

# Impact

An Overview of Current Legal Events of Concern and Interest

Fall 2003

## A Good Idea Gets Even Better: IRS Ruling Expands Use of Cafeteria Plans

By: Claudia Allen



### **The Historical Advantages of Cafeteria Plans**

Cafeteria Plans—commonly known as Flexible Benefit Plans because employees choose how their benefit dollars are spent—have always provided an exceptional savings opportunity for both employers and employees. Also called Section 125 Plans, Cafeteria Plans permit employees to use pretax income for such benefits as medical, dental, and group term life insurance, daycare expenses, and uninsured medical expenses.

The benefits of such plans to covered employees is easily illustrated. Assume that an orthodontist recommends braces, at a cost of \$2,000, for the children of two similarly situated employees, one who does not participate in a cafeteria plan and one who does. Both are in the 27% federal tax bracket. The non-participant employee must earn roughly \$3,333 in order to pay the \$2,000, after taxes and withholdings. In contrast, the employee who participates in her company's cafeteria plan can have the orthodontist's bill paid with \$2,000 on which she pays no tax. Covered expenses are paid directly by the employer (or are reimbursed to the participant who pays them) as they are incurred. The tax savings to the participant employee amount to \$1,333 (about 40% of the pre-tax amount).

Moreover, because these dollars are not included in the employee's paycheck, they are not subject to the employer's portion of payroll taxes for Social Security, Medicare, and federal unemployment taxes. The employer will recognize a savings in payroll taxes of about 10% — in this case, \$200 for this expense alone.

Cafeteria Plans allow employers to provide funds for employees to use for various benefits of their own choosing. These "benefit dollars" are excluded from employees' pay and are fully deductible by the employer. This can be particularly useful in providing benefits to

employees who are covered under their spouse's health insurance and therefore get no benefit from the company-provided health insurance. Rather than merely providing health insurance coverage to all employees, an employer may instead offer "benefit dollars" equivalent to the cost of coverage under the company's group health insurance plan. Employees who do not need health insurance can use those dollars, plus their own salary reductions, for benefits included in the company's Cafeteria Plan — uninsured medical expenses, dependent care, group term life insurance (up to \$50,000), and even vacation days.

Since Cafeteria Plans provide employees with greater control over their benefit selection, morale is improved; employers with Cafeteria Plans report higher retention rates for employees. Such plans are truly beneficial for both employees and their employers.

### **A Revenue Ruling Makes Cafeteria Plans Even Better**

As beneficial as Cafeteria Plans are, there have been limitations. Based on language in the Internal Revenue Code, the consensus of benefits experts was that for medical expenses to qualify for reimbursement under a Cafeteria Plan, they had to be eligible for treatment as a medical expense deduction for income tax purposes. Since only prescription drugs are deductible, Cafeteria Plan participants could not be reimbursed for the cost of over-the-counter drugs.

The IRS and Treasury Department recently issued a Revenue Ruling concerning the scope of medical reimbursements under Cafeteria Plans. Revenue Ruling 2003-102 interprets the law to allow Cafeteria Plans to reimburse a participant for nonprescription drugs if they are for the personal use of the participant or a dependent and they are used to alleviate or treat personal injuries or sickness. This is particularly good news in light of the recent FDA decision allowing certain medicines,

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such as the allergy drug Claritin, to be sold without a prescription. The Revenue Ruling clarifies that purchases of such items as antacid, allergy medicine, pain relievers, and cold medicine are reimbursable, while dietary supplements such as vitamins that are merely beneficial to general health are not.

### **Implementation of Cafeteria Plans**

To implement a Cafeteria Plan, the requirements of Section 125 of the Internal Revenue Code must be satisfied. This section requires a written plan document and notice of specific items to covered employees. Depending on the language of the existing plan, a Cafeteria Plan may have to be amended to allow reimbursement in accordance with the new Revenue Ruling.

Both the election to participate in the plan and the determination of the amount of money allocated to each benefit must be made at the beginning of each year. These amounts cannot be changed unless there is a change in family status. An employee who chooses to participate in the medical reimbursement portion submits bills or receipts for covered expenses throughout the year. In the case of nonprescription drugs, the receipt must identify the date of purchase, the cost and the name of the item.

