

Issued: September 21, 2011

## Email Alert:

# Great News from the IRS on Cell Phone Taxation

The IRS made a significant announcement regarding cell phones on September 14. In Notice 2011-72 (IR-2011-93), the IRS stated that an employer-provided cell phone will not be taxable to an employee when it is provided primarily for substantial business reasons (other than as an employee benefit). This eliminates any need to track business/ministry calls versus personal calls.

### The notice made two important points:

- The cell phone must be provided primarily for “substantial business reasons.” The notice included three examples of substantial business reasons: (1) the need to contact the employee at all times for emergencies; (2) the employee’s need to speak to customers when away from the office; and (3) the employee’s need to speak to customers in other time zones outside of the employee’s normal business hours.
- The reasons must be non-compensatory. Providing a cell phone just for the benefit for the employee will not qualify. The notice included three examples of reasons that do not qualify: (1) promoting the morale or good will of an employee; (2) attracting a prospective employee; or (3) furnishing additional compensation.

**Complete exclusion from taxation, without any allocation between business and personal use, only certainly applies when the employer provides the cell phone.** The exclusion for personal use in the notice is based on personal use as a de minimis non-cash benefit, and does not directly apply when the employer pays cash.

### Cell Phone Allowances and Reimbursements

If your organization reimburses or provides allowances for employee-provided cell phones, the notice and concurrent Memorandum for All Field Examination Operations (9/14/11, Control # SBSE-04-0911-083) provide the following guidance.

In the memorandum, the IRS authorizes IRS auditors to apply similar non-taxable treatment to reimbursements of employee’s personal cell phone expenses meeting three requirements:

1. The employer must require the employee to use the employee’s personal cell phone in connection with the employer’s business;
2. The employee must maintain the type of cell phone coverage reasonably related to the needs of the employer’s business; and
3. The reimbursement must be reasonably calculated and not exceed expenses the employee actually incurs in maintaining the cell phone.

## About CapinCrouse LLP

With more than 700 not-for-profit organizations and 1,500 tax clients, CapinCrouse is the country’s leading accounting and advisory firm primarily serving the Christian not-for-profit community.

Since 1972, CapinCrouse has been serving not-for-profit entities including megachurches, institutions of higher education and secondary schools, and international missions agencies by providing a full range of audit, review, tax, and advisory services.

CapinCrouse is dedicated to helping our clients operate with financial integrity so that they can dedicate themselves to fulfilling their mission.

## Example Provided

The memorandum provides this example of a non-taxable reimbursement:

An employer has a substantial noncompensatory business reason for requiring the employee to maintain a personal cell phone to facilitate communication with the employer's clients during hours outside the employee's normal tour of duty in the office and reimbursing the employee for the use of the phone. The employee uses the cell phone for both business purposes and personal purposes and the employee's basic coverage plan charges a flat-rate per month for a certain number of minutes for domestic calls. The employer reimburses the employee for the monthly basic plan expense to enable the employee to maintain contact with business clients throughout the United States after hours.

**IRS auditors are cautioned to look for situations where the plan being reimbursed exceeds the needs of the employer, or the reimbursement is unrelated to the cost of the plan.**

## Observations

Some aspects to note and consider:

- **Employers must be prepared to justify why a particular employee was provided a cell phone or had the expense reimbursed.** A blanket policy that every employee gets a cell phone might be valid, but you would need to show that there was a noncompensatory, substantial business reason for every employee. More narrowly defined groups of employees - such as all employees who travel, or all those on emergency call - would be easier to justify.
- **The IRS's recognition that emergency availability is a substantial business reason helps in many situations where previously much of the value of the phone previously would have been taxed.** For instance, 95% of an employee's usage might be personal, because the need for the employee's emergency response only arises occasionally. Now, 100% of the value would be nontaxable.
- **Employees who travel, even if only occasionally, will also benefit.** While much of their local use might be personal, the need to keep in touch with customers when away from the office is explicitly recognized.
- The new simplicity in taxing employer-provided cell phones may encourage employers currently using reimbursements or allowances for cell phone costs to investigate options for employer-provided cell phones.
- Employers who provide flat allowances for personal cell phones without knowing the cost of the employee's plan or whether it is reasonably related to the employer's business will still need to report it as taxable.

As always, please contact our tax staff for guidance tailored to your specific situation. We are here to help!

Tax Department  
**317.885.2620**

Atlanta  
**678.518.5301**

Chicago  
**630.682.9797**

Colorado Springs  
**719.528.6225**

Dallas  
**817.328.6510**

Denver  
**720.283.7326**

Indianapolis  
**317.885.2620**

Los Angeles  
**714.671.9300**

New York City  
**212.653.0681**

Orlando  
**407.883.4671**

San Diego  
**858.638.7220**