section 119, the employer may, in determining whether the requirement of paragraph (a)(1)(i) of this section is satisfied, disregard all costs and revenues attributable to such meals provided to such employees. For purposes of this section, each dining room or cafeteria in which meals are served is treated as a separate eating facility, regardless of whether each such dining room or cafeteria has its own kitchen or other food-preparation area.

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

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

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

[T.D. 8063, 50 FR 52308, Dec. 23, 1985, as amended by T.D. 8256, 54 FR 28600, July 6, 1989]

§1.132–8 Fringe benefit nondiscrimination rules.

(a) *Application of nondiscrimination rules*—(1) *General rule.* A highly compensated employee who receives a no-additional cost service, a qualified employee discount or a meal provided at an employer-operated eating facility for employees shall not be permitted to exclude such benefit from his or her income unless the benefit is available on substantially the same terms to:

(i) All employees of the employer; or

(ii) A group of employees of the employer which is defined under a reasonable classification set up by the employer that does not discriminate in favor of highly compensated employees. See paragraph (f) of this section for the definition of a highly compensated employee.

(2) *Consequences of discrimination*—(i) *In general.* If an employer maintains more than one fringe benefit program, i.e., either different fringe benefits being provided to the same group of employees, or different classifications of employees or the same fringe benefit being provided to two or more classifications of employees, the nondiscrimination requirements of section 132 will generally be applied separately to each such program. Thus, a determination that one fringe benefit program discriminates in favor of highly compensated employees generally will not cause other fringe benefit programs

covering the same highly compensated employees to be treated as discriminatory. If the fringe benefits provided to a highly compensated individual do not satisfy the nondiscrimination rules provided in this section, such individual shall be unable to exclude from gross income any portion of the benefit. For example, if an employer offers a 20 percent discount (which otherwise satisfies the requirements for a qualified employee discount) to all nonhighly compensated employees and a 35 percent discount to all highly compensated employees, the entire value of the 35 percent discount (not just the excess over 20 percent) is includible in the gross income and wages of the highly compensated employees who make purchases at a discount.

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

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

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

(b) *Aggregation of employees*—(1) *Section 132(a) (1) and (2).* For purposes of determining whether the exclusions for no-additional-cost services and qualified employee discounts are available to highly compensated employees, the nondiscrimination rules of this section are applied by aggregating the employees of all related employers (as defined in §1.132–1(c)), except that employees in different lines of business (as defined in §1.132–4) are not to be aggregated. Thus, in general, for purposes of this section, the term ''employees of the employer'' refers to all employees of the employer and any other entity that is a member of a group described in sections 414 (b), (c), (m), or (o) and that performs services within the same line of business as the employer which provides the particular fringe benefit. Employees in different lines of business will be aggregated, however, if the line of business limitation has been relaxed pursuant to paragraphs (b) through (g) of §1.132–4.

(2) *Section 132 (e) (2).* For purposes of determining whether the exclusions for meals provided at employer-operated eating facilities are available to highly compensated, the nondiscrimination rules of this section are applied by aggregating the employees of all related employers (as defined in section §1.132–1(c)) who regularly work at or near the premises on which the eating facility is located, except that employees in different lines of business (as defined in §1.132–4) are not to be aggregated. The

nondiscrimination rules of this section are applied separately to each eating facility. Each dining room or cafeteria in which meals are served is treated as a separate eating facility, regardless of whether each such dining room or cafeteria has its own kitchen or other food-preparation area.

(3) *Classes of employees who may be excluded.* For purposes of applying the nondiscrimination rules of this section to a particular fringe benefit program, there may be excluded from consideration employees who may be excluded from consideration under section 89(h), as enacted by the Tax Reform Act of 1986, Pub. L. 99–514, 100 Stat. 2085 (1986) and amended by the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100–647, 102 Stat. 3342 (1988).

