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Part III - Administrative, Procedural, and Miscellaneous

Tax Treatment of Employer-Provided Cell Phones

Notice 2011-72

PURPOSE

This notice provides guidance on the tax treatment of cellular telephones or other similar telecommunications equipment (hereinafter collectively “cell phones”) that employers provide to their employees primarily for noncompensatory business purposes.

BACKGROUND

Section 2043 of the Small Business Jobs Act of 2010, Pub.L.No. 111-240, (the Act) removed cell phones from the definition of listed property for taxable years beginning after December 31, 2009. The Act did not otherwise alter the requirement that an employer-provided cell phone is a fringe benefit, the value of which must be included in the employee’s gross income, unless an exclusion applies, or the potential treatment of an employer-provided cell phone as an excludible fringe benefit. Since enactment of the Act, the IRS has received questions about the proper tax treatment of employer-provided cell phones. Accordingly, this notice addresses the treatment of employer-provided cell phones as an excludible fringe benefit.

Gross Income

Section 61 of the Internal Revenue Code (Code) defines gross income as all income, from whatever source derived. Section 61(a)(1) provides that gross income includes compensation for services, including fees, commissions, fringe benefits, and similar items. A fringe benefit provided by an employer to an employee is presumed to be income to the employee unless it is specifically excluded from gross income by another section of the Code. See Income Tax Regulations § 1.61-21(a).

Working Condition Fringe Benefits

Section 132(a)(3) of the Code provides that gross income does not include any fringe benefit which qualifies as a working condition fringe. Section 132(d) provides that “working condition fringe” means any property or services provided to an employee of the employer to the extent that, if the employee paid for such property or services, such payment would be allowable as a deduction under §§ 162 or 167.

Section 1.132-5(a)(1)(ii) of the Income Tax Regulations (Regulations) provides that if, under section 274 or any other section, certain substantiation requirements must be met in order for a deduction under §§ 162 or 167 to be allowable, then those substantiation requirements apply when determining whether a property or service is excludable as a working condition fringe. See also Regulations § 1.132-5(c)(1).

Section 162(a) of the Code provides that a deduction is allowed for all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business. However, section 262(a) of the Code provides that, except as otherwise expressly provided, no deduction shall be allowed for personal, living, or family expenses.

In the case of certain listed property, as defined in section 280F(d)(4) of the Code, special heightened substantiation rules apply. Section 274(d)(4) of the Code provides that no deduction shall be allowed with respect to any listed property (as defined in § 280F(d)(4)), unless the taxpayer substantiates by adequate records or by sufficient evidence corroborating the taxpayer's own statement (A) the amount of such expense or other item, (B) the use of the property, (C) the business purpose of the expense or other item, and (D) the business relationship to the taxpayer of persons using the property.

The Act removed cell phones from the definition of listed property for taxable years beginning after December 31, 2009. Because the Act removed cell phones from the definition of listed property, the heightened substantiation requirements that apply to listed property no longer apply to cell phones for taxable years beginning after December 31, 2009.

De Minimis Fringe Benefits

Section 132(a)(4) of the Code provides that gross income does not include any fringe benefit which qualifies as a de minimis fringe. Section 132(e) defines a de minimis fringe as any property or service the value of which is (after taking into account the frequency with which similar fringes are provided by the employer to the employer's employees) so small as to make accounting for it unreasonable or administratively impracticable. Except as specifically provided (i.e., occasional meal money or local transportation fare and reimbursements for public transit passes), a cash fringe benefit is not excludable as a de minimis fringe. See Regulations §1.132-6(c).

Guidance Regarding Employer-Provided Cell Phones

Many employers provide their employees with cell phones primarily for noncompensatory business reasons. The value of the business use of an employer-provided cell phone is excludable from an employee's income as a working condition fringe to the extent that, if the employee paid for the use of the cell phone themselves, such payment would be allowable as a deduction under section 162 for the employee.

An employer will be considered to have provided an employee with a cell phone primarily for noncompensatory business purposes if there are substantial reasons relating to the employer's business, other than providing compensation to the employee, for providing the employee with a cell phone. For example, the employer's need to contact the employee at all times for work-related emergencies, the employer's requirement that the employee be available to speak with clients at times when the employee is away from the office, and the employee's need to speak with clients located in other time zones at times outside of the employee's normal work day are possible substantial noncompensatory business reasons. A cell phone provided to promote the morale or good will of an employee, to attract a prospective employee or as a means of furnishing additional compensation to an employee is not provided primarily for noncompensatory business purposes.

This notice provides that, when an employer provides an employee with a cell phone primarily for noncompensatory business reasons, the IRS will treat the employee's use of the cell phone for reasons related to the employer's trade or business as a working condition fringe benefit, the value of which is excludable from the

employee's income and, solely for purposes of determining whether the working condition fringe benefit provision in section 132(d) applies, the substantiation requirements that the employee would have to meet in order for a deduction under §162 to be allowable are deemed to be satisfied. In addition, the IRS will treat the value of any personal use of a cell phone provided by the employer primarily for noncompensatory business purposes as excludable from the employee's income as a de minimis fringe benefit. The rules of this notice apply to any use of an employer-provided cell phone occurring after December 31, 2009. The application of the working condition and de minimis fringe benefit exclusions under this notice apply solely to employer-provided cell phones and should not be interpreted as applying to other fringe benefits.

EFFECTIVE DATE

This notice is effective for all taxable years after December 31, 2009.

CONTACT INFORMATION

The principal author of this notice is Joseph Perera of the Office of Associate Chief Counsel (Tax Exempt & Government Entities). For further information regarding this notice contact Joseph Perera on (202) 622-6040 (not a toll-free call).