Is It Time for Deductions of Smartwatch Expenses?

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In this article, Dyson and Chittenden analyze whether some or all of the cost of a smartwatch should be deductible as a medical care expense under section 213.

Atrial fibrillation, otherwise known as AFib or AF, can be a silent killer if left untreated. It is the most common serious cardiac arrhythmia and can be asymptomatic or cause symptoms that vary from mild to life altering.[1] It can come and go on its own without explanation. Because AFib can often be asymptomatic, many do not know that they have a serious health issue.[2] Over time, however, the presence of AFib increases the risk of blood clots forming in the individual's heart, and if a clot travels to the brain, a stroke will result.[3] Strokes are the second leading cause of death around the world.[4] Thus, identifying the existence of AFib, so that the appropriate medical treatment and therapies can be determined, is critical to those dealing with this abnormal heart rhythm.

Obviously, this article is not about a medical condition. It is about the tax treatment of expenses incurred by individuals who purchase smartwatches, which offer many features for personal use as well as software functionality designed to help them manage their healthcare. If a smartwatch is the platform for applications that deliver helpful health data to wearers so they can seek medical attention proactively, has the time come to seriously consider whether expenses for purchasing the smartwatch are or should be tax deductible? Specifically, should all or some of the cost of a smartwatch be deductible as an expense for medical care under section 213? If so, a taxpayer could purchase a smartwatch supporting such applications under a flexible spending account, health reimbursement arrangement, or health savings accounts.

For example, the Apple Watch Series 4 supports applications that can provide an electrocardiogram (ECG) and recognize irregular heart rhythms. In September 2018 the Center for Devices and Radiological Health at the Food and Drug Administration concluded that the ECG app should be classified as a Class II device. The ECG app is a software-only mobile medical application intended for use with the watch to create, record, store, transfer, and display a single-channel electrocardiogram.[5] It is intended for over-the-counter use and to provide heart-rate information

[1] *See* Centers for Disease Control and Prevention, "Atrial Fibrillation Fact Sheet" (AFib fact sheet).

[2] Daniel J. Cantillon and Ram Amuthan, "Atrial Fibrillation," Cleveland Clinic for Continuing Education (Aug. 2018).

[3] *See* AFib fact sheet, *supra* note 1. According to the CDC, AFib results in 750,000 hospitalizations per year and contributes to 130,000 deaths.

[4] *See* World Health Organization, "Top 10 Causes of Death" (May 24, 2018).

[5] A stand-alone device devoted solely to ECG heart screening would clearly be deductible under section 213.

to a user, which can be used in consultation with her healthcare provider.

The ECG app is an extension of heart-rate detection capabilities built into earlier Apple Watch models. In March 2019 the Stanford University School of Medicine released its preliminary findings of a virtual study of more than 400,000 participants, which was sponsored by Apple. The study was launched in November 2017 to determine whether a mobile app using data from a heart-rate pulse sensor on the Apple Watch can help identify AFib. According to Stanford's news release and presentation at the American College of Cardiology, the watch's software accurately identified irregular pulse rates in a small percentage of participants, many of whom were later found to have AFib. Preliminary findings revealed that the heart-rate pulse sensor app proved to have a positive predictive value for identifying previously undetected AFib.[6]

The Apple Watch Series 4 also has a fall detection feature that, if enabled, will automatically initiate an emergency call for assistance if a hard fall is detected and the wearer is immobile for one minute.[7] A recent study found that the mortality rate associated with falls has been increasing over the last decade.[8] Obtaining assistance from local emergency responders following a fall may help mitigate the mortality risk for the wearer.

Apple isn't alone in its efforts to expand digital technology for healthcare. Other consumer wearables offer similar health functions. Smartwatches from MobileHelp and Medical Guardian both offer medical-alert fall detection systems and were designed as replacements for traditional fall detection devices. Like the Apple Watch, the MobileHelp Smart also offers heart-rate monitoring. Other smartwatches (or add-on devices) already offer blood-pressure monitoring, and applications available for the Apple Watch can work together with blood glucose monitors to display and store glucose readings and predict future blood glucose levels, so that the wearer can take steps to keep his glucose levels in the acceptable range. As technology continues to advance and evolve, the medical benefits of wearing a smartwatch will continue to grow.