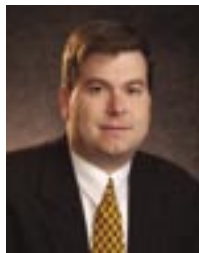
If the expenses are less than the amount allocated to the account, the excess is forfeited at the end of the year. This "use it or lose it" rule has made participants careful about choosing an amount for salary reduction. One additional benefit of the Revenue Ruling is that it makes it easier for employees to use unspent year-end money for non-prescription drugs such as cold or allergy medicine.

*Claudia Allen is a partner in the firm's Tax Department. She regularly practices in the area of employee benefits, including Cafeteria Plans.*

## **When you say full-service law firm, does that include...?**

By: Joseph J. Braun

Although most clients seek our professional assistance for legal advice related to business, real estate matters, tax law, estate planning, or civil litigation, Strauss & Troy strives to be a full service firm in order to meet the legal needs of our clients. This sometimes means that we can offer you the benefit of our experience and knowledge in areas of the law with which you do not normally associate our firm. Whether that means providing assistance in connection with traffic offenses, minor brushes with the criminal court system, or making educated referrals for more serious offenses, we can assist you in nearly any matter involving the law.



It is not uncommon for an existing client to mention such matters to us in passing, only to learn that we may be able to help. Other times, clients contact us after what was thought to be a simple matter turned into a major headache. For example, drivers who receive a speeding ticket or similar traffic citation may decide merely to pay the ticket rather than taking the time to dispute it, even though they believe they were not violating the law. Merely paying the ticket, however, may not be the end of the matter.

Most states have a "points" system under which points are assessed against your driver's license for certain violations. Most moving violations (such as speeding tickets) result in a two-point penalty. The Bureau of Motor Vehicles ("BMV") will suspend the license of drivers who accumulate more than twelve points in any two-year period. Thus, before paying a ticket just to get it over with, it is in your best interest to learn how many points will be assessed against your license and what your point total is. It may be possible to negotiate a lesser offense or to have fewer points assessed against your license.

The area of driving privileges is one in which we are receiving more and more calls. It is possible for your license to be suspended without your receiving notice. In these days of increased mobility, it is not unusual for people to move between driver's license renewals. It is rare for those people to contact the BMV about their change of address. When was the last time you checked to see if the address on your driver's license is current? If not, you may be unaware of important information being sent to you from the BMV. Following up the prior example, if you receive a traffic ticket and points are assessed against your license, notice of the points will be sent to the address on the license. Likewise, notices of suspended or revoked licenses are sent to that address. It is obviously important to update the address on your driver's license any time you move.

The status of your driving privileges is something you should watch carefully. If you fail to renew your driver's license prior to the expiration date and you are stopped by a law enforcement officer, you will be cited for operating a motor vehicle without a valid license. Although this is "just a traffic ticket," it is one that carries high reinstatement fees and other penalties. Similarly, if you receive any type of traffic ticket and do not provide the police officer with proof of insurance at the time you are stopped, the ticket is automatically forwarded to the BMV. The BMV then sends a letter (at the address on your license) requiring you to provide proof of insurance at the time of the stop. Your failure to respond promptly and properly may result in the suspension of your driving privileges and a barrage of fines, costs, and long lines.

There are also serious consequences for neglecting or forgetting to send payment for a traffic ticket or other minor offense. Although people sometimes think a minor matter "fell through the cracks" or that a ticket got lost in the system, such is rarely the case. Instead, the court will actually issue a bench warrant for your arrest. You may not hear from the Court, but the next time you are stopped by a law enforcement officer you may be arrested as a result of the outstanding warrant.

If your child under the age of eighteen receives a traffic citation, the consequences could dramatically affect your daily life in ways you would not expect. Under a law passed by the Ohio legislature last year, the BMV automatically suspends the driving privileges of juveniles who receive more than one moving violation, including speeding, before reaching the age of eighteen. Seeking legal assistance regarding what otherwise appears to be a minor matter may prevent you from spending several months driving your child around town. Subsequent legislation allows juveniles to have limited driving privileges for employment, education, vocational training, or treatment. Taking advantage of this exception could save you hours of driving time while at the same time allowing your teen to learn a valuable lesson.

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# News of the Firm

## Attorneys on the Move



Charles H. Melville

In August, **Charlie Melville** and **Steve Stuhlberg** made a presentation on Agents Without Written Contracts at the MANA (Manufacturer's Agents National Association) Attorney Symposium in Chicago.



