Legal Ethics of Working with Court Reporters
Hosted by San Francisco Legal Professionals Association
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Presenters

- Hon. Charlotte Walter Woolard
- Antonia Pulone, CSR
- Rachel Barkume, RPR, CSR
- Yvonne Fenner, Executive Officer, CRB
- Ana Fatima Costa, Moderator

Topics

1. What becoming a CSR entails; the ethics rules/statutes governing court reporters
2. Does gifting influence impartiality and ethics?
3. What you should never say to a court reporter
4. What are "digital" recorded depositions?
5. The "SoCal stipulation" and how it impacts chain of custody of original transcripts

Handouts

- Outline of Workshop Topics and Citations
- B&P Code §8046 re Professional Conduct of Court Reporting Corporations
- California Code of Regulations § 2475 re Professional Standards of Practice
- ABA Center for Professional Responsibility article on Gifting by Peter Geraghty: *Frequent Flyer Miles, Gifts, Discounts and Rebates from Third Party Providers*
- Hanson Bridgett Memo on Tax Consequences of Receiving Gifts
- *Dangers of the "Usual Stipulation"* by Deposition Reporters Association
- Summary of Relevant Statutes and Rules of Court

TOPIC 1. ***What becoming a CSR entails and the differences between CSRs, digital reporters and videographers.***

—QUESTIONS FROM THE AUDIENCE—

TOPIC 2. ***Does gifting influence impartiality and ethics*?**

Ethical Issues

(a) Law firms may not be aware that the staff is receiving gifts.
(b) Discussion of CSRs' ethical obligations re gifting.

Handouts

- B&P Code §8046 re Professional Conduct of Court Reporting Corporations
- California Code of Regulations, Title 16, Division 24, Article 8, §2475(b)(8)
- ABA Article on Gifting
- Hanson Bridgett Memo on Tax Consequences of Receiving Gifts

—QUESTIONS FROM THE AUDIENCE—

TOPIC 3. ***What You Should Never Say to A Court Reporter***

Ethical Issues
(a) *Outside the earshot of other counsel, attorneys ask court reporters for their opinion about their performance, the witness' veracity, or opposing counsel.*

(b) *An attorney either at a deposition or in court (or sometime thereafter on the phone) asks a reporter for (1) a rough draft, (2) an expedite of the transcript or (3) an excerpt – and tells the CSR not to inform opposing counsel.*

Handouts
- California Code of Regulations, Title 16, Division 24, Article 8, §2475(b)(6)
- California Code of Regulations, Title 16, Division 24, Article 8, §2475(b)(5)

—QUESTIONS FROM THE AUDIENCE—

TOPIC 4. ***What Are Digital Recorded Depositions?***

Ethical Issues:
- Is the witness sworn?
- Confidentiality & accuracy of deposition testimony
- Chain of custody of exhibits and original transcripts
- Are attorneys and staff informed in advance non-CSRs are present?

Handout
- Summary of Relevant Statutes & Rules of Court

—QUESTIONS FROM THE AUDIENCE—

TOPIC 5. ***How the "SoCal stipulation" impacts chain of custody of original transcripts***

Ethical Issues:
- Chain of custody issues; integrity of the record; law firm staff upset when they receive unsealed originals
- Errata not distributed to all parties (discovered at trial during Q&A of witness)
- Original transcripts clearly torn apart and rebound presented to judge at trial.
- Reporters are in a bind, required to keep integrity of original

Handouts
- California Code of Civil Procedure 2025.520
- *Dangers of the "Usual Stipulation"* by Deposition Reporters Association

—QUESTIONS FROM THE AUDIENCE—

Conclusion

California Business and Professions Code Section 8046

Search California Codes

A shorthand reporting corporation shall not do or fail to do any act the doing of which or the failure to do which would constitute unprofessional conduct under any statute, rule or regulation now or hereafter in effect which pertains to shorthand reporters or shorthand reporting. In conducting its practice it shall observe and be bound by such statutes, rules and regulations to the same extent as a person holding a license under this chapter.

(Regulatory Language)

§ 2475. Professional Standards of Practice.

(a) Consistent with any action that may be taken by the Board pursuant to sections 8025 and 8025.1 of the Code, the Board may cite a business that renders professional services, namely shorthand reporting services, within the meaning of Corporations Code section 13401 or cite or discipline any certificate holder, including suspending, revoking, or denying the certification of a certified shorthand reporter, for violation of professional standards of practice.

(b) Every person under the jurisdiction of the Board who holds a license or certificate, or temporary license or certificate, or business that renders professional services, namely shorthand reporting services, within the meaning of Corporations Code section 13401, shall comply with the following professional standards of practice:

(1) Make truthful and accurate public statements when advertising professional qualifications and competence and/or services offered to the public.

(2) Maintain confidentiality of information which is confidential as a result of rule, regulation, statute, court order, or deposition proceedings.

(3) Perform professional services within the scope of one's competence, including promptly notifying the parties present or the presiding officer upon determining that one is not competent to continue an assignment. A licensee may continue to report proceedings after such notification upon stipulation on the record of all parties present or upon order of the presiding officer.

(4) Comply with legal and/or agreed-to delivery dates and/or provide prompt notification of delays.

(5) In addition to the requirements of section 2025.220(a)(5) of the Code of Civil Procedure, promptly notify, when reasonably able to do so, all known parties in attendance at a deposition or civil court proceeding and/or their attorneys of a request for preparation of all or any part of a transcript, including a rough draft, in electronic or paper form. No such notification is necessary when the request is from the court.

(6) Act without bias toward, or prejudice against, any parties and/or their attorneys.

(7) Not enter into, arrange, or participate in a relationship that compromises the impartiality of the certified shorthand reporter, including, but not limited to, a relationship in which compensation for reporting services is based upon the outcome of the proceeding.

