

Tax News

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Tax Rules Affecting Telecommuting

Increasingly, businesses across the country are finding that allowing employees to telecommute can be a win-win situation. Employees can gain more flexibility in their work life. Employers can reduce overhead expenses, secure talent beyond the business' immediate geographic vicinity, and even accomplish contingency planning objectives.

The value of these cost-saving measures and business enhancements are amplified during trying economic times. An overview of the federal tax rules applicable to telecommuters and those who employ them can help identify possible opportunities available when certain employees work off site.

Deducting Home Office Expenses

Types of Expenses. Federal income-tax rules generally categorize telecommuting expenses as either direct or indirect in nature.

Direct expenses are those that relate only to the portion of the telecommuter's home that is actually used as a home office. Such expenses may include improving or repairing the actual work space.

Indirect expenses may relate to both the personal portion of the home as well as the home office. Common examples of indirect expenses include real estate taxes, homeowner insurance premiums, and repairs benefiting the entire home.

Regular and Exclusive Use. Various tests must be satisfied in order for an employee to be able to deduct the direct expenses and the business portion of indirect expenses relating to a home office. The tax law requires that the home office be used regularly and exclusively as a principal place of business or as a place to meet or deal with customers or clients in the ordinary course of business.

As a practical matter, employees don't commonly use a home office to meet with clients. Accordingly, deductions may be limited to situations where the home office is used regularly and exclusively as the employee's principal place of business.

In situations where an employee works from home full-time, the principal-place-of-business test is usually

easily met. However, if one's time is split between the home and an outside office, federal tax rules generally state that the test is also satisfied if administrative or management activities are performed at the home office to the exclusion of other fixed locations.

For the Convenience of the Employer. An employee must also be able to show that the use of a home office is for the convenience of the employer. This test is generally considered to have been met if the employer requests that the employee work from home. Alternatively, this test is also considered satisfied if the employee is not in the office on a regular basis due to the nature of his or her work.

Ultimately, the "convenience" test is determined by the facts and circumstances of the employment arrangement. In general, if the employee requests to telecommute, it commonly results in not having satisfied the test. However, the particular circumstances may show that the arrangement was established for the benefit of the employer, despite the fact that the employee chose to telecommute. For example, if the employer looks for volunteers to telecommute for legitimate business purposes and the employee volunteers, that arrangement could qualify as being for the employer's convenience.

How Tax Benefits Are Claimed

If an employee qualifies to claim various deductions relating to the business use of a home office, he or she would do so on Schedule A, Form 1040, as a miscellaneous itemized deduction subject to a 2%-of-adjusted-gross-income (AGI) floor. Tax rules limit the ability of a taxpayer-employee to claim telecommuting expenses to the extent the business deductions exceed his or her gross income for the tax year.

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An employer may choose to reimburse an employee for expenses incurred relating to office supplies and equipment, as well as for utilities and maintenance expenses allocable to the home office (with the employer potentially claiming a deduction for the reimbursements). Or the employer may provide the telecommuting employee with necessary supplies and equipment and, accordingly, claim an ordinary business expense deduction.

As a general rule, it is advantageous for an expense or reimbursement arrangement to qualify as an “accountable plan.” Otherwise, adverse income-tax consequences may flow to both your business and the employee.

Computers and Other Equipment

If a telecommuting employee purchases a computer or other equipment and uses it exclusively for business-related purposes, he or she may depreciate or expense the item, subject to a 2%-of-AGI limitation. If, on the other hand, the employer provides such equipment, the employer may claim appropriate deductions as if the item were located in the employer’s regular offices.

Wholly unrelated expenditures, such as those relating to general landscaping or improving a room that is not used exclusively for home office purposes, are not deductible under the federal tax rules.

Doeren Mayhew Can Help

If we can be of assistance to you in understanding the tax issues surrounding telecommuting, please call the professionals at Doeren Mayhew at (248) 244-3000. We are here to help.



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