



A Ringing in Your Ears—Businesses and Telephone Tax Refunds  
Podcast of November 18, 2006



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## IRS Releases Simplified Telephone Tax Refund Procedure

This week the IRS has released new “simplified” procedures for businesses to use to claim the telephone tax refund in lieu of assembling the information from all of their phone bills for the period in question. The new program was announced in IRS News Release IR-2006-179, which is included in this document along with the IRS question and answer FAQ related to this matter.

## Businesses and Tax-Exempts Can Use Formula for Telephone Tax Refund

IR-2006-179, Nov. 16, 2006

WASHINGTON — The Internal Revenue Service today announced a formula that will allow businesses and tax-exempt organizations to estimate their federal telephone excise tax refunds.

“The formula will provide a less burdensome option than gathering up to 41 months of old phone records,” said IRS Commissioner Mark W. Everson.

In May 2006, the IRS announced that individuals, businesses and tax-exempt organizations who paid the long-distance telephone excise tax can request the refund on their 2006 federal income tax returns.

“Businesses and tax-exempt organizations generally have more varied phone usage patterns than individuals,” Everson said. “The IRS has met with a number of businesses and tax-exempt organizations to understand their concerns. We believe we have developed a reasonable method for estimating telephone excise tax refund amounts while reducing burden.”

To request a refund, businesses (including sole proprietors, corporations, and partnerships) and tax-exempt organizations must complete Form 8913, Credit for Federal Telephone Excise Tax Paid. To complete this form, businesses and tax-exempt organizations may determine the actual amount of refundable long-distance telephone excise taxes they paid for the 41 months from March 2003 through July 2006, or use the formula to figure their refunds. Businesses should attach Form 8913 to their regular 2006 income tax returns. Tax-exempt organizations must attach it to Form 990-T.

Businesses and tax-exempt organizations can figure their refund amounts by comparing two telephone bills from this year to determine the percentage of their telephone expenses attributable to the long-distance excise tax. The bills they should use are the bill with a statement date in April 2006 and the bill with a statement date in September 2006. They must first figure the telephone tax as a percentage of their April 2006 telephone bills (which included the excise tax for both local and long-distance service) and their September 2006 telephone bills (which only included the tax on local service). The difference between these two percentages should then be applied to the quarterly or annual telephone expenses to determine the amount of their refunds.

The refund is capped at 2 percent of the total telephone expenses for businesses and tax-exempt organizations with 250 or fewer employees – which covers more than 99 percent of all businesses. The refund is capped at 1 percent for those with more than 250 employees. Most organizations in this category typically are able to figure the actual amount they paid in long-distance excise tax. However, the formula provides a more limited, but simpler, approach for those large employers who wish to use it.

For example, if a business has an April 2006 telephone bill of \$1,000, which includes Federal telephone excise tax of \$28, the tax percentage is 2.8 percent. If the September 2006 bill is \$1,100 including Federal telephone excise tax of \$16.50, the tax percentage is 1.5 percent. The business' long-distance excise tax percentage is 1.3 percent (2.8 percent for April minus 1.5 percent for September). The business multiplies 1.3 percent by its total phone expenses over the 41-month period to arrive at the amount of its refund. If this business had more than 250 employees, its refund would be limited to 1 percent of its total phone expenses for the period. If the business had 250 or fewer employees, the 2-percent cap would apply and would not limit the amount of the refund.

The IRS developed the formula after receiving public input and discussing the issue with business organizations, the Small Business Administration and representatives from the tax-exempt community.

The IRS already has provided individual taxpayers with the option to use standard amounts based on the number of exemptions allowed to that taxpayer. Individual taxpayers can request a \$30 refund with one exemption, \$40 for two exemptions, \$50 for three exemptions and \$60 for four or more exemptions.

Options for requesting this refund vary for sole proprietors, who file a Schedule C with the Form 1040, depending on the gross income reported on the Schedule C. Sole proprietors who report gross income of \$25,000 or less on their Schedule C may use the standard amounts or request a refund based on their actual expenses. Sole proprietors reporting more than \$25,000 of gross income have three options: they can use the standard amounts which cover both personal and business expenses, they can use the formula for their business expenses and actual for their personal ones, or they can choose to use actual amounts for both business and personal.

Similar rules depending on the amount of gross income reported on Schedule F or Schedule E apply to farmers and individual owners of rental property.