With nearly 75 million Americans suffering from high blood pressure,[9] more than 100 million living with diabetes or prediabetes,[10] and as many as 6.1 million estimated to have AFib,[11] we believe that the time has come for expenses for smartwatches that support proven healthcare applications to be deductible medical expenses under section 213, at least in part. Striking the right balance between personal expenses and medical expenses is difficult in the context of a smartwatch with software applications recording important health data and offering fall detection as well as numerous other features. The newest versions of smartwatches provide a wide range of multifunctional applications and are not dedicated to a single purpose, such as the latest generation of blood-pressure cuffs and blood-sugar monitors. But the personal benefits should not preclude the health benefits from meeting the primary purpose test of section 213.

The underlying code provision — section 213 — was old even before the digital age started to roar through the landscape. The regulations have not been updated since 1979. For purposes of this discussion, "medical care," as defined by section 213(d)(1)(A), means amounts paid "for the diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the body." The deduction is not limited to expenses incurred because of symptoms of illness; it also covers

[6] *See* Stanford University School of Medicine, "Apple Heart Study Demonstrates Ability of Wearable Technology to Detect Atrial Fibrillation" (Mar. 16, 2019). According to Dr. Lloyd Minor, dean of the Stanford School of Medicine, "The results of the Apple Heart Study highlight the potential role that innovative digital technology can play in creating more predictive and preventive health care." Even more relevant to an individual's personal decision to purchase a smartwatch is Minor's prediction that "atrial fibrillation is just the beginning, as this study opens the door to further research into wearable technologies and how they might be used to prevent disease before it strikes — a key goal of precision health."

[7] Although the IRS has not explicitly stated as much, stand-alone fall detection devices, such as Life Alert, are likely also deductible medical expenses under section 213.

[8] Klaas A. Hartholt et al., "Mortality From Falls Among US Adults Aged 75 Years or Older, 2000-2016," 321 *J. Am. Med. Ass'n* 2131-2133 (June 4, 2019).

[9] *See* Centers for Disease Control and Prevention (CDC), "High Blood Pressure Frequently Asked Questions."

[10] *See* CDC, "National Diabetes Statistics Report, 2017."

[11] *See* AFib fact sheet, *supra* note 1.

physicals and diagnostic procedures when the individual is trying to preserve good health.[12]

The primary challenge in applying the deduction has involved the tension between the characterization of an expense as medical, which is deductible under section 213(d), or as "personal, living, or family expenses," which are generally not deductible under section 262. The regulations explain that "an expenditure which is merely beneficial to the general health of an individual, such as an expenditure for a vacation, is not an expenditure for medical care."[13] Of course, taxpayers have tried to deduct expenses incurred just to feel better: swimming pools when no therapeutic value has been demonstrated;[14] massages, yoga, and vitamin regimens to alleviate stress;[15] vacations at resorts in better climates for a cardiac patient;[16] and traveling to and from the golf course for a patient with emphysema who was advised by a physician to take up golf for therapeutic measures.[17] The IRS and the Tax Court have shut down such attempts.

When the expense does address a legitimate medical need but also provides a personal benefit, applying the section 213 guidelines is more difficult. Perhaps the best analogy is the old vacuum cleaner ruling, Rev. Rul. 76-80, 1976-1 C.B. 71. Issued long before the latest revolution in vacuum cleaners, the ruling concludes that expenses for the purchase of a vacuum cleaner by a taxpayer with an allergy to home dust were not deductible under section 213 because "there was no medical recommendation for the taxpayer's use of the vacuum cleaner or any feature of it, nor was there any indication that the vacuum cleaner would not have been purchased even if the taxpayer had not been allergic to dust." The ruling concludes with the observation that the vacuum cleaner at issue in the ruling was an item ordinarily used for personal, living, and family purposes as a cleaning device and was not purchased primarily for medical care.

But suppose a doctor recommends to a patient with allergies that she purchase a modern-generation vacuum cleaner with HEPA filtration and other advanced features, which exceed the cost of a standard vacuum cleaner, as a way to improve the patient's health. That would seem to substantiate the device as alleviating the patient's illness and therefore the expenses would be deductible.[18] Moreover, the same logic would appear to apply when an individual is instructed by a physician to wear a smartwatch to track heart rate and rhythm or to monitor and store blood glucose levels. But should a doctor's note be necessary to sustain deductibility under section 213 when an individual has unilaterally made an informed decision, based on personal health circumstances, that the expense is necessary to help prevent or monitor disease?

