the employer must report the reimbursements to the Service and the employee on the latter's W-2 form. Or, a *de minimis* provision could be implemented on the Creditor's side with the assumption that cash Rewards in excess of a defined amount may be earned for tax avoidance purposes. In either case, the information return would act as a red flag for the Service to investigate possible tax avoidance activities while minimizing employer and Creditor compliance costs. Additionally, if an employer is required to file an information return for reimbursements in excess of the *de minimis* amount, it could act as a tool to persuade the employer to monitor and control employee charging of business expenses on personal credit cards.

In short, there are multiple reasons why tax avoidance need not become a major issue in the context of excluding cash business-related Rewards from taxable income. Creditors have

¹⁴⁸ I.R.C. §§ 132; 274(d) (West 2009); Treas. Reg. §§ 1.62-2(d)(3)(ii) (as amended in 2003); 1.274-5(g) (as amended in 2003). *See also* discussion on per diem *supra* p. 9.

sound business reasons to avoid awarding extreme amounts of cash Rewards. And, it is not in an employer's best interest to allow an employee to charge business expenses on a personal credit card unless the expenses are related to the employee's duties. Combined with currently applicable anti-avoidance measures and minor adaptations of other measures, excluding cash business-related Rewards from taxable income is a realistic way to make the Service honest without creating opportunities for tax avoidance.

IV. Saying what they do: Proposals for reform

Given that the reality of the Service's current position on taxing cash business-related Rewards is conceptually troublesome, expensive to implement, and opaque, the next step is to find the most satisfactory way to fix it. In light of the aforementioned problems, the primary goal should be to use an accepted exclusion justification to eliminate a troublesome provision while limiting potential tax avoidance opportunities. The first part of this equation smoothes the policy waters and facilitates application of the new policy: by using an accepted exclusion justification, the Service can abandon an untenable position without eliding the fact that a cash business-related Reward is realized income. It also avoids a major amendment to the existing tax structure and facilitates implementation by tying the exclusion to a method already familiar to taxpayers. The second part of the equation satisfies the Service and Congress by avoiding a widening of the tax gap, thus smoothing the political waters.

This goal could be implemented using various possibilities singly or in combination. The basic proposition is that formally exempting cash Rewards to some extent is preferable to

maintaining the current fiction of enforcement. Beyond that, each option has aspects that will protect against tax avoidance schemes should they arise.¹⁴⁹

A. Option 1: Formally exclude all cash business-related Rewards from gross income

The most basic method to fix the cash business-related Reward conundrum is for the Service to formally state that it will not consider such Rewards as taxable income. It could implement this policy in one of two ways, either of which are suitable for an announcement in an administrative notice.¹⁵⁰

First, the Service could state that a cash business-related Reward is part of a reimbursement, but that it will not consider such payments an excess reimbursement under an employer's accountable plan under the Section 62 Regulations. Thus, by default, the Reward will be excluded from gross income. Using this method, the Service's additional administrative cost is minimal because cash Rewards will only ever be income if the reimbursement that gave rise to the Reward does not qualify under Section 62(a)(2)(A).¹⁵¹ And, since the entire reimbursement would then be taxed anyway, the Service has not incurred any administrative cost not otherwise incurred to recharacterize a reimbursement. The employer's additional administrative cost is also nil because it will not track anything other than the reimbursements that it otherwise accounts for. This aspect restricts tax avoidance possibilities, albeit weakly.¹⁵²

Alternatively, the Service could state that it will officially ignore the link between the employer-employee relationship and the cardholder-Creditor relationship, thus rendering a cash

¹⁴⁹ As discussed in Part III, *supra*, the possibility of anti-avoidance is likely slim in any event. Therefore, taking measures to prevent avoidance upon any policy change toward Rewards is premature. Nonetheless, I discuss the anti-avoidance issues associated with each option below and suggest a few measures to address avoidance efforts.

¹⁵⁰ See INTERNAL REVENUE SERV., INTERNAL REVENUE MANUAL § 32.2.2.3.3 (2009), *available at* <http://www.irs.gov/irm/part32/ch02s02.html#d0e12050> (defining a Notice as "a public pronouncement by the Service that may contain guidance that involves substantive interpretations of the Internal Revenue Code or other provisions of the law"). A Service statement regarding either option will require substantive interpretation of Sections 61 and 62.

