Division of Accounting
Payroll Compliance Group

Bulletin # 2016_001
Moving Expenses Fringe Benefits
(Qualified and Nonqualified Reimbursements)

INTRODUCTION

The Division of Accounting (DOA) is responsible for working with State of Delaware (State) Organizations to ensure appropriate application of regulations associated with fringe benefits offered to State employees.

This bulletin provides guidance on the tax implications of employer-paid moving expenses for a newly-hired employee to ensure proper communication with the employee at the time of receipt of the fringe benefit and that the State is in compliance with federal and state tax laws and regulations.

FACTS

Fringe benefits include any compensation other than cash wages. The general rule is that the compensation is taxable; however, the Internal Revenue Code provides exclusions for numerous forms of non-cash compensation provided to employees.

There is specific statutory guidance on the topic of moving expenses. Reimbursements must conform to the rules of accountable plans. Tax determinations are made based on rules for working condition fringe benefits and business deductions (see definitions below) and how expenses are substantiated.

DEFINITIONS

- **Working condition fringe benefits** include property or services that, if the employee had paid for the property or service, the cost would have been deductible on the employee's individual income tax return. Therefore, if the cost of an item is deductible by an employee as a business expense, it <u>may</u> be excludable from the employee's wages as a working condition fringe benefit if provided by the employer. *IRC §132(d)*

- **Accountable Plan** – a plan that meets the requirements as specified by the IRS. *IRC §162; Reg. §1.62-2(c)(1)*

    - Reimbursed expenses paid in connection with the performance of services for the employer.
    - The employee substantiates the reimbursed expenses to the employer within a reasonable time.
    - The employee returns amounts paid by the employer that exceed substantiated expenses.

- **Non-accountable Plan** – a payment or reimbursement arrangement that does not meet requirements of an accountable plan – payments under such plans are wages and subject to withholding.

- **Qualified Moving Expenses:**

  - Moving household goods and personal effects (including in-transit storage expenses), and
  - Travel for the employee and family (including lodging) from the old home to new home.

- **Qualified Reimbursement** – Reimbursement of moving expenses that meet both the IRS distance and time tests (described below).

- **Non-Qualified Reimbursement** – Reimbursement of moving expenses that are taxable to the employee because the IRS distance and time tests were not met.

FINDINGS

Employers may pay for any relocation expenses of an employee; but, only reimbursements for expenses that qualify as deductible can be excluded from the employee's income. All other expenses paid or reimbursed are subject to withholding for federal, state, and local income; OASDI; and Medicare taxes.

For relocation expenses to be qualified moving expenses, the employee must meet three tests:

1. The move is closely related to the start of the employee's work.
2. The location of the employee's new home meets the distance test.
3. The individual's employment actually or potentially meets the time test.

Closely Related to the Start of Work:

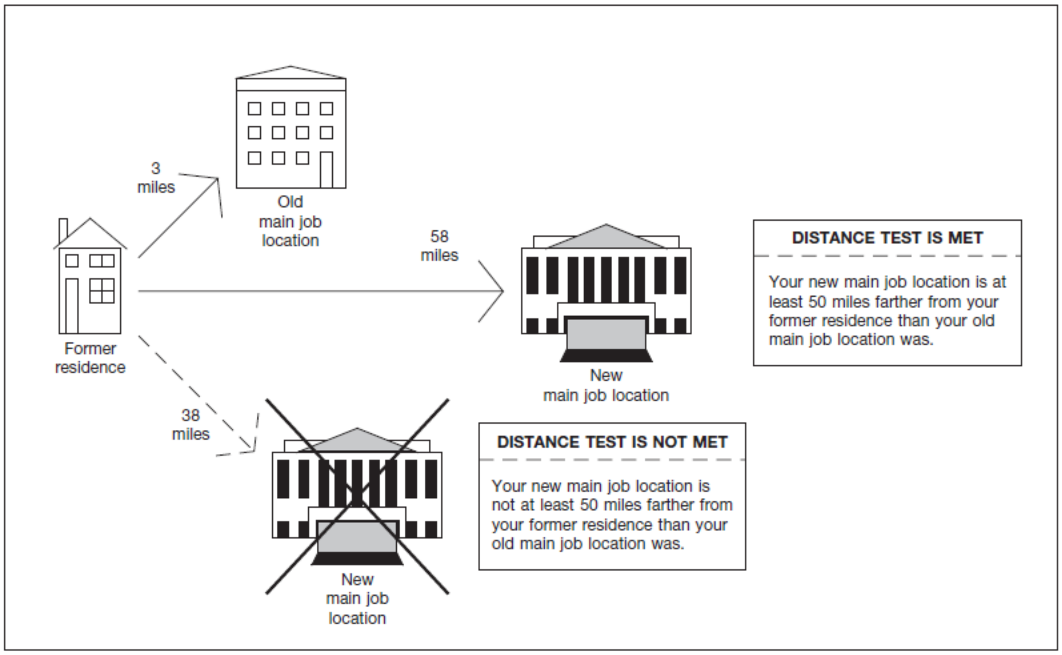
For any relocation costs to be Qualified Moving Expenses, the move must be closely related to the start of work in a new location. The move must occur within one year of when the employee starts working for the State. Either the move must have been required by the State because the employee is required to live near the place of employment; or, the commuting time from the new residence is shorter than the commute time from the old residence.

