

INFORMATION REPORTING PROGRAM ADVISORY COMMITTEE (IRPAC)

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August 31, 2009

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Mr. Jeffrey T. Rodrick
Office of Associate Chief Counsel (Income Tax & Accounting)
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Attn: CC:PA:LPD:PR
(Notice 2009-46), Room 5203
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Ben Franklin Station
Washington, DC 20044

**Emerging Compliance
Issues**

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Re: Methods for Determining Personal Call Usage on Employer-provided Cell
Phones - Notice 2009-46

Dear Mr. Rodrick:

The Information Reporting Program Advisory Committee (IRPAC)¹ appreciates the opportunity to provide comments on the development of new methods for determining personal call usage on employer-provided cell phones. We commend your efforts to seek comments from the public as you have done in Notice 2009-46 (the "Notice"). This notice requests comments from the public regarding several proposals to simplify the procedures under which employers substantiate an employee's business use of employer-provided cellular telephones or other similar telecommunications equipment; e.g. Blackberry, pager, iPhones, smart phones and other 3G equipment, PDAs, GPS locators (hereinafter collectively referred to as "cell phones"). Where services include fees for such items as internet use and text messaging, we note that monthly user statements usually breakout usage by event, time used or gigabytes transmitted so we believe that the applications discussed below can be applied the same as for phone usage. Where use for any of these services is unlimited at a flat fixed fee or specified under a flat minute plan, we have also offered some ideas below.

IRS Notice 2009-46 suggests some means of documenting business use of cell phones that would be simpler than the current requirement for detailed logs of date, time,

Modernization

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¹ IRPAC was established in 1991 in response to an administrative recommendation in the final Conference Report of the Omnibus Budget Reconciliation Act of 1989. Since its inception, IRPAC has worked closely with the IRS to provide recommendations on a wide range of issues intended to improve the information reporting program and achieve fairness to taxpayers. IRPAC members are drawn from and represent a broad sample of the payer community, including major professional and trade associations, colleges, and universities, and state taxing agencies.

duration, business purpose, etc. IRPAC believes that the ideal solution, as suggested by IRS Commissioner Douglas Shulman, is for Congress to pass legislation ensuring no tax consequences to employers or employees for personal use of work-related devices such as cell phones provided by employers. Looking to an impending legislative change, IRPAC believes the best course of action for the present is a moratorium on enforcement.

Moratorium on Enforcement

In light of the pending legislation to remove cell phones from the definition of listed property, IRPAC recommends the temporary suspension of enforcement of the listed property rules as they impact cell phone use as well as the related employee income inclusion for personal cell phone use. As has been pointed out in other letters submitted to the IRS in response to Notice 2009-46, a moratorium on enforcement would be consistent with the Commissioner's recent action suspending the imposition of tax shelter penalties pending a legislative amendment to narrow an overbroad section of IRC §6707A.

Comment Pursuant to Notice 2009-46

The simplification of the substantiation requirements covered in Notice 2009-46 is also a step in the right direction. In this regard, IRPAC submits the following comments on the three alternative methods under consideration and also provide comments on other topics indicated in Notice 2009-46 of interest to the IRS.

Simplified Substantiation Methods

1. Minimal Personal Use Method

Proposal 1: The entire amount of an employee's use of an employer-provided cell phone would be deemed to be for business purposes if the employee can account to his or her employer with sufficient records to establish that the employee maintains and uses a personal (non-employer-provided) cell phone for personal purposes during the employee's work hours.

- Recommendation: The employer should establish a policy under which an employee who is provided a cell phone by the employer will agree to maintain and use a non-employer provided cell phone for personal use. For purposes of this proposal, the employee should be required to provide a copy of at least one of their cell phone billing statements for their personal-use cell phone at least annually to substantiate that the employee maintains a personal cell phone.

Proposal 2: A specified amount or type of "minimal" personal use would be disregarded in determining the amount of personal use of an employer-provided cell

phone. For example, “minimal” could be defined by reference to a particular number of minutes of use or for certain personal purposes.

