

Yet Another Wireless Issue – Cell Phones and the IRS

The Taxman Commeth...

At least for now

For a variety of reasons, I have not been a fan of corporate ownership of wireless phones and devices which are distributed to employees (see BAEC Bulletin. Although telecommunications consultants and managers recognize the cost savings in such corporate ownership, from a liability perspective, I believe that corporate ownership of these devices used by employees are simply not in the best interest of the enterprise. And recent litigation and settlements prove this point. But that's another topic for another day.

In an interesting and somewhat scary story from the wireless world, two 2008 cases (and resulting fines) involving different branches of the University of California system, have raised the level of awareness that the IRS classifies cell phones as "listed property" under Section 280 F(d)(4) of the US Code. To those of us who don't memorize the tax code, this may be cause to move quickly on to the Classifieds. STOP RIGHT HERE!!

This issue is critical because as of this moment, the IRS considers wireless devices in the same category as it does employer-provided vehicles, and thus subject to rigorous documentation obligations in order to be eligible for the big Ds – depreciation and deductibility (there is a weak argument that because it only specifies "cell phones," and not all wireless devices that this argument doesn't apply, but I suspect that moniker is simply a remnant of when the rule

was written when “cell phones” were the only wireless devices, obviously a condition which is no longer the case.) Because these devices are considered listed property, regardless of how logical (or il-logical) this classification may seem at first blush, the management of these devices by the employer is critical to both the employer and employee. Just so that we’re clear, the IRS fines assessed in these cases are not for the faint of heart. In 2008, UCLA paid a ... (...wait for it...) \$239,196 bill and UC San Diego paid \$186,471 for failing – or having its employees fail--to document precise information about each call made or received on the device owned by the employer.

In order for an employer to be able to deduct the cost of not only the device itself, but the service it provides (read: monthly fees), the employer must have current and specific documentation that reflects precisely how each device is used. In order for the enterprise to be eligible to take advantage of these corporate expenses, the enterprise must document 4 distinct elements related to use:

1. the amount of the expense (not only equipment, but per call amount as well)
2. the time and place of the use of the property (time and duration of call)
3. the business purpose of the expense; and
4. the business relationship between the employer (taxpayer) and the individual actually using the phone.

According to a note in Thompson's Employer's Guide to Fringe Benefits Rules (October, 2006), employers wishing to avoid the scrutiny and terror of an audit, "must collect and retain monthly statements, which generally set for the amount of the expense, the time and date of each call and the number dialed." The report goes on to say that failure "to maintain adequate documentation may result in lost deductions and possible Federal employment tax (federal income tax withholding, federal unemployment taxes, and Medicare assessments for employees."

The current law, which was written long before wireless devices were as ubiquitous and essential as they are today, requires that a wireless device be treated exactly as is any other executive perk. However, as is often the case with long standing regulations affecting technology, the laws no longer match the technology. That is, as technology has evolved, the rules that were designed to regulate and/or monitor its use are simply no longer a good fit.

However, in an effort to make some needed changes in the existing structure, H.R. 5450 Modernize Our Bookkeeping In the Law for Employee's Cell Phone Act of 2008 (or MOBILE Cell Phone Act of 2008) was presented to, and passed by the House of Representatives in early 2008. Unfortunately, the bill has been stalled in the Senate (where it is known as S. 2668) since Spring, 2008. However, the bill stands to serve many good purposes, and it is hoped that the Senate will take action on it early in the new year and administration.

The purpose of this bill, whose original sponsor in the Senate is John Kerry (D- MA), and which is co-sponsored by New York Senator Chuck Schumer, and also supported by Grover Norquist of Americans for Tax Reform (when, do you suppose, was the last time that these three were on the same page of anything intentionally) is to reclassify wireless devices from “listed property” ((26 USC 280F(d)(4)(v)) to that of “business property” (26 CFR 162(a)(3)) This change would

- eliminate the highly detailed, and in effect onerous, substantiation requirements that currently are the obligation of enterprise taxpayers;
- minimize to eliminate penalties and taxes assessed against enterprises for not meeting the substantiation requirements under audit;
- lessen the possibility that a tax-exempt organization could be subject to intermediate sanctions; and
- reduce the possibility of tax preparers being subject to penalties for failing to meet such requirements.

Before the full-fledged crunch of tax season surfaces, it might be worth a call to the office of either or both of New York’s senators to encourage them to resurrect and pass this bill. A constituent phone call (or thousands of them) could yield big savings for both you and your enterprise clients (in financial and emotional terms).