(8) Other than the receipt of compensation for reporting services, neither directly or indirectly give nor receive any gift, incentive, reward, or anything of value to or from any person or entity associated with a proceeding being reported. Such persons or entities shall include, but are not limited to, attorneys, an attorney's family members, employees of attorneys or an employee's family members, law firms as single entities, clients, witnesses, insurers, underwriters, or any agents or representatives thereof. Exceptions to the foregoing restriction shall be as follows: (A) giving or receiving items that do not exceed $100 (in the aggregate for any combination of items given and/or received) per calendar year to or from an attorney, an attorney's family members, an employee of an attorney or an employee's family members, a law firm as a single entity, a client, a witness, an insurer, an underwriter, or any agent or representative thereof; or (B) providing services without charge for which the certified shorthand reporter reasonably expects to be reimbursed from the Transcript Reimbursement Fund, sections 8030 et seq. of the Code, or otherwise for an "indigent person" as defined in section 8030.4(f) of the Code.

Note: Authority cited: Section 8007, Business and Professions Code. Reference: Sections 8025, 8025.1 and 8030, Business and Professions Code.

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Frequent flyer miles, gifts, discounts and rebates from third party providers

By Peter Geraghty
Director, ETHICSearch
ABA Center for Professional Responsibility

You have a solo practice that concentrates in family law. A court reporting firm has offered you discount points that can be redeemed at the end of the year for cash refunds and other benefits. Can you keep the benefits?

You also use a credit card for your practice that generates frequent flyer miles for every purchase you make. Do you have an obligation to inform your clients that you are receiving miles when you make purchases on their behalf? Must these miles be allocated to your clients?

ABA Formal Opinion 93-379 *Billing for Professional Fees, Disbursements and Other Expenses* made the following statement about what a lawyer should do when offered a discount from third party providers:

> …In the absence of disclosure to the contrary...if a lawyer receives a discounted rate from a third party provider, it would be improper if she did not pass along the benefit of the discount to her client rather than charge the client the full rate and reserve the profit to herself. Clients quite properly could view these practices as an attempt to create additional undisclosed profit centers when the client had been told he would be billed for disbursements.

The opinion based its reasoning on Model Rules 1.5 *Fees* and 1.4 *Communication*. It cited to subpart (b) of Rule 1.5 as it existed prior to the ABA Ethics 2000 Commission's changes to the rule in 2003 which stated as follows:

> ..When the lawyer has not regularly represented the client, the basis or rate of the fee shall be communicated to the client, preferably in writing, before or within a reasonable time after commencing the representation.

The opinion also cited to paragraph 1 of the Comment to Rule 1.5 that stated:

> In a new client-lawyer relationship ... an understanding as to the fee should be promptly established. It is not necessary to recite all the factors that underlie the basis of the fee, but only those that are directly involved in its computation. It is sufficient, for example, to state that the basic rate is an hourly charge or a fixed amount or an estimated amount, or to identify the factors that may be taken into account in finally fixing the fee. When developments occur during the representation that render an earlier estimate substantially inaccurate, a revised estimate should be provided to the client. A written statement concerning the fee reduces the possibility of misunderstanding. Furnishing the client with a simple memorandum or a copy of the lawyer's customary fee schedule is sufficient if the basis or rate of the fee is set forth.

Note that both the black letter Rule 1.5 and comment were subsequently amended pursuant to the ABA Ethics 2000 Commission's recommendations in 2003, although the substance of the two above excerpts from the rule are substantially the same in the current version of the rule. The E2K did, however, add paragraph 1 to the comment that in part incorporates some of the reasoning of Formal Opinion 93-379. This paragraph states:

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> …Reasonableness of Fee and Expenses
> [1] Paragraph (a) requires that lawyers charge fees that are reasonable under the circumstances. The factors specified in (1) through (8) are not exclusive. Nor will each factor be relevant in each instance. Paragraph (a) also requires that expenses for which the client will be charged must be reasonable. A lawyer may seek reimbursement for the cost of services performed in-house, such as copying, or for other expenses incurred in-house, such as telephone charges, either by charging a reasonable amount to which the client has agreed in advance or by charging an amount that reasonably reflects the cost incurred by the lawyer.

Alaska State Bar Ethics Opinion 95-4 took issue with ABA Formal Opinion 93-379's position that a lawyer could keep the benefits of a discount so long as the lawyer obtained client consent after full disclosure:

> A lawyer who obtains a discounted airline ticket or hotel room should not charge the client the cost for the undiscounted fare or room. The benefits of any discount must be passed on to the client. [FN2]…
> FN2. ABA Formal Opinion 93-379 seems to imply that surcharges can be added on to discounted third party services so long as they are disclosed. Opinion 93- 379 at 9. The Committee declines to adopt such a standard for Alaska. Given the lawyer's overriding

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> obligation to treat clients fairly and reasonably, we can see no justification for not passing the benefits of discounts on to clients. –Alaska Bar Opinion 95-4 (1995).

Other state and local bar opinions have concluded that a client should be the beneficiary of rebates, discounts or gifts given to her lawyer in exchange for engaging the services of a third party on the client's behalf unless the client consents to the lawyer keeping the rebate or discount after full disclosure. See, Alabama (Birmingham Bar Association) Opinion 89-83 (1989):

> A lawyer who receives an "award check"from the court reporter as a result of ordering deposition transcripts that were paid for by a client may only accept the "check,"which may be used to order merchandise through the court reporter from an exclusive merchandise catalog, after obtaining consent of the client after full disclosure. A lawyer may not accept anything of value absent the knowledge and consent of his client after full disclosure. - 901 Law. Man. Prof. Conduct 1058 (1989).