Steven F. Stuhlberg



James G. Heldman

**Jim Heldman** served as Co-Chair of the 21st Annual Cincinnati Associates Tribute Dinner, honoring Joseph A. Pichler, Chairman of the Board of the Kroger Company. The dinner was for the benefit of the Hebrew Union College-Jewish Institute of Religion. Mr. Heldman was also recently appointed Co-Chair for the 2004 campaign of the Jewish Federation of Cincinnati, Lawyers' Division.



Gordon H. Hood

**Gordon Hood** and **Paul Theissen** were recently honored as "Senior Counselors" by the Cincinnati Bar Association and Cincinnati Bar Foundation. The organizations recognized attorneys who have practiced law for 50 years or more or who have reached 75 years of age.



Paul J. Theissen



Jeremy A. Hayden

**Jeremy Hayden** spoke on the new tax law changes and planning opportunities at a meeting of the Business & Tax Section of the Northern Kentucky Bar Association and at a continuing education seminar for certified public accountants. Mr. Hayden will address the Southwest Ohio Tax Institute in December.



Michael A. Ruh

**Michael Ruh**, **Joe Braun**, and **Jeremy Hayden** discussed legal issues faced by small business owners at a seminar hosted by the Northern Kentucky University Small Business Development Center.



Joseph J. Braun

## MAD Team Update

Strauss & Troy's Make A Difference ("MAD") Team continues to be very busy, generously sharing time and money with those less fortunate:

- The MAD Team recently made a donation to the "Shop With a Cop" program, enabling five children to purchase new school clothes and supplies.
- The Team just completed a project benefiting the Interparish Ministries, supplying and packaging 200 bags containing personal care items for needy families. Interparish Ministries, located in Newtown, Ohio, serves the community by providing emergency food and clothing to families suffering financial and other hardships. To recognize the MAD Team's work on this project, WCPO-TV Channel 9 News filmed the MAD Team as part of a public service announcement, promoting Community Care Week. The spots will be broadcast this fall and again next spring.
- The MAD Team donated six cases of paper products to the YWCA House of Peace.
- For its annual Holiday Project, the MAD Team will once again adopt the girls at Holly Hill Children's Service in California, Kentucky. The girls will receive gifts of clothing and other "wish list" items during a holiday party given by the Team members on Tuesday, December 16.

## Sponsorships

As a part of our tradition of generously sharing with others, Strauss & Troy is pleased to have sponsored a variety of deserving causes over the past few months. We are proud to have supported the following programs and events as a small part our continuing commitment to the Greater Cincinnati community:

- American Diabetes Association PRO-AM
- Arsenal Challenge Cup
- Arthritis Foundation
- Cedar Village
- Chabad Jewish Center
- Cincinnati Arts Association
- Cincinnati Children's Hospital Medical Center
- Cincinnati Nature Preserve - Back to Nature Fundraiser
- Cystic Fibrosis Foundation
- Healing Connections Association, Inc.
- Inner City Youth Opportunities
- Jewish Community Center
- Jewish National Fund
- Kids Voting
- Kindervelt #55
- Leadership Northern Kentucky
- Legal Aid Society
- New Perceptions, Inc.
- Northern Kentucky Chamber of Commerce
- St. Xavier Lacrosse Parents Association
- The Federal Bar Association - 2004 National Convention Committee
- UC Law Alumni Association
- Volunteer Lawyers for the Poor Foundation
- WCET 48 Action Auction
- Yavneh Day School

# Client Spotlight



**H**i-Tek Manufacturing is a leading supplier of high-precision machining services, conveniently located in Mason, Ohio. It produces precision components for a variety of industries, primarily for high-temperature applications of aircraft engines and power generation turbines. Hi-Tek offers a complete suite of Electronic Discharge Machining (EDM), Laser Cutting & Welding, CNC Machining & Grinding, and Performance Reliability Testing services. This high-precision machining capability has positioned Hi-Tek to be a leading supplier for the major turbine engine manufacturers in the world: GE Aircraft Engines, Pratt & Whitney, Rolls Royce, Siemens Westinghouse, Solar Turbines, and GE Power Systems. Additional markets served include the aerospace, hydraulics, automotive, medical, and electrical industries.