¹⁵¹ That is to say that the expense is a not deductible expense under one of Sections 161 through 199.

¹⁵² See *supra* Part III.B.

business-related Reward just another rebate on a cardholder's charges. Using this method, neither the Service nor the employer has any need to incur any administrative cost because the Reward is simply a rebate. The employee still has a tax benefit, but the Service can simply decline to recognize it as such, perhaps on grounds of administrative difficulty.¹⁵³ Additionally, there is no existing curb on using this exemption to achieve tax avoidance. If tax avoidance is not of primary concern, as expounded in Part III, then this is not a problem. But, if it is a concern at some level, this option is unsatisfactory.

B. Option 2: Classify cash business-related Rewards as excess reimbursements that may be excluded as a *de minimis*-type benefit

Limiting tax avoidance can be undertaken in many ways, but the simplest way in this case is to require reporting of cash business-related Rewards earned by a taxpayer in excess of a defined "*de minimis*" amount.¹⁵⁴ Underlying the argument that cash business-related Rewards should be excluded is the assumption that most taxpayers will only use a personal cash Reward card for usual business expenses, e.g., normal business trips and occasional purchases of emergency office supplies. The fear that cash business-related Rewards will be used for tax avoidance purposes is based on the misuse of business expense reimbursements. Thus, to preserve the assumption and prevent tax avoidance, a cash business-related Reward could be considered an excess reimbursement subject to nonrecognition as a type of *de minimis* payment. The underlying logic is that use of a personal cash Reward card in excess of a specified *de minimis* amount indicates that the card is being used for expenses not normally incurred in connection with service as an employee and the reimbursement is therefore presumptively wage

¹⁵³ For example, an employee may obtain a tax benefit by not being taxed on the portion of per diem that her employer pays her, but that she does not spend. See discussion *supra* p. 9.

¹⁵⁴ In this section the term "*de minimis*" is not limited exclusively to those fringe benefits under Section 132. However, the reason for excluding cash business-related Rewards is similar – administrative convenience under an assumption of appropriate business practices.

income. That is not to say that amounts in excess of the *de minimis* amount must be taxed. Rather, the Service should treat reports of reimbursements in excess of the *de minimis* amount as a red flag and afford the taxpayer the opportunity to show that all reimbursements were valid.

Applying this assumption requires a judgment about what constitutes a reasonable presumption of excessive use. In the absence of information about the actual cash Rewards received, the judgment could be made by reference to the total reimbursements paid to any one employee, as a percentage of the employer's total reimbursed expenses, or as a percentage of the employer's total expenses. These options mirror the evaluation of the existing *de minimis* fringe benefit rule,¹⁵⁵ but would not necessarily be tied to Section 132. Rather, the Service should either amend the Treasury Regulations¹⁵⁶ under Section 62 or issue a notice¹⁵⁷ interpreting Section 62. In either case, the Service should state that a cash business-related Reward is an excess reimbursement subject to exclusion as a defined *de minimis* benefit because of the administrative burden of accounting for cash business-related Rewards.

Unlike Option 1, Option 2 imposes administrative costs on the employer, but these are likely minimal. For an employer to comply with a *de minimis* provision such as those proposed below, the employer must compare existing records of reimbursements made to an individual employee and compare such amount to Service guidelines. Since the Service must obtain such information for it to be useful, the employer should be required to flag reimbursements in excess of Service guidelines made to employees who have reported to an employer the use of a cash Reward card. The only new information required is a statement filed with a reimbursement request that an employee used a cash Reward card to charge such reimbursable expense. The information about reimbursements could be easily reported on an employee's W-2, thus avoiding

¹⁵⁵ Treas. Reg. § 1.132-6(b) (as amended in 1992).

¹⁵⁶ As permitted by Section 7805(a).

¹⁵⁷ See INTERNAL REVENUE SERV., *supra* note 150.

unnecessary paperwork and complexity. And, by potentially increasing the employer's reporting costs, an employer would have an incentive to prevent unreasonable employee use of cash Reward cards.