The Alabama opinion cited to DR 1-102(A)(4) of the Alabama Code of Professional Responsibility (The Model Rule corollary is subpart (c) of Rule 8.4 *Misconduct*) that prohibits a lawyer from engaging in conduct involving fraud, deceit and dishonesty for the proposition that a lawyer must be "…scrupulous in dealing honestly and forthrightly with members of the public—and particularly with his own clients." See Also District of Columbia Opinion 185 (1987) and Iowa Opinion 00-2 (2000), a digest of which states:

> A lawyer may sell "probate and other similar bonds"to clients, but the commissions, rebates, discounts, etc., belong to the client and must be disclosed and credited to the client unless the client consents to their distribution to the lawyer…- 1101 Law. Man. Prof. Conduct 3601.

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Frequent flyer miles

How a lawyer should deal with frequent flyer miles present issues that are more complicated than discounts and rebates. Two ethics opinions, from the Massachusetts and Boston bars, have dealt specifically with frequent flyer miles. Both opinions addressed the same hypothetical and came to slightly different conclusions.

Boston Bar Association Opinion 93-4 (1993) stated that in most situations, a lawyer need not disclose that he receives frequent flyer miles to his clients provided that he did not purchase a ticket that was more expensive solely to obtain miles. The opinion also noted that the fact that credit card purchases often result in miles that accrue to the credit card holder is generally known to the public and that therefore no disclosure is necessary. The opinion also noted that it would be difficult to properly credit each client for the miles, since

the lawyer would accumulate the miles over a long period of time and for many different clients, the miles are typically not transferable to anyone other than family members and the amount of miles to be gained for any one transaction is generally nominal in value. The opinion did indicate, however, that if the lawyer were to use his frequent flyer miles to purchase a ticket to travel on behalf of a particular client, he should disclose it to the client so that the client can decide if she wants to reimburse the lawyer for the use of his miles. The opinion also noted that in the event that the lawyer does a great deal of travel on behalf of a particular client, the lawyer should "either use the credit for the benefit of the client, if practical, or discuss the matter with the client."

Massachusetts Bar Opinion 94-1 stated that the lawyer must disclose the fact that he receives the credits if it is more that a "*de minimis*" value. The opinion suggested that in the event that the lawyer makes significant purchases or travels frequently on behalf of a client that would result in a significant amount of miles, the lawyer should disclose this to the client and give the client the option of purchasing the tickets himself. The opinion stated:

> The variety of different situations which might give rise to an economic benefit for the lawyer make it impossible to formulate a hard and fast rule as to when the benefit must be disclosed to the client. Consistent with the provisions of DR 2-106(B) and DR 5-107 (A)(2), the committee's view is that, assuming that there is no additional cost to the client in procuring the service which carries with it a benefit, the requirement of disclosure to the client depends on two factors. First, is the benefit of more than *de minimis* value and one which could be claimed by the client? If so, the client should be advised of the availability of the benefit. For example, in those cases where the air travel in a given case is more than *de minimis* and a client could obtain frequent flyer miles by paying for the travel directly, the lawyer should discuss with the client whether he wishes to pay directly and thereby obtain the benefit for himself. Similarly, where travel for an individual client is of such magnitude that sufficient frequent flyer miles are accumulated to purchase tickets which could be used for additional travel on that client's behalf, the issue should be discussed with the client. Second, is the benefit, while not available to the client, of such significant value as to have a potential to influence the attorney's selection of the service provider? In that case, the existence of the benefit should be disclosed to the client. Disclosure will ensure that the client is able to inform himself as to the reasonableness of the expense. It will also avoid any appearance that the attorney's selection of the service provider was not based solely on the needs of the client, but was influenced by the availability of the benefit.

The opinion also stated that the lawyer must disclose the fact that he is receiving miles if the lawyer begins to make purchasing decisions based upon the credit or benefit he may potentially receive from the third party provider.

On a related topic, See "Can a Lawyer Accept Referral Fees or Commissions from Non-Lawyers?" which appeared in the June 2007 issue of *YourABA*.

Questions involving rebates, discounts and other benefits from third party providers can present thorny ethical issues. As always, check your state or local bar association ethics opinions and rules of professional conduct. Your local bar association may be also be able to help.

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Memorandum

TO: Deposition Reporters Association of California
California Court Reporters Association

FROM: Wendy L. Tauriainen

DATE: February 11, 2011

RE: **Taxation of incentives given by court and deposition reporting firms**

I. Issue Presented.

Deposition and court reporting firms ("Reporting Firms") often provide incentives to legal assistants, attorneys, and others in exchange for booking the Reporting Firm's services. These incentives can have significant value, such as bottles of champagne, video game systems, department store gift cards, and points to be earned toward vacations. This memo will analyze the tax consequences to both Reporting Firms and recipients of such incentives.

II. Tax Consequences to Recipients.

The IRS has recently become more attuned to the issue of treating so-called "gifts" as income. In 2006, the IRS reached a settlement with the Academy of Motion Picture Arts and Sciences involving the value of gift bags distributed to presenters and performers of its Academy Award shows.[1] The IRS stated that the recipients of these gift bags generally must report the fair market value of the bag and its contents as income.[2] While the gift bags are called "gifts," they are not gifts for income tax purposes because they are not given "solely out of affection, respect, or similar impulses for the recipients of the gift bags."[3] Instead, they were provided in exchange for the artist performing or presenting at the Awards show.[4] The settlement between the IRS and the Academy involved the Academy's promise that it would distribute tax information to recipients of the gift bags notifying them of their responsibility to satisfy their tax obligations.[5] The IRS news release regarding the settlement stated that the IRS would continue to focus on compliance by recipients to ensure that the fair market value of the gifts is reported as income.[6] The IRS also stated it would continue to monitor compliance by the providers of gift bags to ensure that Form 1099s are issued to recipients.[7] The Academy has since discontinued

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[1] IRS News Release IR-2006-128.
[2] IRS "Gift Bag Questions and Answers". (2006),http://www.irs.gov/newsroom/article/0,,id=161153,00.html.
[3] *Id*.
[4] http://www.irs.gov/pub/irs-utl/academyawards.pdf.
[5] IRS News Release IR-2006-128.
[6] *Id*.
[7] *Id*.

the practice.[8] The Reporting Firm incentives are very similar to the awards shows gift bags -- they are things of value in exchange for a benefit conferred -- and should be treated similarly to ensure compliance with tax rules.