Hi-Tek is a privately owned business founded in 1980. Cletis Jackson, one of the founders, is President and CEO. The business began operations by providing EDM machining services for the aerospace industry and has transformed dramatically since its inception. In 1990, Hi-Tek moved into a new, state-of-the-art manufacturing facility with over 75,000 square feet of space. The original buildings for the Hi-Tek operation are still part of the 95,000 square feet of total capacity and are located directly across the street from the main facility. Included with this facility expansion is a continued evolution of manufacturing services.

There have been many challenges along the way for Hi-Tek. The ups and downs of the aerospace and power generation industries, the ever growing presence of off-shore manufacturing capability, the highly competitive nature of the markets/customers we serve, and continuous downward pricing expectations have all contributed to the ongoing requirements for continuous improvement. To meet the challenges facing a contracting job shop in today's high-precision machining market, Hi-Tek has strategically implemented the following **Mission Statement** over the past ten years to execute its strategy:

- Always put customers' needs first.
- Apply leading-edge technology.
- Invest in modern equipment.
- Empower the employees.
- Train, Educate, and Communicate.
- Continually improve processes.
- Expand markets.
- Have fun doing our jobs

Each of the elements of our mission statement has been key to the consistent growth and success of Hi-Tek. Our customers' needs have continually evolved over the past 20 years, and expanding our capabilities by consistently investing in new equipment and infrastructure has allowed Hi-Tek to keep up with the ever-changing times. What began as a simple EDM shop serving a specific area of the aircraft engine market has evolved into a full-service, make-complete, high-precision machining organization capable of serving a variety of markets.

Examples of Hi-Tek's achievements reflecting its commitment to service and quality include:

- Developed a full service manufacturing engineering organization.
- Invested in Wire EDM, Plunge EDM, 5-Axis Conventional Machining, 5-Axis CBN Grinding, and Laser.
- Developed a state-of-the-art tool and gage facility.
- Developed a state-of-the-art Electrode Stamping facility.
- Developed a state-of-the-art Metallography Laboratory
- Implemented ISO Quality Procedures:
  - ISO9001:2000
  - AS9101:2002
  - NADCAP Process Certifications:
    - NDT, Welding, Laser, and EDM
- Implemented Six Sigma continuous improvement program
  - All Hi-Tek engineering and quality personnel are certified Black Belts or Green Belts.
- Implemented a Manage Enterprise ERP computer system.
- Implemented Unigraphics 3D modeling system.
- Developed a training organization.

Hi-Tek has always met its customers' continuously changing requirements, and will continue these continuous improvement practices. The **Vision Statement** for Hi-Tek Manufacturing is:

***"Be the supplier of choice for the technology market's high-precision machining needs!"***

Hi-Tek Manufacturing is a true example of an organization that implements its Mission and realizes its Vision.

***To learn more about Hi-Tek Manufacturing, visit  
[www.hitekmsg.com](http://www.hitekmsg.com)***

Clients who have been involved in an at-fault automobile accident sometimes contact us about fighting the associated traffic citation because they are fearful that such a citation will result in civil liability if the other driver files suit. While conviction of a traffic offense is not an admission of liability in a subsequent civil trial, you may nevertheless want to retain the services of an attorney. Many insurance companies examine whether their insured was convicted in deciding whether they will dispute liability and pay for any damages.

Much of our experience in these peripheral areas of the law comes from our attorneys' service as City Solicitor, Mayor's Court prosecutor, and in other municipal capacities. Our knowledge of this aspect of the legal system provides us with the ability to assist our clients with situations that arise each day. We are happy to discuss such matters in order to help you save time, expense, and inconvenience. Accordingly, if you are faced with a matter involving traffic offenses or similar matters, do not hesitate to call. Even if it involves issues beyond the scope of our practice, such as most criminal matters, we will be happy to provide you with an educated referral to an attorney who can help.

*Joe Braun, a member of the firm's Litigation Department, has served as a prosecutor in Mayor's Court and has assisted numerous clients in connection with the areas of law discussed above.*

## Only as Good as the Paper They're Written On? Enforcement Of Oral Agreements

By: Steven F. Stuhlberg



Among the phrases for which lawyers are famous for uttering, "Get it in writing!" is high on the list. Partially because of the difficulty in proving the terms of alleged oral agreements, and partially because of legal obstacles to enforcing such agreements, the advice to reduce agreements to writing is sound. Despite the wisdom of our lawyerly advice, we nonetheless recognize the reality that many deals are consummated solely by a firm handshake, without any written record of the parties' promises and obligations. This article will therefore explore the general rules of law regarding the enforcement of oral agreements.

