Tzinberg & Associates, P.C.
certified public accountants

ACCOUNTABLE PLANS

Employee information regarding how to claim deductions for expenses you incur in connection with your employment. These expenses include those for local transportation (other than commuting), business meals and entertainment (at 50% of cost), travel away from home, supplies, education, etc.

The tax treatment of these items depends on the arrangement you have with your employer. In particular it depends on whether you are reimbursed for your costs and, if so, under what type of arrangement.

No reimbursements. If your employment-related expenses aren't reimbursed by your employer they are deductible, but only as a “miscellaneous itemized deduction.” This means they are lumped together with other miscellaneous items (e.g., investment expenses, tax return preparation costs) and are only deductible as an itemized deduction to the extent the total exceeds 2% of your adjusted gross income (AGI). This is known as the 2% “floor.” Thus, depending on your AGI and your other miscellaneous deductions, you may lose all or part of your employee expense deduction.

“Accountable” reimbursement plans. An accountable plan is one under which your employer reimburses you for your employment-related expenses (or pays you an expense allowance) but requires you to “adequately account” for the expenses. This means you must submit a record of the expense to the employer (account book, diary, expense statement, etc.) along with receipts and other documentation indicating the expense amount, time and place, business purpose, and business relationship to anyone else involved (e.g., a client, supplier, etc.).

For the plan to qualify as an accountable plan, it must also require you to pay back any excess payments you receive. For example, say you receive $1,000 under an expense account arrangement and only incur $800 in expenses. In order for the plan to qualify as accountable, it would have to require you to return the $200 not spent.

If you are reimbursed (or receive an allowance) for expenses under an accountable plan, the tax treatment is simple: do nothing. The transaction is treated as a wash. The reimbursement or allowance should not be included in your income on the W-2 form you receive from your employer and you don't take a deduction for the expense.

If your employer only reimburses (or gives you an allowance for) part of your costs, you can claim a deduction for the excess expenses that actually came out of your pocket. In this case, however, the expenses are only deductible as a miscellaneous itemized deduction, as discussed above.

Nonaccountable reimbursement plans. If your employer doesn't maintain an accountable plan, expense reimbursements or allowances you receive from your employer, if any will be included in your wages on the W-2 form you receive from the employer. You then separately deduct your expense as a miscellaneous itemized deduction, again, however, subject to the “2% floor” described above. This system may operate unfairly from your perspective.

Example: Ellen is paid $50,000 in wages. Her adjusted gross income is $60,000 and her employee expense is her only miscellaneous itemized deduction. She incurred $1,000 in employment-related expenses and was reimbursed the full amount by her employer but not under an accountable plan. Her W-

2 form will show $51,000 in total wages received, including the reimbursement. Since her miscellaneous total was less than 2% of her AGI ($1,020), she gets no deduction.

Planning approaches. If you are in a situation in which the 2% floor is denying you your expense deductions, there may be ways to change your situation to take care of the problem. If you receive reimbursements or allowances, your employer might be willing to put an accountable plan in place. Alternatively, the employer may be willing to cover the costs directly, rather than having you pay the expenses.

If you don't receive reimbursements or allowances, you might still be able to convince your employer to cover the costs directly if you are willing to take a reduction in salary to offset the employer's additional cost. You will be in the same economic position (the expenses come out of your pocket), but you're in a better tax position because the reduced salary will save you taxes, unlike incurring the expense which didn't.