Trusts and fiduciaries may not use the standard amount available to individuals. They should use the formula to figure their refunds, or request the actual amount paid.

The Treasury Department announced in May that the government would stop collecting the federal excise tax on long-distance telephone service beginning Aug. 1, 2006 and provide refunds for taxes billed after Feb. 28, 2003.

Details on the telephone tax refund will be included in 2006 tax return materials and on [IRS.gov](http://IRS.gov).

## IRS Question and Answer Sheet

### Telephone Tax Refunds

#### Questions and Answers for Businesses and Tax-Exempt Organizations

**Q. Are businesses required to dig through all their old phone records to figure their telephone tax refund?**

A. No. The IRS has developed a formula that most businesses and tax-exempt organizations can use to figure their refund. To use the formula, eligible taxpayers need only review their phone bills for 2 months, instead of all 41 months included in the refund period. In addition, eligible taxpayers need to know their total telephone expenses for the 41-month period and the number of employees reported on their federal withholding tax return (Form 941) for the second quarter of 2006.

The formula is an alternative to basing a refund request on the actual amount of tax paid. All taxpayers have the option of requesting a refund using the actual amount of tax paid.

Whether they use the formula or actual taxes paid, businesses and tax-exempt organizations must use Form 8913, Credit for Federal Telephone Excise Tax Paid, to request the refund. Businesses attach this form to their regular income tax return for 2006. Tax-exempt organizations attach it to Form 990-T.

**Q. Who can use the formula?**

A. In general, businesses and tax-exempt organizations that were operating at any time during the period from March 1, 2003, through July 31, 2006, and continued to incur phone expenses from April 2006 through September 2006, may use the formula. This includes corporations, S corporations, partnerships, trusts and estates. (Trusts and estates are treated as businesses in applying the formula.) Nonprofit tax-exempt organizations, including churches and charities, can also use the formula.

In addition, individual owners of rental property and self-employed people, including independent contractors, sole proprietors and farmers, can use the formula, but only if they report gross rental and business income totaling more than \$25,000 on their 2006 federal income tax returns. This is the amount shown as:

- Gross income on Schedule C, Line 7,
- Gross receipts on Schedule C-EZ, Line 1,
- Rents received on Schedule E, Line 3, and
- Gross income on Line 11, Schedule F.

Individuals with more than one activity who fill out multiple business or rental schedules

should add together all gross rental and business income amounts shown on these schedules. Similarly, married couples filing joint returns should also combine their gross rental and business income amounts from these schedules.

**Q. How does the formula work?**

A. To use the formula, businesses and tax-exempt organizations follow these steps:

1. Take the April 2006 phone bill (this is the bill with an April 2006 statement date) and divide the total federal telephone excise tax by the total phone bill (including federal telephone excise taxes) to arrive at the percentage of the bill attributable to federal telephone excise tax. If you have more than one type of service or service provider (land line, fax, cell, local, long distance, bundled, etc.), combine all bills dated in April before making this computation. For this purpose, there is no need to separate the taxes paid on long-distance service from those paid on local service. April is a representative month during which the government was still collecting the excise tax on long-distance service.
2. Take the September 2006 phone bill and divide the total federal excise tax by the total phone bill to arrive at the percentage of that bill attributable to federal telephone excise tax. The percentage should be lower because the government was only collecting the federal excise tax on local telephone service.
3. Subtract the September percentage from the April percentage to arrive at the percentage that represents the federal long-distance tax. This is the percentage businesses and tax-exempt organizations will use to figure their refunds (capped as discussed below).
4. Multiply the long-distance tax percentage by the total phone expenses shown on telephone bills dated after Feb. 28, 2003, and before Aug. 1, 2006. The refund is capped at 2 percent of phone expenses for small businesses (those with 250 or fewer employees) and one percent for large businesses (those with more than 250 employees). Use the number of employees for the pay period that included June 12, 2006. This is the number reported on Line 1, Form 941 (Employer's Quarterly Federal Tax Return) for the second calendar quarter of 2006. Interest is added to the refund amount.

You can use the formula, even if your organization or business only operated for part of the 41-month period. However, if you were not in business or operating April through September 2006, you cannot use the formula. You can only request a refund for months for which the telephone tax was paid.

