BY BRUCE D. ARMON

Money for Nothing

Sign-on bonuses and moving expenses may seem like easy money, but beware of the tax consequences and contractual obligations created by these and other benefits.

LIKE THE ROCKERS in Dire Straits' classic song from the 1980s, many physicians are being courted by prospective employers with what seems to amount to "money for nothing" in the form of wonderful perks for joining a practice. These benefits, which typically take the form of straight cash or cash reimbursements for documented expenses, are not unique to geography, specialty, or even professional experience. While these offers are flattering and can be a significant influence in choosing one practice over another, consider and address the specific tax issues relating to these perks to ensure you get the maximum benefit with minimal repercussions.

Moving and relocation expenses

Unless you finish your residency or fellowship in the community in which you plan to settle for the long term, you will likely be forced to move to a different city and, presumably, transfer your personal belongings.

A prospective employment agreement may provide two distinct options: 1) the employer will give the physician a specified amount of cash to spend on the move, or 2) the employer will reimburse the physician for the "reasonable expenses" associated with the relocation of normal household items for the employee and her dependents in connection with the relocation to the employer's community (a term that is often defined in the employment agreement). The second provision also might include language stating that "reasonable expenses" do not include expenses for relocating large animals (e.g., horses or livestock) or for moving boats and trailers. This would be consistent with the U.S. tax statutes, IRS regulations, and case law.

While this is not intended to be a tax law article, as a general principle, moving and relocation assistance that is paid directly to a prospective employee, without an accounting of the expenses by the employee to the employer, is subject to federal income tax, social security, Medicare, and state income taxes. The employer should withhold these necessary amounts at the time of payment. In contrast, moving and relocation expenses paid to a third party for direct moving expenses are excludable from the employee's income and are not subject to federal income tax, social security, Medicare, or state income tax.

A prospective employer can pay the employee for her moving expenses directly, but there are several key principles that are relevant. Internal Revenue Code Section 82 generally characterizes any amount that is attributable to employment and is received or accrued by an individual as payment for, or re-

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imbursement of, expenses of moving from one residence to another to be "compensation for services." The important exception to this proposition is employer reimbursements of, or payments for, moving expenses which are considered "qualified moving expense reimbursements." These qualified reimbursements are fringe benefits that are excluded from the individual's income.

What makes certain moving expenses qualify for this exception? Four requirements must be met for an employee to receive a federal tax deduction for moving expenses: 1) The taxpayer must pay or incur "moving expenses" and such term is defined, 2) The moving expenses must relate to commencement of work at a new principal place of work, 3) The new principal place of work must be a specified distance (at least 50 miles) farther from the former residence than the former principal place of work, and 4) The taxpayer must work at the general location of the new principal place of work for a specified period following the move. If an employee qualifies for this deduction, this is considered an "above the line" deduction and therefore subtracted from the employee's gross income to determine adjusted gross income.

In addition to the tax consequences, it is very important to address the business implications of a "breach" in the moving and relocation provision. You must understand what the ramifications will be if you do not stay in the defined community as a full-time physician (which also should be defined) for a designated period of time (e.g., twelve months). Must you repay the entire moving relocation amount or is the amount amortized so that for each month you practice full-time in the community a certain percentage is forgiven?

Are there any contractual exceptions to the repayment provision? For instance, will the repayment be forgiven if the employer terminates your agreement "without cause?" What happens if the employee terminates the agreement "with cause?" What happens if the employer does not offer you the opportunity to become a shareholder/member/owner of the medical practice within a certain period of time?

Signing bonus

To attract a desirable candidate, an employer might offer a significant signing bonus. Without exception, a signing bonus is subject to federal income tax withholding, social security, Medicare, and state income tax withholding and these amounts should be deducted at the time of payment.

The agreement should unequivocally state the amount of the signing bonus and when it will be paid. Creative arrangements for when and how these amounts are paid can benefit the physician employee and the employer and minimize the tax consequences. Some employers pay a bonus in one lump sum upon execution of the employment agreement. Other employers pay the signing bonus on the employee's first day of work for the employer. Some employers might split the payments in several increments. If a physician is in his last year of training, the employer might spread a signing bonus throughout the year before he starts working for the employer to help cover the physician's meager training salary and provide a financial cushion before he starts to earn a more robust income.

The agreement will likely include a full repayment provision, with interest, if the physician does not actually start working for the employer, for any reason, on or before a specific date. This is to protect against a prospective employee who literally takes the money and runs.

Similar to the discussion with respect to the moving and relocation expenses, a physician should understand what, if any, repercussions apply if he does not maintain a full-time practice for the employer for a designated period of time. There may also be exceptions to repayment provisions depending on the grounds on which the employee was terminated.

A prospective employer might include a promissory note which a physician signs at the time of execution of the employment agreement. The length and terms included in the promissory note could actually be more onerous than the employment agreement itself.

It is also important to remember that a sign-on bonus might substantially inflate an employee's first-year salary. The base salary in years two and beyond will not include the sign-on bonus. Often times, an employee may be able to negotiate bonus provisions that begin in year two of the employment agreement (sometimes in the first year as well) to help offset the decrease in gross annual income resulting from there being no subsequent signing bonus or retention

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bonus payable to the employee.

Medical education loan repayment

Many new physicians complete their training with debt in excess of $100,000. Some employers offer to pay the medical education loans (principal and interest) during a designated period of time. To continue to receive this benefit, the physician often must maintain a full-time practice of medicine in the physician's given specialty, remain a full-time employee of the employer, maintain staff privileges at certain hospital(s), and not otherwise breach the employment agreement.

Similar to the provisions for signing bonuses, it is important to understand the tax implications of these payments and the repayment obligations, if any, if employment is terminated. For instance, if the employer repays the physician's loan, the total amount paid will be treated as additional compensation for the physician employee. The physician may be able to deduct the interest portion of these payments (as opposed to the principal) on his federal tax return, but the physician will be responsible for any tax obligation for the loan repayments, net of interest. Still, this is certainly preferable to having to pay the entire loan with after-tax dollars.

Additional employment benefits

Prospective employees of a practice might also be eligible to receive several thousand dollars annually in CME expenses, direct payment of board certification examination fees and a preparatory course, generous retirement benefits, or a significant life insurance policy. Depending on the individual's personal circumstances, some benefits (e.g., family health insurance effective on day one of employment) might be more important than asking for an extra week of vacation each year.

Before signing any employment contract that includes moving and relocation provisions, a sign-on bonus, medical school loan repayments, or any other fringe benefit, a physician should speak with his professional advisers—attorney and accountant—to ensure the agreement is properly drafted and protects the physician appropriately from a business, legal, and tax perspective.

Just as it is wise to use caution when accepting perks from industry sales representatives these days, if employment bonuses seem too good to be true, you should tread carefully. There could be harsh backlash from accepting such bait.

With apologies in advance to Mark Knopfler and his band mates, a physician should be careful in negotiating an employment agreement to avoid winding up in "Dire Straits" under the false pretense that she is receiving "Money for Nothing." ■

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