### **Historical Perspective**

Most American law can trace its origins to England, and the law regarding oral contracts is no exception. British law recognized the validity of agreements, both written and oral. The problem with oral contracts, however, was the potential for an unscrupulous person to fabricate a claim of an oral agreement where none existed. In 1676, concerned about the possibility of such abuse, the British Parliament enacted "an Act for the Prevention Of Frauds And Perjuries," declaring certain types of oral contracts unenforceable. This Act, which was designed to prevent fraud, became known as the "Statute of Frauds." It formed the basis for similar laws in the United States. Today,

some form of the original Statute of Frauds finds expression in all 50 states, although the scope and wording vary from state to state.

### **The General Rule: Some Contracts Must be in Writing**

Today's Statute of Frauds requires the following agreements to be in writing in order to be enforceable:

1. Contracts relating to interests in land (including leases);
2. Promises to satisfy debts of another person;
3. Contracts in consideration of marriage; and
4. Contracts that cannot be performed within one year.

The fourth category – contracts that cannot be performed within one year – has the effect of forcing parties who allege oral agreements not to overstate or exaggerate their claims. Knowing that some oral contracts are enforceable, many an unwary party has hurt his own cause by claiming that an alleged oral agreement was to continue for a period greater than one year. Stated simply, an oral contract is unenforceable if one party promises to provide a service or to pay money for a period of more than twelve months. In contrast, the same contract is enforceable if it can conceivably be performed within twelve months, even if it is for an indefinite period of time. Where the agreement is for a specific period of time in excess of one year it will be rendered unenforceable under the Statute of Frauds.

### **Exceptions**

The original basis for the Statute of Frauds was to protect innocent persons from fraudulent claims regarding oral agreements. Following the passage of the statute, however, those who sought to take advantage of others began to use the statute itself to perpetrate fraud. The statute provided a technicality for unscrupulous persons to avoid their contractual commitments to parties who, ignorant of the law, entered into unenforceable oral contracts and performed their obligations in good faith. For example, Jones could agree to do painting for Smith for a period of 18 months in exchange for Smith's agreement to pay Jones upon completion of the work. After 18 months of painting, Smith could refuse to pay, arguing that the agreement is unenforceable since it was for a period of more than one year.

To avoid such an inequitable result, the courts created exceptions to the Statute of Frauds. The "doctrine of partial performance" protects a party who partially or completely performs its obligations under an oral contract. In our example, this doctrine precludes Smith from using the Statute of Frauds to avoid paying Jones for the services he rendered in good faith. In general, the courts have refused to allow the Statute of Frauds to be asserted for fraudulent purposes. Thus, under those circumstances, courts will enforce oral contracts against a defrauding party, in order to protect the innocent.

Courts have also avoided unjust applications of the Statute of Frauds under theories of implied contract, "quasi-contract," or unjust enrichment even though the alleged oral agreement itself falls within the statute. Under these doctrines, a person who sells goods or performs services pursuant to an unenforceable oral contract may be allowed to recover the value of such

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goods or services. The intent of these exceptions to the statute of frauds is to require a party who receives a bargained-for benefit from another party to pay the reasonable value of the products or services provided rather than getting something for nothing.

The common theme of the courts' application of the Statute of Frauds and its various exceptions is an attempt to achieve justice in each individual case. To do so, the courts sometimes interpret the Statute broadly to prevent dubious claims regarding oral contracts, and sometimes interpret the Statute narrowly to allow legitimate oral contract claims.

**Conclusion**

Despite the legislatures' noble attempts to streamline the law regarding oral contracts, the best advice remains to reduce agreements to writing to avoid confusion and controversy. If, however, you enter into a handshake agreement that goes bad, all may not be lost. Navigating

the shoals and reefs of statutes, exceptions, and exceptions to exceptions can be subtle and difficult, but it can be done. Whether you want to enforce an oral agreement or to avail yourself of the protection of the Statute of Frauds in defense of a dubious claim, you should have an experienced navigator at your side – an attorney knowledgeable in this area of law. Just don't be surprised if he tells you, "Next time, get it in writing!"

*Mr. Stuhlberg is a partner in the firm's Litigation Department, regularly practicing in the area of commercial disputes.*

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