A. Gift or Payment for Services?

The tax consequences to the recipient depends on whether the incentive is a gift or payment for a service. True gifts are not included in the gross income of the recipient.[9] Whether or not a transfer is a gift is determined by examining the intent of the transferor.[10] The absence of a legal or moral obligation to make the transfer does not make the transfer a gift.[11] An incentive will be treated as a taxable payment for services unless the motive for the transfer is "detached and disinterested generosity" made out of "affection, respect, admiration, charity or like impulses."[12] This is true even if the transferor receives no economic benefit from the transfer.[13]

Incentives given by Reporting Firms in exchange for bookings will not be treated as gifts for tax purposes because there is a clear relationship between the incentive and the performance of a service by the recipient. The *quid pro quo* nature of the transaction removes any possibility that the incentive is given out of disinterested generosity. Further, even if the incentive were characterized as a prize or award, the IRC specifically includes amounts received as prizes and awards in gross income unless the prize or award is transferred directly to a charity.[14]

Given that the incentives provided by Reporting Firms in exchange for business are payments for services rather than gifts, the IRC requires the recipients of those payments to treat the value of the incentives as gross income.[15] This means that recipients must report the value of the incentives they receive as income on their tax returns. Failure to do so could result in the assessment of additional taxes, interest and penalties by the Internal Revenue Service.

B. Can the Income Be Excluded by the Individual Recipient?

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[8] Academy of Motion Picture Arts and Sciences "Academy and IRS Reach Gift Basket Accord" (2006), http://www.irs.gov/pub/irs-utl/academyawards.pdf.
[9] IRC Section 102.
[10] See *Commissioner v. Duberstein*, 363 U.S. 278 (1960) ("Gift" to taxpayer of automobile in recognition of business referrals made to business friend was payment for services despite taxpayer's reluctance to accept gift).
[11] See *Old Colony Trust Co. v. Commissioner*, 279 U.S. 716, 730 (1929) (Payment by employer of employee's income taxes was not a gift despite lack of obligation on employer's part for such payment).
[12] See *Commissioner v. LoBue*, 351 U.S. 243, 246 (1956) (Transfer of stock options to employee not made "with the kind of detached and disinterested generosity which might evidence a 'gift' in the statutory sense."); *Robertson v. United States*, 343 U.S. 711, 714 (1952) (Taxpayer's receipt of prize money for a winning symphonic composition constituted taxable income rather than a gift).
[13] See *Robertson*, 343 U.S. at 714.
[14] IRC Section 74; Treas. Regs. Section 1.74-1(a)(1).
[15] IRC Section 61(a). (Stating gross income means income from whatever source derived, including compensation for services, including fees, commissions, fringe benefits, and similar items.)

1. Incentive Given by Reporting Firm to Individual.

Where the incentive is given directly by the Reporting Firm to an individual attorney or law firm employee, it is unlikely that an individual attorney or law firm employee could exclude the value of the incentives from income. Given the "payment for services" nature of the incentives, the fair market value of the incentives must be reported by these recipients as taxable income.

2. Incentive Given by Reporting Firm to Law Firm.

Similarly, an incentive given by the Reporting Firm to a law firm, which then transfers the incentive to its employee, may also be includible in the employee's taxable income. Gifts by an employer to an employee may not be excluded from being considered income of the employee.[16] However, the IRC does permit the exclusion from income of certain fringe benefits.[17] Thus, whether the law firm must impute income to the employee for the value of any incentives the law firm receives from a Reporting Firm and then passes on to an employee depends on whether the incentive falls under any of the exceptions in the fringe benefit rules.

The only fringe benefit exception which could apply to incentives is the “de minimis fringe.” A de minimis fringe benefit is one which is so small as to make accounting for it unreasonable or administratively impracticable.[18] While de minimis fringe benefits can be deducted as business expenses, they will not be included in the recipient’s gross income.[19] The Treasury Regulations give examples of benefits which do and do not qualify as de minimis. For example, occasional typing of personal letters by a company secretary, occasional cocktail parties, traditional birthday or holiday gifts of property with a low fair market value (but not cash), and flowers provided on account of illness are all de minimis fringe benefits and may be excluded from gross income.[20] By contrast, season tickets to sporting or theater events, membership dues to a country club or gym, or even use of an employer-provided vehicle more than once a month are not de minimis fringe benefits and must be included in income.[21] Further, no cash or cash equivalent (such as a gift certificate or gift card) will qualify as a de minimis fringe benefit.[22]

The value of the incentive provided to the law firm by the Reporting firm, and then passed onto the employee, may or may not be excludible from the employee’s income under the de minimis fringe benefit exception depending on the nature and value of the incentive. A department store gift card will never be excludible because it is a cash equivalent. Items like theater tickets or group meals may be excludible assuming they are given so infrequently both to the employees as a whole and to individual employees as to make

[16] IRC Section 102(c).
[17] IRC Section 132(a).
[18] IRC Section 132(e).
[19] See, *e.g.*, IRS Field Service Advice 200219005 (December 31, 2001).
[20] Treas. Reg. Section 1.132-6(e)(1).
[21] Treas. Reg. Section 1.132-6(e)(2).
[22] Treas. Reg. Section 1.132-6(c).

accounting for them unreasonable or impracticable.[23] Of course, determining how frequently or infrequently these items are distributed, and to whom, requires some degree of administrative tracking, which necessarily hinders an argument that such tracking is unreasonable or impracticable.

If the law firm determines that the fringe benefit is not excludible as a de minimis fringe, it must include the fair market value of the benefit in the employee's wages and withhold the appropriate employment taxes. Failure to do so could subject the law firm to additional taxes, penalties and interest. Further, the employer could be required to issue amended W-2s to affected employees who would then be required to file amended tax returns and possibly pay additional tax, interest and penalties.