1. Employee-level *de minimis*-type evaluations

A *de minimis* provision keyed to reimbursements to an individual employee can be implemented in two ways. First, the *de minimis* provision could be tied to Regulation 1.62-2 and provide that reimbursements to an individual employee who uses a cash Reward card are assumed to satisfy Section 162(a) if such reimbursements are equal to or less than a defined percentage of the employee's income or a specified inflation-adjusted amount. This method is relatively simple and easy to administer, but is somewhat inequitable because some employees within a company or in certain industries are likely to incur large expenses in connection with performing a service as an employee, e.g., for business travel. However, although setting a rigid *de minimis* quantity disadvantages those employees, it does not prevent them from earning an in-kind Reward on additional reimbursed expenses and still justifiably avoiding taxation on a Reward. This fact is also an infirmity because, again, the tax avoidance limitation is reduced to a determination of whether an expense is in connection with services rendered as an employee.

Alternatively, the provision could be tied to Regulation 1.62-2, but assume that such reimbursements satisfy Section 162(a) only if they comply with the *de minimis* fringe benefit rules in Section 132. This method provides greater tax avoidance protection, but will likely be more difficult to implement. The first benefit of this plan is that by tying the reimbursement to the existing *de minimis* fringe benefit exception, the Service avails itself of that category's narrow definition, i.e., that such payments be relatively infrequent and so small that accounting

for them would be “unreasonable or administratively impractical.”¹⁵⁸ Thus, the two measures combined provide greater tax avoidance protection than either one singly. This type of hybrid exclusion may also limit the ability of any one employee to earn cash business-related Rewards, thus improving systemic equity. And, aside from the increased costs discussed above, administrative efficiency is essentially unchanged because employers would account for expenses using the same apparatus currently used for *de minimis* fringes.

However, this second *de minimis* option is not without fault. Although simplicity increases administrative efficiency and transparency, it is unclear whether the frequency with which an employer pays fringe benefits would be evaluated at the employee level or the employer level as required by tying the provision to Section 132.¹⁵⁹ Although an employer could require that an employee report use of a cash Rewards card to charge reimbursable expenses, it is unclear if this would exclude the employer-level option for measuring frequency¹⁶⁰ and shift the exclusion to an employee-level evaluation. And, in any event, evaluating frequency at the employee level would essentially require that a reimbursable expense occur only as often as a *de minimis* fringe would, thus imposing an unrealistic restraint on the exclusion and discouraging accurate reporting and effective monitoring of the use of cash business-related Rewards.

2. Employer-level evaluation of *de minimis*-type benefits

A *de minimis*-type provision (under Section 62 with or without reference to Section 132) that measures reimbursements at the employer level would be less expensive to implement, but

¹⁵⁸ I.R.C. § 132(e) (West 2009).

¹⁵⁹ The *de minimis* fringe rules define frequency with reference to the provision of such fringes to the entire workforce if it would be administratively difficult to measure the frequency that an individual employee obtains such benefits. Treas. Reg. § 1.132-6(b)(2) (as amended in 1992). For example, employer-provided donuts would be tracked at the employer level because it would be administratively difficult to determine the frequency of any one employee’s benefit (eating a donut). STAFF OF JOINT COMM. ON TAXATION, 98TH CONG., GENERAL EXPLANATION OF THE REVENUE PROVISIONS OF THE DEFICIT REDUCTION ACT OF 1984 858–859 (1984).

¹⁶⁰ For example, by comparing an individual’s reimbursed expenses with those of the company generally. Employer-level evaluation of *de minimis* benefits is discussed *supra* in Part IV.B.2.

potentially less equitable. It could be implemented by reference to the ratio of the reimbursements made to employees using a cash Reward card to either the employer's total reimbursed expenses or the employer's total expenses, either generally or in a particular category. The best solution is to tie the ratio to the expenses that give rise to a valid reimbursement, e.g., travel expenses. In this way, the *de minimis* amount will act as a better indicator of expenses beyond those that are valid reimbursements.

To implement this type of provision, the employer should collect information about cash Reward use from employees, but not report any one employee's reimbursements for expenses paid with a cash Reward card to the Service unless the specified ratio is exceeded. This requirement would persuade employers to self-monitor employee use of cash Reward cards to reduce compliance costs. The Service would also incur minimal additional administrative costs.

