

United States: IRS releases 2016 adjusted limitations for foreign housing exclusion or deduction

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In brief

The Internal Revenue Service (IRS) has issued Notice 2016-21 to provide adjustments to the foreign housing limitations provided under Section 911(c)(2)(B) of the Code. The adjusted limitations are based on geographical locations and are used to determine the maximum allowable annual housing exclusion or deduction for tax years beginning on or after January 1, 2016. Taxpayers may also elect to apply the 2016 adjusted limitations to tax years beginning in 2015. In practice, an increase in the limitation for a particular location may result in more favorable Section 911 tax benefits for those assignees residing in such locations, depending upon their specific situations – a potentially welcome result for global mobility programs.

The IRS releases this information on an annual basis. Notice 2016-21 supersedes previously released notices, including Notice 2015-33.

In detail

What is the maximum housing exclusion?

Under the general rules of Section 911, a qualified individual may elect to exclude from gross income his or her foreign housing cost amount. However, the housing cost amount is limited. Without any adjustments to the limitations, the maximum foreign housing exclusion is \$14,182 assuming the qualified individual's taxable year is entirely within the applicable period. This limitation is based on the annual foreign earned income

exclusion limitation and is calculated as follows:

- **Housing expense limitation = \$30,390** (\$101,300 x 30%)
- **Less: Base housing cost of \$16,208** (\$101,300 x 16%)
- **Maximum housing exclusion = \$14,182** (\$30,390 - \$16,208)

Note that this amount should be prorated if the individual only qualifies for part of the year. Notice 2016-21 was published to increase the housing expense limitation (the \$30,390 amount noted in the formula above) for

geographic areas with higher housing costs when compared to housing costs in the United States.

What are some key observations?

The following are a few key observations from this year's adjusted limitations:

- Six new locations have been added to the 2016 list. They include Butzbach, Germany; Koblenz, Germany; Conakry, Guinea; Muscat, Oman; Ljubljana, Slovenia; and Huntingdon, United Kingdom.

- In a number of countries, smaller cities whose housing costs are generally higher than the standard – but are not specifically listed with a housing expense limitation amount may fall under a catch all for ‘all cities other than,’ with a corresponding housing expense limitation provided. In this way, these cities are provided with an expense limitation that is higher than the general limitation amount. This year, Korea, Italy, and Norway no longer have this catch-all category. Thus, smaller cities not specifically listed will no longer be eligible for higher expense limitations.

- More cities than usual were eliminated in this year’s list (as compared to 2015). They include:

Darwin, Northern Country, Australia
Antwerp, Belgium
Hoogbuul, Belgium
Brasilia, Brazil
Dartmouth, Canada
Edmonton, Canada
Halifax, Canada
Victoria, Canada
Le Havre, France
Bad Aibling, Germany
Bad Nauheim, Germany
Friedberg, Germany
Gieselstadt, Germany
Kitzingen, Germany
Wertheim, Germany
Wuerzburg, Germany
Catania, Italy
Leghorn, Italy
Pisa, Italy
Sigonella, Italy
Camp Caroll, Korea
Uijongbu, Korea
Waegwan, Korea
Stavenger, Norway

As a result, those cities must use the regular 2016 housing expense

limitation amount unless there is a catch all for ‘all cities other than’ that applies. If a city is not specifically listed and there is a catch-all category ‘all cities other than’ for that country, taxpayers should check that category to see if they are able to claim a higher expense amount.

As an example, Halifax in Canada was listed in 2015 but was removed from the 2016 list. Because there is no category in Canada for ‘all cities other than,’ a taxpayer resident in Halifax must use the regular 2016 housing expense limitation.

- Eleven Japanese cities saw the same modest \$700 increase to the limitation on housing expenses from \$35,600 in 2015 to \$36,300 in 2016. These include Atsugi, Camp Zama, Chiba-Ken, Fussa, Haneda, Kanagawa-Ken, Machidi-Shi, Sagamihara, Saitama-Ken, Tachikawa, and Tokyo-to. But limitations for other Japanese cities had moderate reductions including Tokyo which went from \$83,500 down to \$81,300. Doha, Qatar and Pyongtaek, Korea also saw increases.
- Many countries had a widespread drop in the limitations for some or all their listed cities. These include Australia, Belgium, Canada, Chile, France, Germany, Greece, The Holy See, Ireland, Italy, Korea, Luxembourg, Netherlands, Norway, the Philippines, Portugal, Qatar, Singapore, Spain, Switzerland, and the United Kingdom.
- Five cities in France had the largest decrease in the housing limitation amount from \$78,300 in 2015 to \$68,600 in 2016 – a

drop of \$9,700. These cities include Garches, Paris, Sevres, Suresnes, and Versailles. Zweibrueken, Germany also incurred a \$9,700 decrease (from \$50,900 in 2015 to \$41,200 in 2016.)

- Milan, Italy had a decrease of \$9,600 (from \$77,900 in 2015 to \$68,300 in 2016.) Sydney, Australia had a decrease of \$8,600 (from \$70,000 to \$61,400). Montreal and Toronto in Canada also had decreases of \$8,100 and \$8,300 respectively. Madrid in Spain also dropped from \$63,600 to \$55,700.
- Hong Kong, China continues to have the highest limitation of \$114,300, which remains unchanged from last year's limitation amount.

The takeaway

It is important that taxpayers make no assumptions about the housing expense limitation from year to year. Cities come on and off the list based on housing costs annually – resulting in significant increases and decreases to expense limitations. Notice 2016-21 should be consulted to ensure that the appropriate housing expense limit has been taken into account.

The US tax reductions attributable to Section 911 can provide an important benefit for multinational companies that tax equalize their employees working overseas. Practitioners should be aware of the additional relief provided under Notice 2016-21 for US citizens and residents who qualify for the foreign housing exclusion or deduction under Section 911.

It is important to note that taxpayers should consider whether Section 911 as compared to the foreign tax credit will provide the greatest tax benefit – an often complex determination due to the various limitations.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact your PwC Global Mobility Services engagement team or one of the following professionals in the United States:

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