3. Similarity of Some Kind of Incentives to Tips.

Alternatively, a law firm may be required to withhold and pay employment taxes based on the kind of the incentive received by the employee because of the similarity of incentives to tips. Similar to tips, incentives are paid by Reporting firms to a law firm's employees and are payments made in the course of the employee's employment. Employees are required to report to their employer cash tips received in amounts over $20 in one month.[24] Employers are then obligated to withhold employment taxes from those amounts. "Cash" tips for these purposes includes "monetary media of exchange."[25] Tips paid in the forms of passes, tickets and other goods or commodities are not included in the employee's wages.[26] Thus, where incentives are paid in the form of things like pre-paid charge cards, or other cash-equivalents, an analogy can be drawn to the reporting and withholding requirements which apply to tips, leaving the employee potentially obligated to report the value of the cash-equivalent incentives to the employer and the employer potentially obligated to withhold employment taxes on those amounts.

4. Tax Liability of Law Firm for Incentives Paid To Their Employees Acting Within the Scope Of Their Employment.

When an incentive is provided to, say, a paralegal or a secretary for booking a deposition at the instruction of a member or another employee of the firm, the question arises: who is the recipient of the incentive, the law firm or the employee? No authority found conclusively determines the answer. Law firms therefore cannot with precision predict how the Internal Revenue Service will treat the matter and, in fact, the issue may turn on the specific facts of each case. As discussed in the Conclusion, law firms may want seriously to weigh the pros and cons of permitting their employees to receive such incentive gifts, for this and all of the other reasons just discussed.

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[23] Treas. Reg. Section 1.132-6(b).
[24] IRC Section 6053(a).
[25] Treas. Reg. § 31.3121(a)(12)-1.
[26] *Id*.

III. Tax Consequences to Reporting Firms.

A. Treatment of Incentives as "Kickbacks."

IRC Section 162(c)(2) disallows business expense deductions for payment of illegal "kickbacks." Kickbacks are defined as payments that could subject the payor to criminal penalty or the loss of license or privilege to engage in a trade or business.[27] Under the California Code of Regulations, the Court Reporters Board of California may suspend, revoke or deny certification of a shorthand reporter for directly or indirectly giving any gift, incentive, reward or anything with a value exceeding $100 in aggregate during a calendar year to any person or entity associated with a proceeding being reported.[28] This rule also applies to Reporting Firms which are corporations and thus under the jurisdiction of the Court Reporters Board of California.[29] While Reporting Firms that qualify as "professional corporations" under California Corporations Code section 13401(b) themselves are not required to be licensed, they are nevertheless in the view of the California Court Reporters Board subject to the statutes and regulations governing licensees.[30] California Business & Professions Code section 8019 makes any violation of the statutes regulating the profession a misdemeanor. Thus, if a Reporting Firm provides an incentive that violates the statutes in the Business & Professions Code, it also commits a misdemeanor, making application of IRC Section 162(c)(2) a possibility.

B. Treatment of Incentives as Gifts.

Reporting Firms may be incorrectly treating the incentives given to specific individuals in exchange for business as "gifts" and deducting some or all of the cost of the incentive as a business expense. The IRC allows a business expense deduction for gifts to an individual which do not exceed $25 in one year.[31] However, to be deductible under this rule, the gift must be an item which is not included in the recipient's gross income. For these purposes, "gifts" include packaged food to be consumed later and tickets to a place for entertainment as long as the transferor does not accompany the recipient.[32] As discussed in Section II above, Tax Consequences to Recipients, these incentives do not qualify as gifts for this purpose and may not be deducted as a business expense under this rule.

The IRC also allows a business expense deduction for incentives given to a recipient other than an employee of the transferor, *as long as the value of the incentive is includible in the*

[27] IRC Section 162(c)(2).
[28] California Code of Regulations Section 2475(a) and (b).
[29] California Business and Professions Code Section 8046; California Code of Regulations Section 2468(a).
[30] On October 26, 2010 the California Court Reporters Board issues an administrative citation and fine against U.S.Legal for violating Business & Professions Code section 8046 and the Board's regulations regulating gifts. http://www.courtreportersboard.ca.gov/lawsregs/cite-fine.pdf ,
[31] IRC Section 274(b)(1). ("No deduction shall be allowed under section 162 or section 212 for any expense for gifts made directly or indirectly to any individual to the extent that such expense, when added to prior expenses of the taxpayer for gifts made to such individual during the same taxable year, exceeds $25.")
[32] Treas. Reg. Section 1.274-2(b)(1)(iii)(b).

recipient's gross income.[33] This section is an exception to the rule disallowing deductions for entertainment expenses. If the incentive is something in the nature of "entertainment," it will only be deductible if specific requirements are met. For these purposes, entertainment includes things like vacations given out in exchange for services performed.[34] However, to be deductible under this rule, the Reporting Firm must issue a Form 1099 to the recipient if the total value of the incentives in one year exceeds $600.[35]

C. Gifts to Law Firms.

As discussed above, IRC Section 274(b) limits the deductibility of gifts to individuals to $25. However, because the section refers to a gift to *an individual*, gifts to law firms in amounts over $25 may be deductible. To be deductible, the Reporting Firm must make the gift with no intention that it will be enjoyed by any particular person and the Reporting Firm must not reasonably be able to ascertain the ultimate recipient of the gift.[36] This means that, to qualify for this exception from the $25 limit, the law firm must be large enough that the Reporting Firm can reasonably claim it did not know who the ultimate recipient would be. Recalling that this deals only with whether the Reporting Firm may deduct the cost of the incentive, not to whether the incentive is income to someone or something else, the likelihood of this argument succeeding when, as here, the incentive is provided in exchange for booking identifiable business is unclear.