**Q. I qualify to use the formula, but my telephone expense records are not broken down by month. Is there an acceptable method for me to estimate my telephone expenses for the 41-month refund period?**

A. Yes. You can base your estimate on the amounts you reported as business-related telephone expense on your returns for tax years 2003 through 2006. Prorate the telephone expense amount for a particular tax year if part of the year falls outside the refund period (2003 and 2006 for most taxpayers).

For example, like most taxpayers, Company Z files its income tax return on a calendar-year basis. It operated continuously during all four years and claimed telephone expense deductions totaling \$12,000 in tax year 2003, \$11,000 in 2004, \$12,000 in 2005 and \$12,000 in 2006. Z estimates the amount of its telephone expense that falls within the 41-month refund period as follows. In tax year 2003, only 10 months (March through December) fall within the telephone tax refund period. Z estimates its telephone expenses for this period by multiplying the \$12,000 telephone expense deduction for 2003 by 10/12 (10 months divided by 12, the number of months in the tax year) to arrive at a figure of \$10,000. There's no need to prorate the deductions for 2004 and 2005, because these tax years fall entirely within the refund period. In 2006, 7 months (January through July) fall within the refund period. Accordingly, Z prorates its \$12,000 telephone expense deduction by multiplying it by 7/12 to come up with an estimate of \$7,000. Z adds together the prorated telephone expense for 2003 (\$10,000), the actual telephone expense deduction for 2004 (\$11,000), the actual deduction for 2005 (\$12,000) and the prorated expense for 2006 (\$7,000). The result, \$40,000, is Z's estimated telephone expense for the 41-month refund period.

Note: For reporting purposes, telephone taxes need to be allocated by month or quarter. See Form 8913 and its instructions for more information.

**Q. Which cap should a business or nonprofit use if its number of employees is 250 or less for part of 2006 and more than 250 for the rest of the year?**

A. The cap is determined based on the number of employees for the pay period that includes June 12, 2006. This is the number reported on Line 1, Form 941 (Employer's Quarterly Federal Tax Return). Thus, employment levels at other times of the year have no impact.

**Q. In applying the percentage cap, are part-time employees considered the same as full-time employees?**

A. Yes. Use the number of employees reported on Line 1 of Form 941 for the second quarter of 2006. This figure includes both full-time and part-time employees. It does not include household employees, employees who received no pay, pensioners and active members of the armed forces.

**Q. Can you provide an example of how the formula works?**

A. Company Z had ten employees during the pay period that included June 12, 2006, and, as noted above, had telephone expenses totaling \$40,000 for the 41-month period beginning after Feb. 28, 2003 and ending before Aug. 1, 2006. Its phone bill, dated April 5, 2006, was \$1,000 (including federal excise tax of \$28), and its phone bill dated Sept. 5, 2006, was \$1,100 (including excise tax of \$16.50). Company Z's telephone tax percentage for April is 2.8 percent (\$28 divided by \$1,000) and its telephone tax percentage for September is 1.5 percent (\$16.50 divided by \$1,100). Subtracting the September telephone tax percentage of 1.5 percent from the April percentage of 2.8 percent gives Company Z a long-distance tax percentage of 1.3 percent.

Company Z qualifies as a small business (one with 250 or fewer employees) and its telephone tax percentage falls below the two-percent cap that applies to small businesses. Multiplying 1.3 percent by Company Z's total telephone expenses of \$40,000 results in a telephone tax refund of \$520. Interest is added to this amount.

If Company Z instead had more than 250 employees, and wanted to use the formula, its long-distance tax percentage would be capped at one percent and its refund using the formula would be \$400 (\$40,000 times one percent), plus interest.

**Q. Are there any additional forms required to use the formula?**

A. No. All businesses and tax-exempt telephone tax refund requests must be made using Form 8913, Credit for Federal Telephone Excise Tax Paid. No additional forms are needed to use the formula.

**Q. Does an eligible entity have to use the formula?**

A. No. The formula was designed to make it easier for businesses and tax-exempt organizations to request the telephone tax refund. It is optional. Any business or tax-exempt organization can choose to request a refund based on the actual amount of long-distance telephone excise tax billed after Feb. 28, 2003 and before Aug. 1, 2006.

**Q. Does the IRS plan to audit telephone tax refund requests?**

A. The IRS expects to treat telephone tax refund requests in a manner similar to other tax returns. In general, the IRS accepts most federal tax returns as filed. However, to make sure taxpayers are following the law, the agency examines or audits some returns.