- **Recommendation:** The employer should establish a policy defining appropriate use of employer provided cell phones along the same lines as policies governing use of employer provided computers and other technology. Rather than attempting to quantify personal use, the policy should establish that minimal or incidental personal use should not result in any measurable cost to the employer and should benefit the employer by allowing employees to avoid unnecessary or time consuming inconveniences at the expense of their business duties.
- **Recommendation:** Fees under cell phone plans with “unlimited use” billing will be the same even if there is employee personal use. Similarly, a flat minute plan, where the employer typically purchases the number of minutes it expects to use, will be the same even if there is employee personal use. Unlike employer provided vehicles where personal use results in additional expense, such as gas and wear and tear, cell phone expense under “unlimited use” or “fixed flat minute” billing is the same cost no matter the use. If an employer provides a cell phone with “unlimited use” or “fixed flat minute” billing and the employees job requires at least 50% business use, the IRS should assume that the entire cost of the cell phone is business use.

2. Safe Harbor Substantiation Method

An employer would treat a certain percentage of each employee’s use of an employer-provided cell phone as business usage. The remaining percentage of use would be deemed to be for personal purposes. For this proposal, the IRS and Treasury Department propose a business use percentage of 75 percent.

- **Recommendation:** Changes in technology and pricing are frequent in this area and the employer will need a reasonable method for determining an appropriate and stable schedule of charges. The employer should be allowed to elect to use either actual billings or, if IRS deems it necessary, an annual schedule of pricing based on aggregate experience published by the IRS. However, IRPAC strongly recommends the IRS avoid publishing such a national rate list. Like the life insurance imputation tables and the company vehicle value tables, the prices become outdated too fast and then become very unfair to administer.
- **Recommendation:** IRPAC notes that many employers currently treat 20% - 25% of each monthly billing as wages for personal use of cell phones. The IRS suggested safe harbor of 75% business use/ 25% personal use is a fair

resolution of a difficult determination and one that many employers will elect to follow. Further considerations on this point are outlined below.

3. Statistical Sampling Method

In general, an employer could use an approved statistical sampling methodology similar to that provided in Rev. Proc. 2004-29, 2004-1 C.B. 918, to determine the percentage of personal use of employer-provided cell phones.

- Recommendation: The one method that seems allowable for documenting both listed and de-listed property is under Reg. §1.274-5T(c) which allows a sampling supported by collateral evidence. There is potential in the approach under Rev. Proc. 2004-29, however, this revenue procedure does not authorize the use of statistical sampling to substantiate meal and entertainment expenses as required by §274(d), nor the use of statistical sampling to determine a taxpayer's liability for employment taxes or whether an amount is excludable from a taxpayer's income, nor establish the correctness of a taxpayer's interpretation of §274(n) or characterization of meal and entertainment expenses as expenses excepted from §274(n)(1). In this regard, we are uncertain of the IRS allowance as these are the very points of consideration in this context. We also note that use varies between employees even within the same industry and this will make establishing a sampling strategy difficult.

Other Topics of Interest

1. Employer's Written Policy

Specific provisions that should be required to be included in an employer's written policy prohibiting personal use of employer-provided cell phones.

An employer's written policy should be made applicable to all employees and clearly written so as to explicitly provide that personal use of employer provided cell phones and related technology is prohibited by the employer. Members of IRPAC have suggested the following policy inclusions:

- A broad description of the allowable, appropriate business use of employer provided cell phones that make clear the business purpose of providing the cell phone.
- A clear policy statement restricting use of employer provided cell phones to the specified allowable business use and clearly stating that personal use is unauthorized and prohibited.
- The policy should specify limited types of situations in which incidental personal use is acceptable, providing that such use does not result in any measurable cost to the employer, and benefits the employer by aiding the

employee in efficiently carrying out the employer's business. The policy should provide guidelines for the amount of minimal personal use considered to be incidental personal use.

- The policy should not be required to provide comprehensive lists of allowable business and personal use. Such an endeavor would be very cumbersome and is unlikely to capture all situations.
- The policy should identify sanctions for failure to comply with the provisions of the policy.
- The policy should identify a department, division, or individual responsible for dissemination of the policy to employees, responding to incidents of misuse, and generally enforcing the policy.

2. Methods Used by Employers to Determine Fair Market Value of Employer-Provided Cell Phones

Examples of methods currently used by some employers to determine the fair market value of an employee's use of an employer-provided cell phone are provided below with some discussion of their limitations and benefits.