The deduction available for gifts to business entities seems to conflict with the Section 102 requirements that "gifts" must be made out of disinterested generosity. The deduction is aimed clearly at transfers where the transferor believes there is some business advantage to be gained, rather than pure generosity. However, the Treasury Regulations regarding these gifts refer to items like theater tickets, books and "several" baseball tickets.[37] It is arguable that gifts to law firms that exceed an as-yet undefined threshold, would no longer qualify as "gifts" and would not be deductible.

An additional complication is that, until recently, only payments made to law firms which operated as partnerships triggered the issuance of a Form 1099; payments made to law firms operating as corporations were exempt from the requirement.[38] However, a recent change in

[33] IRC Section 274(e)(9) (Allows deduction of expenses "includible in the gross income of a recipient . . . who is not an employee of the taxpayer as compensation for services rendered or as a prize or award . . .")
[34] Treas. Reg. Section 1.274-2(c)(5) ("[I]f a manufacturer of products provides a vacation trip for retailers of his products who exceed sales quotas, as a prize or award includible in gross income, the expenditure will be considered directly related to the active conduct of the taxpayer's trade or business."); Treas. Reg. Section 1.274-2(b)(1)(iii)(a) ("[A]ny expenditure which might generally be considered either for a gift or entertainment, or considered either for travel or entertainment, shall be considered an expenditure for entertainment rather than for a gift or travel.")
[35] IRC Section 274(e)(9).
[36] Treas. Reg. Section. 1.274-3(e)(2).
[37] *Id.*
[38] The exemption does not extend to payments for legal services, which must be reported on Form 1099 whether or not the law firm is a partnership or a corporation. IRC Section 6045(f).

the law has eliminated the exemption for payments of more than $600 made to corporations after December 31, 2011.[39] Thus, for incentives over $600 paid in any year after December 31, 2011, Reporting Firms will be required to issue Form 1099s to both corporate law firms and partnerships. Reporting Firms unaware of this change who fail to issue Form 1099s to sole practitioners who practice law as corporations, could be subject to tax penalties.[40] Of course, as mentioned, even if the value of the incentive is less than $600 and the recipient doesn't receive a Form 1099, the recipient must still report the income unless it can be otherwise excluded. [41]

D. Substantiation Requirements.

Business expenses are not deductible unless the taxpayer properly substantiates the expense. This often means detailed recordkeeping about the nature of the expense including the recipient of the gift, the amount, and the purpose. A more thorough discussion of the substantiation rules is beyond the scope of this memo. However, failure to meet the requirements can have serious tax impacts to the Reporting Firm that improperly deducts incentive expenses without proper substantiation.

IV. Other Issues.

Incentive payments may also implicate state income tax rules and ethical issues. National and state court reporting associations and regulatory boards promulgate limits on the value of incentives which can be distributed per recipient on the grounds that such payments may taint the impartiality of the reporter with regard to the parties to the action.[42] Further, incentive payments by large Reporting Firms may violate the unfair competition rules of the California Business and Professions Code. These issues are not addressed in this memorandum, but we would be happy to do additional research if that would be useful.

V. Conclusion.

Incentives distributed to employees of law firms by Reporting Firms in exchange for bookings are not gifts. These incentives clearly represent income and must be reported by somebody, depending upon who the IRS deems the recipient to be. Aside from the ethical and professional prohibitions against these incentives, both recipients and the Reporting Firms risk potentially serious tax consequences, depending on the value of the incentives.

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[39] IRC Section 6041(i); Act Sec. 9006(c) of Patient Protection and Affordable Care Act (PPACA) (P.L. 111-148).

[40] IRC Section 6721. Failure to file penalties have been increased beginning with Form 1099s due after December 31, 2010. Penalties range from $30 per return for returns filed with correct information and no more than 30 days late to a minimum penalty of $250 per return for failing to file due to intentional disregard of the law.

[41] IRC Section 1.

[42] See, *e.g.*, National Court Reporters Association Code of Professional Ethics limiting incentives to $100 per recipient per year (http://ncraonline.org/NCRA/codeofethics/); see also California Code of Regulations Section 2475(b)(8) limiting incentives to $100 per recipient per year.

For attorneys and law firm employees, failing to report the value of the benefits received as income, and paying tax on that income, could result in the imposition of tax and penalties. Where law firms have policies in place prohibiting employees from accepting incentives, serious tax issues may still arise to the extent these policies are not enforced. Similarly, if a law firm receives the incentive and passes it along to an employee, there could be both income and employment tax consequences for the employee and the law firm.

Finally, a Reporting Firm that improperly deducts the cost of the incentives (for example where the incentives are actually kickbacks, the deduction exceeds the allowable amounts, or the Incentives are not properly substantiated) could also result in the imposition of additional tax and penalties on the Reporting Firm.

Overall, incentives provided in exchange for business present significant risks for both the Reporting Firms and the law firms and law firm employees who receive them.

To ensure compliance with requirements imposed by the IRS, we inform you that any tax advice contained in this communication (including any attachments) was not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any transaction or matter addressed herein.

DEPOSITION REPORTERS ASSOCIATION OF CALIFORNIA, INC.

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DANGERS OF THE "USUAL" STIPULATION

It is a mystery how the practice of "May we stipulate to relieve the reporter of his/her duties under the Code" began, but it has become customary, at least in the southern part of the state, often resulting in heated discussion should an attorney want to go "per Code." In fact, it has become so prevalent that many attorneys in Southern California believe -- as reporters have actually heard stated in depositions -- that a stipulation must be done before they can close the record. A favorite line was, "We have to do a stipulation, otherwise the reporter will just keep writing." Perhaps it was said in jest, but no one so much as chuckled, and no one challenged the assertion.

As licensed court reporters and past presidents of Deposition Reporters Association of California, we would like to offer some thoughts on the hazards of the all-too-common practice of stipulating away proper handling of the transcript by the deposition officer.

WHAT IS "PER CODE"?

