



Is Your Reimbursement Plan Hurting You?

By Rebecca M. Shull, MSA, CPA

Clifford & Associates

<http://www.sharetheharvest.com> 1-800-456-1803 rebeccas@sharetheharvest.com

The IRS categorizes reimbursement plans into the following two types:

I. Accountable Plans

Employees under an accountable plan must turn in logs and receipts to substantiate their expenses at least every 60 days. The employer only reimburses substantiated expenses. The employee does not receive any monies remaining in the reimbursement fund at year-end. Reimbursements under an accountable plan are tax-free to employees and do not appear on Form W-2.

2. Nonaccountable Plans

Reimbursements under a nonaccountable plan are taxable income to employees and should be included in box 1 of Form W-2. The employee must itemize to claim business expenses on his or her tax return. Expenses are claimed as a miscellaneous deduction on Schedule A subject to a threshold of 2% of adjusted gross income. Clergy are subject to an additional limitation, called the "Deason Rule." The Deason Rule states that the percentage of unreimbursed expenses that

are attributable to housing (housing ÷ total ministry income) are not deductible.

For example, consider the cases of Pastor A and Pastor Z in the illustration below. Pastor A's church has an accountable plan, so Pastor A receives reimbursement of \$4,000, tax-free. Pastor Z receives a \$4,000 travel allowance from his church under a nonaccountable plan. The allowance is taxable income included in box 1 of Pastor Z's Form W-2 from the church. Note that Pastor Z ends up paying **substantially more taxes**.

| INCOME: | Pastor A | Pastor Z | |
|--|----------|----------|-------------------|
| Salary | \$20,000 | \$20,000 | |
| Housing | 10,000 | 10,000 | |
| Nonaccountable Travel Allowance | | 4,000 | |
| Total Income | \$30,000 | \$34,000 | |
| Adjusted Gross Income (AGI) | \$17,880 | \$21,880 | |
| EXPENSE: | | | |
| Mileage | 8,000 | 8,000 | |
| IRS 2010 Reimbursement Rate Per Mile | 0.50 | 0.50 | |
| Clergy Mileage Expense | \$4,000 | \$4,000 | |
| Accountable Reimbursement (Tax Free!) | \$4,000 | | |
| 29% Disallowed by Deason Rule (10000/34000) | | 1,160 | |
| | | 2,840 | |
| 2% of AGI Threshold | | 438 | |
| Itemized Deduction | | \$2,402 | |
| TAXES: | | | |
| Self-Employment Tax | \$4,239 | \$4,239 | |
| Federal Income Tax | 861 | 1,461 | |
| State Tax | 237 | 363 | |
| City Tax | 400 | 480 | Difference |
| Total Tax if Unable to Itemize | \$5,737 | \$6,543 | \$806 |
| Total Tax if \$13,000 of Other Itemized Deductions | \$5,000 | \$5,366 | \$366 |