



---

## MMS Position Paper: Employer-Paid Cell Phone Use/Tax Liability

MMS position papers are a compilation of our staff's research, education, 20+ years of field experience, and our interpretation of current laws as we understand them. The information contained in this paper is not legal advice and is intended to be used as general information to help your organization formulate your organization's guidelines. It is understood that your organization is legally responsible for all policies and procedures, and their legal basis.

**Application:** If an employer pays the monthly cell phone bill of an employee, and the employee uses the cell phone for personal use, a portion of those payments must be included as taxable compensation on the employee's W-2. While there are ways to limit the taxable portion, IRS regulations place a burden on the employee and the employer to prove the non-taxable portion. The following information summarizes what the IRS requires in this matter and then discusses some limited ways to avoid the burden imposed by the IRS.

**Listed Property** – In 1989, the IRS classified cell phones as "listed property." This means the cost of an employer-provided cell phone needs to be treated (for tax purposes) like an employer-provided vehicle. In both cases, if an employee uses an employer-provided car or cell phone for personal use, the personal use portion of the ongoing cost needs to be reimbursed back to the employer or it needs to be added to the employee's W-2 as taxable compensation.

In the case of cell phones, each month's cell phone bill paid by the employer needs to be itemized call-by-call to distinguish how much of the cell phone usage was a personal call compared to those made for the direct benefit of the organization. The percentage of personal call minutes compared to the total minutes used then needs to be applied to the total bill. The employee then needs to either reimburse the employer for those costs within 60 days or the personal use value must be added to the employee's W-2.

**An Excessive Burden** – Many articles have been written over the past 20 years about the burden these IRS regulations place on employees and employers. Repeated attempts have been made in the U.S. Congress to remove the record keeping burden, but to no avail. Meanwhile, IRS regulations regarding this matter are clear. While there are no appropriate exceptions in submitting to the regulations, there are ways to avoid the record keeping burden.

**Alternatives/Options** – Few employees and employers will take the time to separate the personal and business use calls made on a cell phone bill every month. Some organizations mistakenly

believe they can do this for a few months and arrive at a flat personal use percentage. Unfortunately, the IRS does not condone this practice. Every month's bill must be itemized for business and personal-use calls. What many organizations choose to do instead is follow one of two options:

1. Monthly Allowance – The primary option most organizations choose to avoid the record-keeping burden is to issue a monthly allowance to the employee that is intended to cover the cost of cell phone usage. While the monthly allowance is fully taxable, it removes the need to keep a record of business and personal use. Some organizations will label this a “communications allowance” or a “technology allowance” in that it can only be used for this purpose. In this context, the employer requires the employee to use the funds to satisfy a specific business-related purpose with the allowance. The employer will want to determine how much allowance is needed to cover the cost of a cell phone that satisfies the business requirement of the cell phone for each employee.

In this case, the employee could itemize the business use of the monthly cell phone bill and request a non-taxable reimbursement from the employer. Most employees will not follow through on this since it creates the same record keeping burden that led to the allowance in the first place.

As a reminder, an allowance (as described above) is fully taxable and must be included in an employee's W-2.

2. Two Cell Phones – Another option some organizations consider is for the employee to own two cell phones – one that is purchased and used 100% for business purposes and one that is purchased and primarily used for personal use. In this case, the IRS requires the employer to have a written policy limiting the use of the business-use cell phone for business purposes, and the employer is required to periodically audit the cell phone bills of the employee to confirm there are no personal calls listed. This option doesn't appear to lessen the burden on the employer. With this in mind, most employers will not consider this to be a viable option.

**Changing the Law?** – Reports surface occasionally that suggest Congress is prepared to overturn this portion of the IRS regulations. With a tight economy and limited tax revenues, Congress doesn't appear to be eager to make this kind of change. Unfortunately, tax law change is constant, and it's possible this specific part of the law may be removed or modified in the future. Stay tuned to MMS for future changes.