Unfortunately, it is not uncommon to find that even well-respected attorneys and publications are unclear about how the transcript would actually be handled "per Code." In an article for *L.A. LAWYER* magazine, it was written, "The court reporter then maintains custody of the original transcript and lodges it directly with the court upon request by one or more parties." With all due respect, that is not the procedure per CCP Section 2025.550(a), and, realistically, no reporter would (or should) accept responsibility for maintaining the original transcript, let alone lodging a deposition transcript with the court.

After completion of the deposition transcript, the Code provides the witness 30 days (plus 5 days for mailing of notice) to either appear in person to review the transcript or submit changes/corrections in writing. After 35 days, the original transcript is sent to the noticing attorney, with the deposition officer notifying all parties of changes made by the witness.

WHAT ARE YOU STIPULATING AWAY?

Although some attorneys do include in the stipulation that the reporter is relieved after producing a verbatim transcript, consider that a blanket stipulation includes waiving that requirement, as well as even the basic requirement to certify the transcript upon completion.

Even with that parameter, there are many other unintended ramifications. Realize that by entering into the "usual stipulation," the reporter could argue (s)he does not have to maintain stenographic notes [CCP 2025.510(e)], does not have to notify parties and the witness should a nonparty request a copy of the transcript [2025.570], perhaps even provide a partial or expedite to one side without offering it to opposing counsel [CCP 2025.510(d)]. After all, everyone agreed that the reporter was "relieved of duties under the Code."

Beyond those duties attorneys routinely stipulate away, having the reporter send the original transcript before review by the witness effectively removes the deposition officer from any responsibility regarding corrections, signature, and notification to the parties thereof. Under that scenario, the deposition officer has no ability to certify the witness's execution of the original transcript and cannot ensure that all parties are notified of corrections, if any. Reporters have often discussed the propriety of attorneys themselves assuming duties that, by law, are required to be done by the independent officer of the court.

Perhaps more importantly, when opposing counsel is made responsible for overseeing corrections and signature, any certified transcript provided by the reporter at a later date, either to a party or a nonparty, will not reflect such corrections or changes made by the witness. It then becomes incumbent on the attorney to seek out important information regarding witness review. We ask you to imagine operating on a certified transcript without the benefit of knowing whether the witness reviewed, signed, made corrections.

IS IT PROPER?

The CCP clearly states that there are certain provisions that can be modified by stipulation; for instance, method of recordation of the deposition [CCP 2025.330(b)], and the ability to waive signature or change the time period for review and signing [CCP 2025.520(a) and (b)]. Absent specific language that parties alone have discretion to modify procedures, many would contend that, at a minimum, the court reporter must be a party to the stipulation. Just as the Code provides that a witness must agree to waive signature, it seems reasonable that a reporter must agree to waive his/her duties.

Although court reporters will usually agree to abide by a stipulation entered into between all counsel present at the deposition that calls for the release of the original transcript, our silence should not be interpreted as agreement. If reporters don't interject regarding the stipulation in a deposition, it is because we are in no position to educate attorneys on the law, are ethically bound not to comment on the proceedings in any way, and that we certainly don't want to jeopardize working relationships by being labeled as a "troublemaker" because we refuse to accommodate the wishes of the parties.

So the question becomes whether attorneys have the right to stipulate away a deposition officer's duties, either with or without agreement by the reporter.

WHAT IS THE EFFECT ON COST?

We offer our belief that stipulating away the original to opposing counsel effectively means the noticing attorney is subsidizing his/her opponent's case. Antitrust laws prohibit reporters from discussing specific rates; however, our combined personal experience of working for deposition firms throughout the state seems to bear out that rates for an O&1 are generally significantly higher in Southern California as compared to Northern California. It appears that Southern California rates reflect the fact it is customary for the noticing attorney to provide opposing counsel a "free" transcript (the original). In contrast, lower rates in Northern California for the O&1 reflect an expectation that the Code will be followed and that opposing counsel will order a certified copy of the transcript, which would seem to be a proper allocation of expenses in civil cases.

A byproduct of opposing/witness's counsel receiving essentially a free copy (the original) is that they have no financial stake in the length of the deposition transcript. Some have been known to take that opportunity to ask endless questions, sometimes exceeding that of the noticing attorney, to make his/her record. Perhaps it is a style; perhaps it is a tactic to increase costs for the noticing attorney. In either case, it has at times resulted in argument, with the reporter being asked by the noticing attorney to close the record, only to be reopened on opposing counsel's dime, so to speak.

Per CCP 2025.470, a reporter may not go off the record without agreement of the witness and all parties present unless a party or the witness states an intention to move for a protective order. Reporters cannot rule on whether the examination is "outside the scope." Reporters do not "work" for the noticing attorney, so the admonition that "I'm paying you, and I instruct you to go off the record" will fall on deaf ears. Just another consideration in deciding whether to release a "free" transcript to opposing counsel.

In closing, the law exists to protect the integrity of the deposition transcript. Should the current law need revision, perhaps attorneys and reporters can work together to change it. In the interim, given that procedures in the CCP seem to work well in Northern California, we would advocate that Southern California attorneys rethink the custom and practice of a stipulation at the end of a deposition. In all honesty, some reporters are more than happy to relinquish responsibilities, but we are at a loss to understand the benefit to attorneys in doing so.

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RELEVANT STATUTES AND CALIFORNIA RULES OF COURT, SUMMARIZED

CALIFORNIA CODE OF CIVIL PROCEDURE:

2025.220

States the requirements to notice a deposition. Notice necessary to reserve the right to use at trial a video recording of the testimony of the treating or consulting physician or of an expert witness. Requires the operator of the video equipment to be a person who is authorized to administer an oath and who is not financially interested in the action. Disclosure of the existence of a contract, if any, between the noticing party or a third party financing all or part of the action and whether the party noticing the deposition or a third party financing all or part of the action directed his or her attorney to use a particular officer or entity to provide services for the deposition.