The IRS has recognized that some expenses may be deductible under section 213, even if motivated by the desire to improve health and not by imminent probability of a disease.[19] After years of resisting the position, the IRS ruled in 1999 that expenses incurred by taxpayers to participate in a smoking cessation program and related prescription medications constitute deductible medical expenses, even though participation is not suggested by a physician and the taxpayer is not diagnosed with a specific disease. But this recognition does not extend to expenses for participation in weight-reduction programs — at least in the absence of weight-related medical ailments — that are for the purpose of improving one's appearance, health, and sense of well-being.[20] That is true even though a health benefit can result from the taxpayer's successful participation in such a program.

[12] *See* Rev. Rul. 2007-72, 2007-50 IRB 1154 (amounts paid for an annual physical examination or full body scan are for diagnosis and therefore qualify as expenses for medical care, even though the individuals were not experiencing any symptoms of illness). The IRS has stated that medical information plans, which store medical information in a computer data bank and retrieve and furnish the information upon request of an attending physician, are deductible medical expenses. *See* IRS Publication 502. The ability of applications on smartwatches to record heart-rate data that can be provided to a physician arguably perform this function as well.

[13] Reg. section 1.213-1(e)(1)(ii).

[14] *Haines v. Commissioner*, 71 T.C. 644 (1979).

[15] *Huff v. Commissioner*, T.C. Memo. 1995-200.

[16] *Havey v. Commissioner*, 12 T.C. 409 (1949).

[17] *Altman v. Commissioner*, 53 T.C. 487 (1969).

[18] *Id*. *See also* Rev. Rul. 55-261, 1955-1 C.B. 307 (cost of an air conditioner held to be deductible under section 213).

[19] Rev. Rul. 99-28, 1999-1 C.B. 1269, revoking Rev. Rul. 79-162, 1979-1 C.B. 116; *see also* GCM 37115.

[20] Rev. Rul. 79-151, 1979-1 C.B. 116; *but see* Rev. Rul. 2002-19, 2002-1 C.B. 779 (weight-loss programs for an individual with hypertension and an individual with obesity are deductible medical expenses).

The fact that a smartwatch is somewhat expensive and can be used for several years should not preclude deductibility. As a rule, capital expenditures are not deductible under section 263. That prohibition against the deduction of capital outlays for long-lived property does not apply, however, to equipment and devices purchased for medical reasons, such as eyeglasses, crutches, wheelchairs, artificial teeth, and portable air conditioners. Expenses for these items are deductible under section 213, even though they may be in service for years and have trade-in value.[21] Thus, cost and useful life do not preclude a smartwatch from being deductible. The challenge, as noted above, is that the expenditure for the capital asset must have as its primary purpose the medical care of the taxpayer, his spouse, or his dependent.[22]

In other words, the medical benefits of a smartwatch cannot be secondary to the personal benefit of having a wearable device that has software applications that can do more than just provide health data to the wearer and the wearer's physicians. If, as posited above, the smartwatch is purchased at the direction of a physician who wants the patient to monitor her heart rate and rhythm, should the purchase be deductible under section 213(d)? We think the answer should be "yes" — even in the absence of physician direction, especially if the individual is at risk for any of the potential medical issues that can be detected by the applications on a smartwatch. We acknowledge, however, that the IRS will likely be resistant to such an approach. Thus, it may well be that the time has arrived when the IRS should not have the last say on this issue.

We have been in a similar debate before because of the dizzying emergence of technology becoming such an integral part of our daily lives and providing personal benefits. Before 2010, cell phones and telecommunications equipment were included in the definition of "listed property" in section 280F(d)(4)(A)(v). Being "listed" has the effect of not only limiting the amount of depreciation for the property (that can otherwise be used for personal purposes), but imposing detailed recordkeeping requirements under section 274(d)(4) for business deduction and fringe benefit purposes.[23] To exclude the value of the business use of listed property from an employee's income under the working-condition fringe benefit exclusion of section 132(d) and the accountable plan rules of section 62(c), detailed records must be kept. For employer-provided cell phones or cell phone services before 2010, the entire value of the use of the cell phone (including monthly service charges) had to be treated as wages if insufficient records of business calls were kept.