Although these *de minimis* type provisions will greatly decrease the tax avoidance possibilities involved in formally not taxing cash business-related Rewards, they are far from perfect. A *de minimis* provision, especially one measured at the employer level, will ensure that the Service knows about the extra reimbursements. Therefore, a taxpayer will be compelled to match the cash business-related Rewards received to any excessive reimbursements and somehow show that they should not be considered taxable income, perhaps by showing that the expenses were for legitimate employer expenses.¹⁶¹ There is still a question about misuse of cash business-related Rewards under the *de minimis* threshold. On the one hand, the proposed exclusion is an administrative judgment that those expenses are not worth pursuing, even if they are inappropriate. On the other is a justifiable concern that those expenses are not valid

¹⁶¹ Legitimate expenses could also be presumptively excluded from the tally of expenses measured using the *de minimis* rule, but this does not solve the possibility of employer-employee collusion.

reimbursements and should be taxed. On this point, we return to the use of a *de minimis* exclusion as an anti-avoidance technique.

If further assurance against tax avoidance is necessary, using a *de minimis*-type exclusion as described requires that the Service rely on self-reporting¹⁶² or acquire information from a Creditor. As previously discussed, self-reporting is a relatively ineffective method of tax collection.¹⁶³ While the Service could tax accrued points based on an estimate of the value of the points earned on excessive reimbursed expenses and require taxpayer reporting to adjust the amount,¹⁶⁴ this would not alleviate the taxpayer's or the Service's administrative burden and can lead to very unsatisfactory results because of the timing mismatch between a reimbursable expense and the realization of a cash Reward.¹⁶⁵ Consequently, greater protection against avoidance schemes requires Creditor reporting.

C. Option 3: Additionally require a Creditor to report payment of cash Rewards to an individual taxpayer in excess of a defined amount

Requiring that a Creditor report a taxpayer's redemption of a cash Reward strengthens the Service's ability to prevent tax avoidance, but the cost of doing so may be too high to justify what will likely be small revenue gains. The problem is that, in order to prevent tax avoidance, a Creditor should be required to report all or nearly all cash Reward payments. Otherwise, a taxpayer could simply use multiple cash Reward cards to accomplish the same goal. However, reporting nearly all cash Reward payments will increase the Creditor's compliance and the Service's administrative costs.¹⁶⁶ Taxpayer privacy will also be significantly impacted because

¹⁶² As discussed in Part II.B., even though a cardholder accrues Reward points, the cardholder may never convert those points to recognizable income.

¹⁶³ See *supra* Part II.B.

¹⁶⁴ This method is no different from what the Service does when it assesses tax on any other type of reported income when the taxpayer does not file a return.

¹⁶⁵ See discussion *supra* Part II.B.

¹⁶⁶ Although the Creditor likely already maintains an automated record of all Reward payments, additional processing costs related to issuing an information return will increase the Creditor's burden. The Service must also

many cash Reward payments arise from personal expenses and are not income. Additionally, if a *de minimis* provision is in place, the revenue gains resulting from such information reporting will likely be negligible.

If the Service nonetheless deems information reporting necessary and permissible, there is only one existing option to implement a Creditor information reporting provision: Section 6041. Section 6041 requires anyone who pays to a United States person a fixed or determinable amount of gain, profit, or income in excess of \$600 to report such payment to the Service. However, since not all Reward payments are income, and the payor cannot definitively determine if a payment is income, the Service has ruled that it does not require reporting of Reward payments under Section 6041.¹⁶⁷ Using Section 6041 also requires that an effective *de minimis* amount be used for information reporting: \$600. However, this is not an effective solution to tax avoidance because an employee could simply use multiple cash Reward cards to avoid reporting. In spite of this, Section 6041 presents the best existing opportunity for a safety valve. No other information reporting provision can reasonably be tied to a Reward payment.¹⁶⁸ And, the Service could amend the regulations or issue a notice declaring that for information reporting purposes, cash Rewards will be considered fixed and determinable income. This step is not unprecedented, but is somewhat radical and the political ramifications must be considered.

Of course, Congress or the Service could create a new information reporting provision to address the issue. For example, Section 6050W will soon require that all payment settling entities (which category will include credit card issuers) report payments made in settlement of

process these returns thus increasing its administrative costs as well, albeit marginally because of the use of automated systems. *See generally* Soled, *supra* note 123, at 388-393.

