

Taxing travel reimbursements: Not all expenses are tax-free

The rules for reimbursing employees' travel expenses seem straightforward enough—employees account to you for their expenses, submit receipts for those expenses, and detail the business purpose of their trip. The accountable plan rules are your starting point; however, there's a lot more to consider.

Where the employee is traveling, the duration of their stay, and the primary purpose of the trip are all key factors in determining if travel expenses are taxable or not.

Tax home

You can reimburse employees for their travel expenses when they travel away from their tax home on business. Tax homes aren't employees' homes, unless they're working from home. Tax homes are employees' regular or main place of business.

Because employees' tax homes are their regular or main work locations, you can reimburse WFH employees when they come into the office for an occasional meeting. You can also reimburse them when they travel to clients' offices. Key: They regularly work from home.

Reimbursing hybrid workers is more challenging. It's not simply the number of days they're working at home vs. the number of days they're working in the office. This assessment is a combination of qualitative and quantitative factors:

- The total time they ordinarily spend in each place (quantitative).
- The level of their business activity in each place (qualitative).
- Whether their income from each place is significant or insignificant (quantitative).

What kind of travel is it?

Figuring out employees' tax homes is the easy part. There are two other key limitations you must consider before your reimbursements are tax-free.

Limitation #1: Temporary or indefinite assignment

Let's say you need to embed Alex, your employee, into a client's office for what you believe will be 10 months. Alex lives and works in Chicago and your client is located in Los Angeles. Alex's tax home is Chicago. His condo will be unoccupied while he's in L.A., so he'll incur twice the living expenses for those 10 months.

If Alex's assignment is *temporary*, he can be reimbursed for all of his L.A.-related travel expenses. If the assignment is *indefinite*, he eats those extra costs.

The IRS, of course, has **defined** temporary and indefinite. A temporary assignment is an assignment to a single location you realistically expect to last and does in fact last for one year or less. Reimbursements for temporary

assignments are 100% tax-free.

An indefinite assignment is an assignment that's not temporary. Reimbursements to employees for travel expenses related to an indefinite assignment are fully taxable. If you don't know from the get-go how long an employee's out-of-town assignment will be, it's indefinite. In addition, an employee's temporary assignment can easily be converted into an indefinite assignment if you fall into one of these traps:

- **Trap #1—things change:** Reimbursements become taxable once your realistic expectation changes. If, during the sixth month, it becomes apparent Alex will need to be in L.A. for 14 months, your reimbursements are taxable beginning with the sixth month.
- **Trap #2—successive assignments:** Reimbursements are taxable from Day 1, if Alex's L.A. assignment is broken up into a series of shorter-term assignments.

Limitation #2: Business only (or mostly)

Employees may only be reimbursed tax-free for their business travel.

Small break: Reimbursable business expenses include expenses related to the cost of a flight or a hotel room if those costs are reduced by a weekend stay-over at the beginning of a business trip.

No break: If employees extend their stay to vacation, expenses related to their personal time aren't reimbursable tax-free.

The opposite is also true—employees who work while they're on vacation can be reimbursed for those costs. Let's say Janet is vacationing with her family in Oahu and your company just signed an important client, also located in Oahu. You email her some confidential information she has to convey to the client in person right away. This doesn't convert Janet's entire vacation into a business trip, but you can reimburse her for her business-related expenses.