(c) *Availability on substantially the same terms*—(1) *General rule.* The determination of whether a benefit is available on substantially the same terms shall be made upon the basis of the facts and circumstances of each situation. In general, however, if any one of the terms or conditions governing the availability of a particular benefit to one or more employees varies from any one of the terms or conditions governing the availability of a benefit made available to one or more other employees, such benefit shall not be considered to be available on substantially the same terms except to the extent otherwise provided in paragraph (c)(2) of this section. For example, if a department store provides a 20 percent qualified employee discount to all of its employees on all merchandise, the substantially the same terms requirement will be satisfied. Similarly, if the discount provided to all employees is 30 percent on certain merchandise (such as apparel), and 20 percent on all other merchandise, the substantially the same terms requirement will be satisfied. However, if a department store provides a 20 percent qualified employee discount to all employees, but as to the employees in certain departments, the discount is available upon hire, and as to the remaining departments, the discount is only available when an employee has completed a specified term of services, the 20 percent discount is not available on substantially the same terms to all of the employees of the employer. Similarly, if a greater discount is given to employees with more seniority, full-time work status, or a particular job description, such benefit (i.e., the discount) would not be available to all employees eligible for the discount on substantially the same terms, except to the extent otherwise provided in paragraph (c)(2) of this section. These examples also apply to no-additional-cost-services. Thus, if an employer charges non-highly compensated employees for a no-additional-cost service and does not charge highly compensated employees (or charges highly compensated employees a lesser amount), the substantially the same terms requirement will not be satisfied.

(2) *Certain terms relating to priority.* Certain fringe benefits made available to employees are available only in limited quantities that may be insufficient to meet employee demand. This situation may occur either because of employer policy (such as where an employer determines that only a certain number of units of a specific product will be made available to employees each year) or because of the nature of the fringe benefit (such as where an employer provides a no-additional-cost transportation service that is limited to the number of seats available just before departure). Under these circumstances, an employer may find it necessary to establish some method of allocating the limited fringe benefits among the employees eligible to receive the fringe benefits. The employer may establish the priorities described below.

(i) *Priority on a first come, first served, or similar basis.* A benefit shall not fail to be treated as available to a group of employees on substantially the same terms merely because the employer allocates the benefit among such employees on a ''first come, first served'' or lottery basis, provided that the same notice of the terms of availability is given to all employees in the group and the terms under which the benefit is provided to employees within the group are otherwise the same with respect to all employees. For purposes of the preceding sentence, a program that gives priority to employees who

are the first to submit written requests for the benefit will constitute priority on a ''first come, first served'' basis. Similarly, if the employer regularly engages in the practice of allocating benefits on a priority basis to employees demonstrating a critical need, such benefit shall not fail to be treated as available on substantially the same terms to all of the employees with respect to whom such priority status is available as long as the determination is based upon uniform and objective criteria which have been communicated to all employees in the group of eligible employees. An example of a critical need would be priority transportation given to an employee in the event of a medical emergency involving the employee (or a member of the employee's immediate family) or a recent death in the employee's immediate family. Frustrated vacation plans or forfeited deposits would not be treated as giving rise to particularly critical needs.

(ii) *Priority on the basis of seniority.* Solely for purposes of §1.132–8, a benefit shall not fail to be treated as available to a group of employees of the employer on substantially the same terms merely because the employer allocates the benefit among such employees on a seniority basis provided that:

(A) The same notice of the terms of availability is given to all employees in the group; and

(B) The average value of the benefit provided for each nonhighly compensated employee is at least 75% of that provided for each highly compensated employee. For purposes of this test, the average value of the benefit provided for each nonhighly compensated (highly compensated) employee is determined by taking the sum of the fair market values of such benefit provided to all the nonhighly compensated (highly compensated) employees, determined in accordance with §1.61–21, and then dividing that sum by the total number of nonhighly compensated (highly compensated) employees of the employer. For purposes of determining the average value of the benefit provided for each employee, all employee's of the employer are counted, including those who are not eligible to receive the benefit from the employer.