¹⁶⁷ I.R.S. Priv. Ltr. Rul. 93-40-007 (June 29, 1993) (ruling that an airline company is not required to report in-kind Rewards paid to a taxpayer because it is impossible for the airline to know if the payment is income to the recipient).

¹⁶⁸ For example, while the general language of Section 6044 is near ideal, the Section only covers payments made by cooperative organizations as patronage dividends, something that a cash Reward certainly is not.

reportable payment transactions, e.g., transactions in which a consumer uses a credit card to pay for goods or services. A similar provision could be created requiring reporting of cash Reward payments, but seems severely disproportionate to the probability of avoidance.

Thus, despite the fact that information reporting could improve the Service's ability to fight tax avoidance, the costs of such a step are an obstacle, implementation using the current Code is impractical, and implementation using a new provision unrealistic. In light of these issues, adding an information reporting requirement to control tax avoidance schemes using cash Rewards is not a winning proposition.

In summary, the most efficient way to exclude cash business-related Rewards is to either issue a notice stating that they are reimbursements, but not excess reimbursements, or to do the same, but implement a *de minimis*-type provision not tied to Section 132 and evaluated at the employer level. These options will be the least expensive and most administratively efficient to implement because they require minimal additional reporting. Additionally, they provide some tax avoidance protection because the underlying reimbursement must satisfy Section 162 requirements. While both options provide a degree of opportunity for tax avoidance, they present a good balance between efficiency and avoidance and avoid the policy problems behind implementing a Creditor information reporting provision.

V. Conclusion

For nearly one hundred years, the United States has slowly developed its federal income tax system. Over that time, the Code has become more complex as Congress has sought to increase revenue and compliance while treating the citizenry fairly and without creating undue

cost to the government or to taxpayers. Sometimes the legislative efforts are successful and sometimes they are not. Thus, it falls to the Service to fill in the gaps, to determine how to enforce the Code, and sometimes, to determine whether to enforce it in a given situation. Unfortunately, the Service does not always make the right decision and later changes its position. The taxation of cash business-related Rewards is a prime example of when the Service should reconsider its stance and change its policy.

As demonstrated in this paper, the Service's current position regarding the taxation of cash business-related Rewards is untenable. Although the Service says that it will tax such Rewards, its position is unsound. First, there is no reason to treat in-kind and cash Rewards differently. As shown in the literature and by reference to the nature of Reward programs as business contracts, there are adequate ways to value in-kind Rewards. Furthermore, the difficulties in matching in-kind Rewards to business expense reimbursements are the same as those involved in matching cash Rewards to business expense reimbursements. And, the amount of revenue that the government stands to gain from taxation of Rewards is likely very small. Additionally, the Service's position is impossible to enforce effectively or efficiently because, without further action, it must rely on self-reporting. While the taxpayer ultimately bears the burden of reporting income, without third party reporting, the Service will never know who reports cash business-related Rewards and who does not. Consequently, the integrity and horizontal equity of the system are irretrievably impaired. On the other hand, creating information reporting requirements sufficient to address the problem would generate large compliance and administrative costs and infringe upon taxpayer privacy.

The best solution to this tax policy pickle is for the Service to officially say as it does by announcing that it will no longer consider cash business-related Rewards as taxable income.

Rather than create additional complexity in the Code or Regulations, the Service should interpret existing provisions to make this declaration and use existing anti-avoidance techniques to prevent tax avoidance schemes from taking advantage of it. There are several options for doing this, but the best is to issue a notice or similar guidance announcing that cash business-related Rewards are reimbursements subject to Section 62 and all pertinent Regulations. This method has some anti-avoidance features, but would be strengthened by also requiring employers to report reimbursements in excess of a defined *de minimis* amount made to employees who use a personal cash Reward credit card. Using this technique, the Service would gain an anti-avoidance partner because an employer will seek to avoid the reporting requirement by monitoring employee use of cash Reward cards. And the taxpayer, employer, and Service would avoid significantly increased administrative duties. Creditor reporting should not be required. To constitute an effective safeguard, Creditor reporting would impose undue compliance and administrative costs on the Creditor and the Service, respectively. And, it would invade the privacy of many taxpayers using a cash Reward card for personal expenses who have therefore not earned any taxable income at all. In this way, the Service will ameliorate this particular policy problem without creating significant avoidance possibilities or huge costs to private parties. And, it can finally do as it says and say as it does.

