

PUBLICATION

Substantiation Requirements for Employer-Provided Cell Phones

October 17, 2011

The Small Business Jobs Act of 2010 was signed into law by the President on September 27, 2010. Section 2043 of that Act removed cell phones from the definition of “listed property” for taxable years beginning after December 31, 2009. This change relieved employers of many of the burdensome recordkeeping requirements imposed by the IRS in claiming business deductions.

Recent IRS Notice

On September 14, 2011, the IRS provided guidance interpreting Section 2043 in Notice 2011-72 (Notice) and the accompanying Field Exam Memorandum (Memorandum), Control Number: SBSE-04-0911-083. As a result of these relaxed substantiation requirements, employers may consider reviewing current cell phone policies to ensure they are claiming the maximum benefit.

A. Examples of Qualifying/Non-Qualifying Purposes. In general, the Notice eliminates the recordkeeping and substantiation requirements for an employee's use of an employer-provided cell phone so long as the employer provides the cell phone primarily for non-compensatory business reasons. The following three examples are provided in the Notice to illustrate qualifying non-compensatory business purposes:

1. The employer needs to contact the employee at all times for work related emergencies;
2. The employer's requirement that the employee be available to speak with clients at times when the employee is away from the office; and
3. The employee's need to speak with clients located in other times zones at times outside of the employee's normal work day.

The Notice also provides the following three examples which do not qualify as non-compensatory business purposes:

1. To promote the morale or good will of an employee;
2. To attract a prospective employee; or
3. To furnish additional compensation to an employee.

If the cell phone is provided for a qualifying purpose, the employee's use of the cell phone for business purposes will automatically be treated as a non-taxable, working condition fringe benefit and the value of any personal use by the employee will be excluded from gross income as a de minimis fringe benefit. The employer also benefits in that no employment tax withholding should be required on the employee's use, whether business or personal.

B. Cash Reimbursements Not Addressed. The Notice does not address the tax treatment for cash reimbursement from an employer to an employee for that employee's use of his or her personal cell phone for

business purposes. Although not authoritative, the Memorandum accompanying the Notice does provide some guidance in instructing IRS agents to analyze such reimbursements in a manner similar to that set forth in the Notice. As a result, so long as the employer's reimbursement is made for non-compensatory business purposes, it is arguable that such reimbursement should not be treated as taxable income to the employee. Employers should note, however, that the Memorandum conditions such treatment on the employee maintaining the type of cell phone coverage that is reasonably related to the needs of the employer's business, and also that the reimbursement be limited to the actual cost of the cell phone service.

Employers may wish to revise current cell phone reimbursement policies to more closely align with the Notice and Memorandum. The Notice does not apply to any other fringe benefit.

Summary

The heightened substantiation rules under the Internal Revenue Code for certain listed property creates headaches for many employers who provide property or services to employees as working condition fringe benefits. The removal of cell phones from the definition of listed property should reduce this burden somewhat on many employers, assuming that the cell phone is provided for non-compensatory business purposes. Should you wish to discuss your particular business policies in view of the non-compensatory purposes recognized by the Notice, or wish to otherwise discuss any other aspect of this Notice, please contact any of the attorneys within the Firm's Tax Department.