Returns are audited for a variety of reasons, and most are chosen by computerized screening.

**Q. In case of audit, what records should businesses and tax-exempt organizations keep?**

A. If you use the formula, the IRS suggests that you keep the following records:

- Copies of your phone bills dated in April and September 2006,
- Your business-related telephone expenses for the 41 months for which the refund is available (March 2003 through July 2006), and
- The number of employees during the pay period that included June 12, 2006, as reported on Line 1, Form 941 (Employer's Quarterly Federal Tax Return) for the second quarter of 2006.

If you base your refund request on the actual amount of your telephone tax, keep copies of your telephone bills for the 41-month period.

Either way, do not send these documents with your refund request — keep them for your records.

**Q. Are foreign businesses and tax-exempt organizations eligible to request the**

**telephone tax refund?**

A. Yes. Like other taxpayers, they are eligible to file if they paid federal long-distance taxes billed after Feb. 28, 2003, and before Aug. 1, 2006.

**Q. Can businesses and tax-exempt organizations figure their refunds using the actual amount of tax incurred for one year and use the formula for taxes incurred in another year?**

A. No. Businesses and tax-exempt organizations can choose either method but not both.

**Q. If a taxpayer owns more than one business, does the taxpayer submit a separate refund request for each business?**

A. In some cases, yes. It depends upon whether each business is considered a separate business for tax purposes.

Each business that has an employer identification number (EIN) with the IRS (for example, two corporations owned by the same taxpayer) is considered a separate business for tax purposes and can request a telephone tax refund. Each separate business can choose to figure its refund using either the formula or the actual amount of tax paid. Individuals who operate more than one business as a sole proprietor are issued only one EIN. Thus, an individual can submit only one refund request.

**Q. Can the IRS use telephone tax refunds to offset tax debts?**

A. Yes. Like other tax refunds, the telephone tax refund can be applied against other taxes owed by the taxpayer.

**Q. I am requesting the telephone tax refund on my 2006 business return, and I expect to receive my refund in 2007. Do I have to report it as income on my 2007 return?**

A. Generally, yes. Normally, a business taxpayer can deduct the cost of telephone service, including related taxes. Thus, if you later receive a refund of those taxes, you normally must include it, along with any related interest, in your gross income in the year you receive it.

Further details on reporting these refunds will be included in IRS publications and tax instructions for 2007.

**Q. Why can't the telephone companies pull the information from their databases and provide it to businesses?**

A. Many service providers lack easy access to records for the entire 41-month period. In general, they retain about six months of records on-line. In addition, many taxpayers have more than one service provider or have changed providers at least once in the past three years. Thus, the telephone companies cannot provide complete records for all of their customers.

The formula was created to save time and trouble for businesses and tax-exempts

requesting refunds and help limit the volume of customer record requests to companies in the telecommunications industry. Those wishing to base their requests on actual taxes paid and who lack adequate records may, in some cases, be able to obtain records from their service provider. However, service providers are not precluded from charging customers for providing these records, and customers making these requests may face substantial delays in obtaining them.

**Q. Why can't the IRS figure the telephone tax refund and send it to each eligible business or tax-exempt organization?**

A. The IRS does not have access to all of the information needed to figure these refunds.

**Q. How will the IRS provide the forms and other information needed by businesses?**

A. Details on the telephone tax refund will be included in all 2006 tax return materials and on IRS.gov.

**Q. If a business or tax-exempt organization does not have 41 months of documentation, what are its options?**

A. Businesses and tax-exempt organizations need their phone bills dated in April 2006 and September 2006 to figure their long-distance tax percentage for their refund requests. If a business or tax-exempt organization has its expenses broken out by month, all it has to do is add them together in the groups shown on Form 8913, Credit for Federal Telephone Excise Tax Paid. For example, it can add its March, April and May 2003 expenses together to obtain the total amount of telephone expenses it had for this time period.

If it does not have its expenses by month, it can estimate the amount for each time period on the Form 8913 by using the average monthly phone expense for each year included in the 41-month refund period.

For example, it divides its total telephone expense for 2003 by 12 to get a monthly average. It uses this amount to estimate the amount of telephone expense it incurred for each of the time periods in 2003 shown in column D of Form 8913. It can repeat this step for each subsequent year.