Appendix 1: Comparison of Reward Credit Card Terms

Type of Reward	Type of Card	Name of Card	Rewards Rate ¹⁶⁹	Rewards Value ¹⁷⁰	Max Rewards Value ¹⁷¹	Max Credit Limit ¹⁷²
Cash Reward	American Express Cards¹⁷³	Blue Cash ¹⁷⁴	.5-5%	-	None	None listed
	Bank type Cards¹⁷⁵	Discover More ¹⁷⁶	.25-5%	-	None listed	None listed
		Chase Home Improvement ¹⁷⁷	1-3 points	100 to 1	None	None listed
		Capital One No Hassle Cash ¹⁷⁸	1-2%	-	None	None listed
		Citi CashReturns ¹⁷⁹	1%	-	None	None listed
		Citi Professional Cash Card ¹⁸⁰	1-3%	-	\$500 annually	
Hybrid Reward	American Express Cards	AMEX cards using the Membership Rewards Program ¹⁸¹	1-2 points	200 to 1 (cash)	None listed	Varies; some have no pre-set limit
	Bank Type Cards	Chase Freedom ¹⁸²	1-3 points	100 to 1 (cash)	None	None listed
		Capital One No Hassle Points ¹⁸³	1-2 points	200 to 1 (cash), ¹⁸⁴	none	20,000
		Citi Professional Card with Thank You® Network ¹⁸⁵	1-3 points	120 to 1 (cash)	100,000 points per calendar year	none listed

¹⁶⁹ Rewards Rate refers to the rate at which Reward points are earned on every \$1 paid to the Creditor. Some cards have variable rates for purchases at different classes of merchants. Higher rates are usually paid for gas or groceries, but some cards also award a higher rate for restaurant and travel purchases. Rates for Rewards earned at a premium rate on purchases at selected retailers are excluded.

¹⁷⁰ Rewards Value refers to the conversion value of points to US dollars. For cashback cards, the conversion value is the same as the Rewards rate.

¹⁷¹ Max Rewards Value refers to the Creditor limit set on the maximum value amount of points or cashback that may be redeemed or received annually.

¹⁷² Max Credit Limit refers to the highest revolving credit limit that a Creditor will allow a consumer on a given card.

¹⁷³ American Express and Bank-Type Cards are evaluated separately to correlate with data on consumer credit card use provided by the Federal Reserve as discussed in Part III.

¹⁷⁴ <http://www201.americanexpress.com/getthecard/learn-about/BlueCash> (last visited Apr. 9, 2009)

¹⁷⁵ E.g., credit cards with a MasterCard, Visa, or Discover endorsement.

¹⁷⁶ <http://www.discovercard.com/more/faqs.html> (last visited Apr. 9, 2009)

¹⁷⁷ <http://www.chasecreditcards.com/cash-back-cards.asp> (last visited Apr. 9, 2009)

¹⁷⁸ http://www.capitalone.com/creditcards/products/cash/?linkid=WWW_0608_CARD_TGUNS01_CCMAIN_C2_07_T_CCPC (last visited Apr. 9, 2009)

¹⁷⁹ <https://www.citicards.com/cards/wv/copy.do?screenID=1381> (last visited Apr. 9, 2009)

¹⁸⁰ <https://www.citicards.com/cards/wv/copy.do?screenID=1542> (last visited Apr. 9, 2009)

¹⁸¹ www.membershiprewards.com/terms (last visited Apr. 9, 2009)

¹⁸² http://www.chasefreedomnow.com/earn_rewards/ (last visited Apr. 9, 2009)

¹⁸³ http://www.capitalone.com/creditcards/products/points/?linkid=WWW_0608_CARD_TGUNS01_CCPC_H3_03_T_CCPC (last visited Apr. 9, 2009)

¹⁸⁴ 100 to 1 (airline travel), 135 to 1 (merchandise), 140 to 1 (gift cards). *Id.*

¹⁸⁵ https://www.citicards.com/cards/wv/cardDetail.do?screenID=913&origincontentId=CC_TY_REWARDS&CONTENT_TYPE=card_category_detail (last visited Apr. 9, 2009)