Method 1 – Small Employer

In the month of December each year, the Employer calculates the annual amount of fringe benefit for each employee who is issued a company owned cell phone. The following process is used:

- A month is randomly chosen and copies of all that months cell phone bills are copied.
- The copies are distributed to the employees for them to mark all personal calls on their phone bill and return them to the Employer.
- The Employer calculates a percentage of personal minutes per total minutes used for that month for each employee.
- The percentage is multiplied by the total cost of the phone bill for that month for each employee to equal a dollar amount for personal usage.
- That monthly dollar amount for personal usage is then multiplied by total months used that calendar year to equal annual cost of personal usage of each employee's cell phone.
- This annual cost is then entered under fringe benefit on the last payroll in December and the employee is taxed on this amount.
- If an employee should terminate employment in the middle of a year, he or she will be taxed on their last paycheck for the current personal cell phone usage to date of that calendar year.

We note that implementation of a method such as this one may not be feasible for a large employer with hundreds of employees using cell phones as it is manually intensive in its requirement for individual review, calculation of the personal wage amount and individual extrapolation for each employee based on that review.

Although this may be a viable option for some small employers, other methods will need to be provided as alternatives that will ease the burden on a large employer, such as the use of a safe harbor as discussed above. The advantages of this method is that it does provide the employee with a fairer relationship to actual phone use and where very little use is personal, such as under 5%, the wage imputed would be small in comparison to an employee that has 20% personal usage.

Method 2 – Large Employer

- A cross-section of the users (employees with company owned cell phones) encompassing lines of business, titles, high-volume users and low-volume users is selected for invoice sampling.
- A sample of ten percent (10%) of each cross section user population (maximum 25 users) is selected.
- The initial sample will be taken from the third monthly invoice after the program implementation and annually thereafter, using a recent invoice.
- Only billable peak usage minutes, as defined by the cellular carrier, will be sampled.
- Users selected for invoice sampling will be required to reconcile their usage by providing the number of personal and business calls/minutes.
- Using best efforts, calls from selected samples will be re-verified as to personal or business use, via publicly available directory assistance data.
- Compiled data will be used to determine the average personal and business percentage.
- Personal percentage multiplied by the total cellular expense will equal the average compensations amount for all participants in the applicable cross-section of users.

If made an approved method, the advantage of this method is that it allows the employer an opportunity to demonstrate an average personal use of less than a safe harbor percentage without the need to review each and every employee's records. Although this may be a viable option for some employers, other methods will still need to be provided as alternative elections for those employers unable to carry the burden that this manually intensive sampling approach would require, such as the use of a safe harbor as discussed above.

3. Simplified Method of Determining Fair Market Value

Whether a simplified method of determining the fair market value of an employee's use of an employer-provided cell phone would be appropriate, and, if so, suggested simplified methodologies for determining such fair market value.

- Recommendation: It would seem reasonable to allow the employer to elect to use internally developed pricing schedules or actual billings.
- Recommendation: Today's market place is highly volatile where technology and pricing changes almost daily. Where a company negotiates

a contract for communication services it is not unusual for an employee to find better pricing on their own. Since many employees pay out of pocket for the company service to be later reimbursed, they are more apt to chose the cheap route and acquire their own service for reimbursement. For these reasons, we do not believe that a yearly schedule of pricing published by the IRS will be a reasonable endeavor and may well result in substantially over charging or undercharging the values and the market changes throughout the year. To force a company to draw upon an outside source to determine an expense item can increase errors and the potential for other book-to-tax abuses. A better alternative is to allow use of the actual employee level billings or the employers negotiated annual group contract rate. This will allow for Accounts Payable controls to come into play; providing the review of billings and validation of expenses.

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To the extent that we discover additional matters of importance that the IRS should consider in the rules-making process, we will inform you as soon as possible. IRPAC looks forward to working with you to help ensure that the ultimate determination on the methods for determining personal call usage on employer-provided cell phones is fair and workable for all taxpayers. If you have any questions, please contact the undersigned.

Sincerely,

Jon Lakritz
2009 IRPAC Chair

cc: Douglas H. Shulman, Commissioner, Internal Revenue Service