2025.310

A person may take, and any person other than the deponent may attend, a deposition by telephone or other remote electronic means. The court may expressly provide that a nonparty deponent may appear at the deposition by telephone if it finds good cause and no prejudice to any party. A party deponent shall appear at the deposition in person and be in the presence of the deposition officer.

2025.320

The deposition shall be conducted under the supervision of an officer who is authorized to administer an oath and is subject to certain listed requirements. Services and products provided by the deposition officer shall be offered to all parties or their attorneys attending the deposition, and at the same time. The officer shall not provide notations or comments regarding the demeanor of any witness, attorney or party present at the deposition nor collect any personal identifying information about a witness as a service or product to be provided.

2025.330

The deposition officer shall put the deponent under oath or affirmation. Unless the parties agree or the court orders otherwise, the testimony, as well as any stated objections, shall be taken stenographically. If taken stenographically, it shall be by a Certified Shorthand Reporter. If property noticed, the deposition may also be recorded by audio or video technology.

2025.340

Sets forth procedure if a deposition is being recorded by means of audio or video technology. If a video recording of deposition testimony of a treating or consulting physician or of an expert witness is to be used in court, the operator of the recording equipment shall be a person who is authorized to administer an oath unless all parties attending the deposition agree on the record to waive that qualification.

2025.510

Unless the parties agree otherwise, the testimony at a deposition recorded by stenographic means shall be transcribed. The deposition officer shall immediately notify all parties attending a deposition of any request from a party for a deposition transcript to be made available prior to the time it would be available to the other parties. The officer shall, upon request by any party, make that deposition transcript available to all parties at the same time.

2025.520

If the deposition testimony is stenographically recorded, the deposition officer shall send written notice to the deponent and all parties attending the deposition when the original transcript is available for reading, correcting, and signing, unless the deponent and the attending parties agree on the record that the reading, correcting, and signing of the transcript will be waived or that it will take place at some other specific time.

2025.530

If there is no stenographic transcription of the deposition, the deposition officer shall send written notice to the deponent and to all parties attending the deposition that the audio or video recording is available for review, unless the deponent and all of these parties agree on the record to waive the hearing or the viewing of the audio or video recording of the testimony.

2025.540

The deposition officer shall certify on the transcript of the deposition, or in a writing accompanying an audio or video record of deposition testimony, that the deponent was duly sworn and that the transcript or recording is a true record of the testimony given.

2025.550

The certified transcript of a deposition shall not be filed with the court. Instead, the deposition officer shall securely seal that transcript in an envelope or package endorsed with the title of the action and marked with the deponent's name. The sealed and certified transcript shall be transmitted to the attorney for the party who noticed the deposition. The attorney shall store it under conditions that will protect it against loss, destruction, or tampering.

2025.560

An audio or video recording of deposition testimony shall not be filed with the court. Instead, the operator shall retain custody of that recording and shall store it under conditions that will protect it against loss, destruction, or tampering, and preserve the quality of the recording and the integrity of the testimony and images it contains.

2025.570

Unless the court issues an order to the contrary, a copy of the deposition transcript, or audio or video recording if still in possession of the deposition officer, shall be made available by the officer to any person requesting a copy, on payment of a reasonable charge. States mandatory notice requirements by the deposition officer to all parties attending the deposition and the deponent.

2025.620

Lists provisions for the use of a deposition at the trial or any other hearing in the action. Any party may use a deposition for the purpose of contradicting or impeaching the testimony of the deponent as a witness. An adverse party may use for any purpose a deposition of a party to the action. The deposition preserves a deponent's testimony and may be used in court in lieu of the deponent's presence in court under certain listed circumstances. Discusses the use of a video recording of the deposition testimony of a treating or consulting physician or of any expert witness.

CALIFORNIA RULES OF COURT:

3.1010

Any party may take an oral deposition by telephone, videoconference, or other remote electronic means with certain conditions and proper notice. Upon proper notice, any party may appear and participate in an oral deposition by telephone, videoconference or other remote means. A party deponent must appear at his or her deposition in person and be in the presence of the deposition officer. A nonparty deponent may appear at his or her deposition by telephone, videoconference, or other remote electronic means with court approval upon a finding of good cause and no prejudice to any party. The deponent must be sworn in the presence of the deposition officer or by any other means stipulated to by the parties or ordered by the court.

2.1040

Except as otherwise provided or by court order: Before a party may present or offer into evidence an electronic sound record or sound-and-video recording of deposition or other prior testimony, the party must lodge a transcript of the deposition or prior testimony with the court. Before a party may present or offer into evidence any electronic sound or sound-and-video recording, the party must provide to the court and to opposing parties a transcript of the electronic recording and provide opposing parties with a duplicate of the electronic recording.

CALIFORNIA EVIDENCE CODE:

1235

Evidence of a statement made by a witness is not made inadmissible by the hearsay rule if the statement is inconsistent with his testimony at the hearing and is offered in compliance with section 770.

770 Unless the interests of justice otherwise require, extrinsic evidence of a statement made by a witness that is inconsistent with any part of his testimony at the hearing shall be excluded unless…

(a) The witness was so examined while testifying as to give him the opportunity to explain or deny the statement; or

(b) The witness has not been excused from giving further testimony in the action.

1236

Evidence of a statement previously made by a witness is not made inadmissible by the hearsay rule if the statement is consistent with his testimony at the hearing and is offered in compliance with section 791.

791 Evidence of a statement previously made by a witness that is consistent with his testimony at the hearing is inadmissible to support his credibility unless it is offered after:

(a) Evidence of a statement made by him that is inconsistent with any part of his testimony at the hearing has been admitted or the purpose of attacking his credibility, and the statement was made before the alleged inconsistent statement; or

(b) An express or implied charge has been made that his testimony at the hearing is recently fabricated or influenced by bias or improper motive, and the statement was made before the bias, motive for fabrication, or other improper motive is alleged to have arisen.