



ONE-YEAR LIMITATION

BACKGROUND

Except for the break in assignment uncertainty, this IRS rule is reasonably straightforward and objective. The rule even makes some sense in that there needs to be some limit when the temporary location is really no longer temporary and becomes the true tax home. We understand that many smaller and/or less sophisticated staffing agencies may be unaware of the limitation or intentionally disregard it. However, failure to properly follow the limit could have significant tax, interest and penalty consequences to both employee and employer.

ONE-YEAR LIMIT

The tax rules provide that an away from home assignment will meet this *temporary* requirement (travel expenses not subject to income tax) if the assignment is expected to last less than one year, and does in fact last less than one year. If an assignment is extended for which it will then last more than one year, all transportation, meal & incidental per diem, and housing allowances and costs must be treated as taxable compensation beginning with expenses incurred when it becomes known that the one-year limit is anticipated to be exceeded; not just when the 366th day is reached. Expenses incurred and paid prior to when it is first anticipated the one-year limit will be exceeded do not need to be reclassified as compensation, but all future expenses must be treated as taxable compensation. The one-year limitation applies to the general work location, not just the same assignment, and would apply even if the traveler were employed by a different agency and continued to work in the same general area (within commuting distance of the current worksite or temporary lodging).

BREAK IN ASSIGNMENT

The IRS has specifically ruled that a break of three weeks away from the current assignment work location is too short to start over the counting on the one-year limitation. The IRS has also ruled that a break from the assignment location of seven months is long enough to restart the counting. Unfortunately, the IRS has provided no guidance for break lengths in between these two extremes. We believe a break in an assignment of 16 or more weeks may be adequate to restart the counting for the one-year limitation. The break may be for pleasure or another assignment or both as long as it is in a different location outside of typical commuting distance from the current assignment and the current temporary housing. In addition, there must be no written or oral understanding of returning to the assignment or assignment area during this break period; otherwise the assignment break will not start the counting over. As a result of some *seasonal* case law rulings, school-based assignments will not achieve a break in service for summer vacations.

STRATEGY

Assignments with extensions failing the one-year limitation will create taxable compensation subject to applicable payroll taxes on all the travel benefits once it is anticipated the one-year limit will be exceeded. Assignment extensions must be evaluated in light of this limitation. If the additional income tax burden (could approach or exceed a 40% tax rate) from the increased taxable income is deemed unacceptable and outweighs the intrinsic benefits of the current assignment or location, we will work with the traveler to find a temporary assignment in another location with the understanding that returning to the current assignment after at least 16 weeks will be uncertain and will depend on the client's staffing needs at that time. Alternatively, the final extension could be limited so that the multiple-extended assignment is less than a full year.

The information contained herein is general in nature and based on authorities that are subject to change. Tax information contained in this document is not intended to be used, and cannot be used, by any person as a basis for avoiding tax penalties that may be imposed by the IRS or any state. We recommend each taxpayer seek advice based on their circumstances from an independent tax advisor.