BusinessManagement DAILY

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The pandemic didn't change cell phone reimbursements

Whether you have to tax reimbursements of employees' business use of their personal cell phones has been kicking around for as long as there have been cell phones. Yet, despite the IRS issuing guidance way back in 2011 saying the reimbursements aren't taxable, the issue still seems to keep cropping up. The pandemic has muddied the waters even more.

Here's the skinny on employer reimbursements.

What the IRS said in 2011

The IRS issued two pieces of guidance back in 2011.

In Notice 2011-72, the IRS concluded that employers with non-compensatory business reasons for providing phones and similar equipment (for this purpose similar equipment does not include computers) to employees may do so on a tax-free basis.

A non-compensatory business reason includes such circumstances as when:

- Employers must contact employees at all times for work-related emergencies.
- Employees must be available to speak with clients at times when employees are away from the office.
- Employees need to speak with clients who are located in other time zones at times outside of employees' normal working hours.

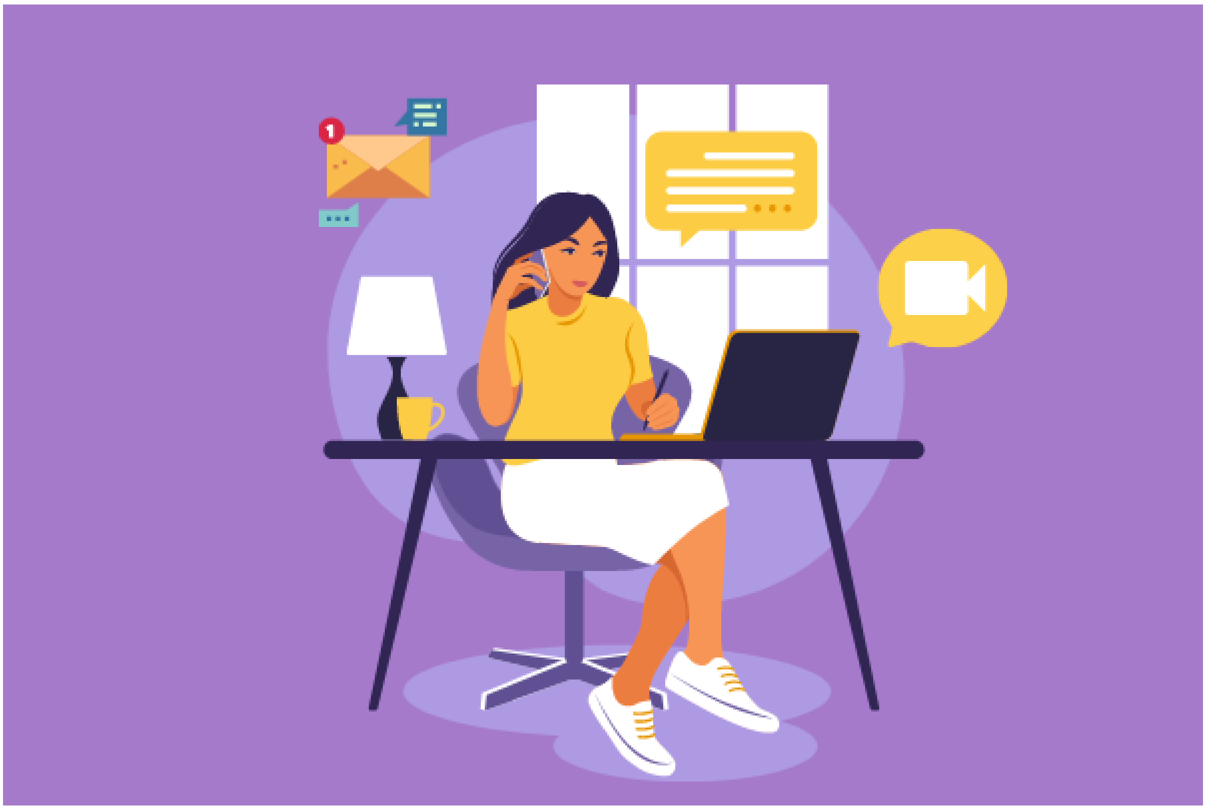
The IRS further concluded in Notice 2011-72 that employees don't have to keep records of their business and personal use, which is an extraordinary exception to the accountable plan rules' substantiation requirement.

IRS Pub. 15-B picks up this language almost verbatim.

Simultaneous with the release of Notice 2011-72, the IRS' Small Business/Self-Employed Division released a memorandum to auditors covering employees who use their own phones for business. The memorandum instructed auditors to follow the rules set out in Notice 2011-72 when performing payroll audits.

So, again, employees don't need to present you with logs of their business and personal use. But because employers have no control, the memorandum set out two additional conditions for tax-free reimbursements:

- Employees' cell phone coverage must be reasonably related to the employer's business needs (i.e., no satellite phones when employees travel locally).
- Reimbursements must be reasonably calculated not to exceed employees' expenses.



Unfortunately, Pub. 15-B doesn’t mention the memo at all. And there are several shortcomings with leaving this information out of Pub. 15-B:

- For employees who use their own phones, employees must at least substantiate their monthly costs by submitting their bills to you.
- Because employees who use their own phones for business must at least provide you with their monthly bills (to guarantee your reimbursements don’t exceed their expenses), flat cash amounts provided to them, regardless of whether they submit their bills, are taxable. It doesn’t much matter what you call your payment.
- Phones are tools, and like any other tool, employees must be able to prove they bought their phones specifically for use with your business. This is usually a tall order. So reimbursements for the purchase of their phones are likely taxable.

Pandemic problems

On more than one occasion, we’ve read that, because a disaster declaration has been made under the Stafford Act, reimbursements for all sorts of things, including employees’ business use of their cell phones and home-office equipment, are tax-free under IRC § 139.

No.

IRC § 139 excludes from income and taxation disaster relief payments:

- To reimburse or pay reasonable and necessary personal, family, living, or funeral expenses incurred as a result of a qualified disaster.
- To reimburse or pay reasonable and necessary expenses incurred for the repair or rehabilitation of a personal residence or the repair or replacement of its contents.
- But only to the extent any expense compensated by a disaster relief payment isn’t otherwise compensated for by insurance or otherwise.

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Cell phone and other pandemic-related home-office expenses (especially electric bills) just don’t fit this bill.

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