

## ***TAXATION OF PERSONAL USE OF CELL PHONES***

### **STATUS**

Issue resolved. The Small Business Jobs Act, Public Law 111-240, removes cell phones and similar devices from the list of items that require taxpayer business purpose substantiation so their cost can be deducted or depreciated like other business property, without onerous recordkeeping requirements.

### **ISSUE**

Under the Internal Revenue Code (Code), there are some quirky rules for determining what is a fringe benefit to an employee and for determining what is included in a subset of fringe benefits known as “working condition fringe benefits.” While we suspect most employers and employees would not consider an employer-provided cell phone to be a “fringe benefit,” it is.

If an employer provides a cell phone to an employee (including the owner), and the employer acquires and pays the costs of using the cell phone, the assumption under the Code is that the employee receives a fringe benefit. To the extent that the employee uses the employer’s cell phone for business purposes, the fair market value of such usage qualifies as a working condition fringe benefit excludable from the employee’s gross income. As such, the cell phone expense is a deductible business expense for the employer, PROVIDED that the substantiation requirements of the Code are met. (The substantiation requirements are requirements that most small business owners are familiar with, since these are the same ones that apply for documenting business use of cars and computers.)

To the extent the employee uses the employer’s cell phone for personal purposes (i.e., only a portion can be substantiated as business use), the fair market value of such personal use is includable in the employee’s gross income.

What happens if the employee fails to substantiate the business use? The ramification for the employee is income tax liability on the imputed income as well as FICA tax (7.15 percent). The ramification for the business is the additional FICA tax (7.15 percent) on the amount of imputed income. In addition, the business will lose a portion (or all, if no substantiation) of the deduction for the cost of the purchase of the telephone (probably a Section 179 direct expensing deduction for the full amount, but a depreciation deduction over ten years otherwise) and lose a portion (or all, if no substantiation) of the deduction for the on-going service charges. Since some or all of those expenses will now be income to the employee, those expenses should still be deductible as wages, and the business exposure should be limited to the employer’s FICA tax on imputed income equivalent of those costs. For the self-employed, it basically means paying for it with after tax dollars.

The section of the Code that defines the property for which substantiation is required includes the phrase: “any cellular telephone (or other similar telecommunications equipment).” So yes, your Blackberry is covered too.