In the early 2000s, the review of recordkeeping requirements for employer-provided cell phone benefits was de rigueur during IRS employment tax examinations. Because the Tax Court had sustained the requirements of detailed substantiation under section 274(d) regarding cell phones over the years,[24] the IRS was well positioned for payroll tax assessments when it determined that the detailed substantiation requirements had not been met by the employer and its employees. After several years of discussions between taxpayers and the IRS, Congress stepped up in 2010 and "de-listed" cell phones and similar telecommunications equipment, eliminating the application of the detailed substantiation requirements under section 274(d).[25] Although the legislation did not address section 162 business substantiation requirements for purposes of deducting costs or excluding the value of the business use under

[21] Reg. section 1.213-1(e)(1)(iii).

[22] For example, some continuous positive airway pressure machines have alarm clocks built in, but the inclusion of such a feature does not preclude the cost of such machine from being deductible under section 213(d).

[23] Under the regulations, deductions for expenses attributable to the business use of listed property are disallowed unless the taxpayer substantiates by adequate records or by sufficient evidence corroborating the taxpayer's own statement the amount of the expenses, the time and place of the use of the listed property, and the business purpose of the expense. *See generally* reg. section 1.274-5T(b)(6) and -5T(c). For cell phones, the related expenses subject to these requirements include the purchase price of the equipment (or an annualized "lease value" approximation of that price), monthly service charges, and any additional per-minute, roaming, long-distance, or other operating charges. *See, e.g.*, reg. section 1.274-5T(6)(i).

[24] *See, e.g.*, *Cottrell v. Commissioner*, T.C. Summ. Op. 2008-101, No. 16067-06S; *Vaksman v. Commissioner*, T.C. Memo. 2001-165, *aff'd*, No. 02-60062 (5th Cir. 2002); *Woods v. Commissioner*, T.C. Memo. 2004-114; *Megibow v. Commissioner*, T.C. Memo. 2004-41; *Nitschke v. Commissioner*, T.C. Memo. 2000-230; and *Ramsey v. Commissioner*, T.C. Memo. 1996-189.

[25] Small Business Jobs Act of 2010, section 2043(a), P.L. 111-240. The amendment is retroactive to tax years beginning after December 31, 2009.

section 62(c) or 132(d), the technical explanation of the provision empowered Treasury to use its common sense.[26] In 2017, Congress recognized again how technological progress has changed the world when it "de-listed" computers and peripheral equipment as part of tax reform.[27]

Shortly after cell phones were delisted, the IRS issued Notice 2011-72, 2011-38 IRB 407, which deemed the section 162 substantiation rules to be satisfied for purposes of the working-condition fringe benefit exclusion if the employer provides the cell phone (or other similar telecommunications equipment) for "noncompensatory business reasons." Moreover, if the device is provided for noncompensatory business reasons, any personal use of the cell phone is deemed to be excludable as a de minimis fringe benefit.[28] In short, the IRS figured out how to harmonize the tax rules with the fact that the cell phone can provide a personal benefit without having to determine whether the business use actually exceeded the personal use of the device.

We believe that the time has come for an analogous discussion of smartwatches. Given that they are increasingly supporting applications that provide real and meaningful health data to a wearer and the wearer's healthcare providers as well as other health benefits, such as fall detection, an analysis similar to cell phones may be appropriate. In other words, the value of such health benefits may justify treating the entire cost of smartwatches as deductible under section 213(d). That is true generally, but especially for anyone at risk for developing AFib and, in the future, for other conditions such as hypertension, hypoglycemia, and hyperglycemia, as new applications become better at detecting these conditions. Any ancillary uses of a smartwatch, such as receiving text messages, emails, and news alerts, are incidental when compared with the healthcare benefits that applications can provide. The tax treatment needs to keep pace with the technology, particularly when the healthcare benefit — such as detecting a life-threatening condition — outweighs the personal benefit of wearing a smartwatch. ■

[26]Joint Committee on Taxation, "Technical Explanation of the Tax Provisions in Senate Amendment 4594 to H.R. 5297, the 'Small Business Jobs Act of 2010,' Scheduled for Consideration by the Senate on September 16, 2010," JCX-47-10, at 25 (Sept. 16, 2010).

[27]Tax Cuts and Jobs Act, P.L. 115-97, section 13202(b). The amendment is effective for property placed into service after December 31, 2017.

[28]The IRS also issued a memorandum to its field examiners providing guidance on reimbursements for business use of personal cell phones, SBSE-04-0911-083.