

Working in the Oilfields – How it impacts your Montana Income Tax

Montana/North Dakota Reciprocity Agreement

Montana has a reciprocity agreement with North Dakota that exempts a North Dakota resident who earns wages in Montana from paying Montana income tax on these wages. This agreement only extends to personal service income, such as salaries and wages, earned by a North Dakota resident. This agreement does not, however, extend to other types of income earned in Montana. A North Dakota resident may have to file an income tax return and pay Montana income tax on this other income.

If you are earning wages in Montana and you are a North Dakota resident, your income may be exempt from Montana withholding. To obtain the exemption from Montana withholding, complete Montana Form MT-R (new for 2013). This form must be completed on or before February 28 or within 30 days after you begin working or change your permanent residence to North Dakota. You must complete a new form and submit it to your employer each year to continue the exemption from withholding.

You can obtain this form from your employer or from the Montana Department of Revenue, PO Box 5805, Helena, MT 59604-5805. A copy of this form is also available online at revenue.mt.gov.

If your Montana employer has withheld Montana income tax from your wages and you wish to get a refund for it, you should file a Montana income tax return Form 2 as a non-resident, report the withholding amount, but do not include your wages. Mail these documents to the Montana Department of Revenue by April 15.

Employee Business Expenses

Q. I work in the oilfields. Can I deduct my travel expenses on my tax return?

The business expense deduction under Internal Revenue Code (IRC) Section 162(a)(2) includes deductions for mileage, meals, lodging and other travel expenses incurred while away from home in the pursuit of a trade or business.



Examples:

1. Joe Smith, a North Dakota resident, works in Montana and receives a W-2 at year's end with Montana withholding. Joe also owns and operates a business from which he receives partnership income.

Under the reciprocal agreement, Joe may receive a refund of his Montana withholding by filing a Montana income tax return Form 2.

The exemption, however, would only apply to the wages Joe received and his partnership income would be subject to Montana tax. The reciprocal agreement only applies to wages and does not extend to other income, such as business income or income received from a partnership or S-Corporation.

2. Bob Jones is a Texas resident and is staying in North Dakota. He works in Montana and receives a W-2 at year's end with Montana withholding. Bob, as a Texas resident (or if he was a resident of any state other than North Dakota) is not covered by the reciprocity agreement and must pay Montana income tax on the wages he earned in Montana. He therefore needs to file a Montana income tax return Form 2 as a non-resident.

(1) Reasonable and necessary

To demonstrate that expenses were reasonable and necessary under the circumstances, you must show that the expenses were necessary to the development of your or your employer’s business and are common or frequent in the type of business you’re conducting.

(2) Tax Home

To determine whether expenses were incurred away from home, it is necessary to determine the location of your tax home. Tax home should not be confused with residency or domicile, as tax home is a term used exclusively for purposes of interpreting IRC § 162(a).

The location of a taxpayer’s tax home, and thereby the deductibility of travel expenses, is dependent upon whether the taxpayer’s employment is **temporary** or **indefinite**.

If employment is temporary:	If employment is indefinite:
The tax home is located at the taxpayer’s residence and travel expenses are deductible if the taxpayer demonstrates the expenses meet the other two criteria.	The tax home is in the vicinity of the taxpayer’s principal place of business and travel expenses are nondeductible.

Generally, your tax home is your principal place of business or post of duty, regardless of where you maintain your family home and/or residence. It includes the entire city or general area in which your business or work is located.

If, however, you can prove that your employment is temporary, you may be able to deduct reasonable and necessary business expenses incurred in the pursuit of business traveling from your residence to your place of work. Employment is temporary when, at the time the job commences, termination is foreseeable within a short period. This period must last no more than one year. The taxpayer bears the burden to prove that his employment was temporary from the outset.

For a more comprehensive discussion on tax home, please see *Robison v. Mont. Dept. of Revenue*, 2012 MT 145, 365 Mont. 336, 281 P.3d 218.

(3) Pursuit of trade or business

To demonstrate that expenses were incurred in pursuit of a trade or business, you must demonstrate that the expense was required by the necessities of business and not personal preferences. Thus, there must be a direct connection between the expenditure and the carrying on of the trade or business of the taxpayer or of his employer. Such expenses must also be necessary or appropriate to the development and pursuit of the business or trade.

For additional information on the deductibility of various travel expenses, please see IRC Section 162, and Sections 1.262-1(b)(5) and 1.162-2(e) of the Income Tax Regulations.

Example:

Bob Doe resides in Nevada, but has worked for the same employer for several years in the oilfields of the Bakken formation. Bob works for ten days and then has four days off. Bob travels to Nevada to visit his family when he has his days off. When he began employment, Bob’s employer did not tell him how long he could expect to work for the company.

Because termination of Bob’s employment was not foreseeable within a short period, Bob’s tax home is located in the vicinity of his principal place of business in the Bakken formation, regardless of the fact that he is a resident of Nevada. Travel and meal expenses commuting to and from the rig are commuting expenses and therefore are not deductible as employee business expenses.

Moreover, there would be no business purpose to drive to the family home on days off. All of the related expenses would therefore be personal in nature and thus cannot be used as a basis for deduction. Therefore, all expenses (vehicle expenses, travel, and meals) incurred when traveling between his personal residence and his work location are nondeductible commuting expenses.

Questions? We encourage you to seek the advice of a tax practitioner regarding your particular tax situation. You can also contact the Montana Department of Revenue toll-free at (866) 859-2254.