(d) *Testing for discrimination*—(1) *Classification test.* In the event that a benefit described in section 132 (a)(1), (a)(2) or (e)(2) is not available on substantially the same terms to all of the employees of the employer, no exclusion shall be available to a highly compensated employee for such benefit unless the program under which the benefit is provided satisfies the nondiscrimination standards set forth in this section. The nondiscrimination standard of this section will be satisfied only if the benefit is available on substantially the same terms to a group of employees of the employer which is defined under a reasonable classification established by the employer that does not discriminate in favor of highly compensated employees. The determination of whether a particular classification is discriminatory will generally depend upon the facts and circumstances involved, based upon principles similar to those applied for purposes of section 410(b)(2)(A)(i) or, for years commencing prior to January 1, 1988, section 410(b)(1)(B). Thus, in general, except as otherwise provided in this section, if a benefit is available on substantially the same terms to a group of employees which, when compared with all of the other employees of the employer, constitutes a nondiscriminatory classification under section 410(b)(2)(A)(i) (or, if applicable, section 410(b)(1)(B)), it shall be deemed to be nondiscriminatory.

(2) *Classifications that are per se discriminatory.* A classification that, on its face, makes fringe benefits available principally to highly compensated employees is per se discriminatory. In addition, a classification that is based on either an amount or rate of compensation is per se discriminatory if it favors those with the higher amount or rate of compensation. On the other hand, a classification that is based on factors such as seniority, full-time vs. part-time employment, or job description is not per se discriminatory but may be discriminatory as applied to the workforce of a particular employer.

(3) *Former employees.* When determining whether a classification is discriminatory, former employees shall be tested separately from other employees

of the employer. Therefore, a classification is not discriminatory solely because the employer does not make fringe benefits available to any former employee. Whether a classification of former employees discriminates in favor of highly compensated employees will depend upon the particular facts and circumstances.

(4) *Restructuring of benefits.* For purposes of testing whether a particular group of employees would constitute a discriminatory classification for purposes of this section, an employer may restructure its fringe benefit program as described in this paragraph. If a fringe benefit is provided to more than one group of employees, and one or more such groups would constitute a discriminatory classification if considered by itself, then for purposes of this section, the employer may restructure its fringe benefit program so that all or some of the members of such group may be aggregated with another group, provided that each member of the restructured group will have available to him or her the same benefit upon the same terms and conditions. For example, assume that all highly compensated employees of an employer have fewer than five years of service and all nonhighly compensated employees have over five years of service. If the employer provided a five percent discount to employees with under five years of service and a ten percent discount to employees with over five years of service, the discount program available to the highly compensated employees would not satisfy the nondiscriminatory classification test; however, as a result of the rule described in this paragraph (d)(4), the employer could structure the program to consist of a five percent discount for all employees and a five percent additional discount for nonhighly compensated employees.

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

(ii) *Executive group employee.* For purposes of this paragraph (d)(5), an employee is an ''executive group employee'' if the definition of paragraph (f)(1) of this section is satisfied. For purposes of identifying such employees, the phrase ''top one percent of the employees'' is substituted for the phrase ''top ten percent of the employees'' in section 414(q)(4) (relating to the definition of ''top-paid group'').

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

(f) *Highly compensated employee*—(1) *Government and nongovernment employees.* A highly compensated employee of any employer is any employee who, during the year or the preceding year—

(i) Was a 5-percent owner,

(ii) Received compensation from the employer in excess of $75,000,

(iii) Received compensation from the employer in excess of $50,000 and was in the top-paid group of employees for such year, or

(iv) Was at any time an officer and received compensation greater than 150 percent of the amount in effect under section 415(c)(1)(A) for such year.

For purposes of determining whether an employee is a highly compensated

employee, the rules of sections 414 (q), (s), and (t) apply.

(2) *Former employees.* A former employee shall be treated as a highly compensated employee if—

(i) The employee was a highly compensated employee when the employee separated from service, or

(ii) The employee was a highly compensated employee at any time after attaining age 55.

[T.D. 8256, 54 FR 28618, July 6, 1989]

§ 1.132–8T Nondiscrimination rules—1985 through 1988 (temporary).

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

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

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

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

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

(3) *Classes of employees who may be excluded.* Except as otherwise provided in this section, for purposes of applying the nondiscrimination rules of this section to a particular fringe benefit program, there may be excluded from consideration the following classes of employees provided that, with respect to each class (other than the class described in paragraph (b)(3)(iii) of this section), all employees in the class are excluded from participating in the particular fringe benefit program—

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

(ii) All employees who are included in a unit of employees covered by an agreement with the Secretary of Labor