NOTE: If an individual relocated before obtaining a job with the State, the moving expenses may still qualify for tax-free reimbursement as long as the employee started working for the State within one year of the move.

Distance Test:

For any relocation costs to be a qualified expense, the move must meet the distance test which is based on the location of the former home, the location of the old place of work, and the location of the new place of work. The new place of work must be at least 50 miles further from the old residence than the old place of work was from the old residence. See the illustration below from IRS Publication 521 – Moving Expenses.

Figure A. Illustration of Distance Test



Distance Test Calculation

1. Enter the number of miles from the former home to the new workplace _____miles
2. Enter the number of miles from the former home to the old workplace _____miles
3. Subtract line 2 from line 1. If zero or less, enter -0-…………………… _____miles
4. Is line 3 at least 50 miles?

☐ Yes. Distance test met.

☐ No. Distance test not met. Moving expenses are not deductible.

Time Test:

Employee must work full-time at least 39 weeks during the first 12 months after arriving in the general location of the new job.

Moving expenses must be reasonable; but, the definition of reasonable is not specifically defined. IRS Publication 521 indicates that expenses are reasonable if the cost of traveling from the former home to the new one is by the shortest, most direct route available by conventional transportation. Where the regulations refer to members of an employee's household, it means individuals who lived with the employee in the old home and are relocating with the employee to the new home.

The following moving expenses are considered to be reasonable and deductible:

1. The cost of packing, crating, and transporting household goods and personal effects and those of members of the household from the former home to the new one. A professional moving company can be used, or the employee may use his own vehicle for moving some items.

2. The cost of storing and insuring household goods and personal effect within any period of 30 consecutive days after the employee's things have been moved from his former home and before they are delivered to the employee's new home.
3. The cost of connecting or disconnecting utilities.
4. The cost of shipping an employee's car or pets to his new home.
5. The cost of moving household goods and personal effects from a place other than the employee's former home, but the deductible portion is limited to the amount it would have cost to move it from the employee's old home.
6. The cost of transportation and lodging for the employee and members of the employee's household while traveling from the former home to the new home. Lodging expenses include the cost of lodging for one day after the employee could no longer live in his old home and expenses incurred on the day the employee arrives in the area of his new home. Transportation expenses include parking fees and tolls paid for driving from the former home to the new home.
7. If an employee uses his own vehicle, or if additional personal vehicles are driven to relocate the employee's family, mileage is reimbursable at the rate published in IRS Publication 521.
8. All expenses are for one trip by the employee and the employee's household, although the employee and the members of his household do not have to travel together or at the same time.

Because employees may not deduct the following items as moving expenses, if any of these items are reimbursed, the value is taxable.

1. Any part of the purchase price of the new home.
2. Car tags and driver's license.
3. Buying/selling home expenses (closing costs, mortgage fees/penalties, points, real estate taxes).
4. Expenses of entering into or breaking a lease including security deposits.
5. Home improvements to help sell your home.
6. Loss on the sale of the home.
7. Losses from disposing of club memberships.
8. Pre-move house hunting expenses.
9. Refitting of carpet and/or draperies.
10. Return trips to the former address.
11. Storage charges except those incurred in transit.

Tax Reporting Requirements

Employers may pay all or some of the employee's moving expenses directly, such as paying a moving company to move the employee's household goods and personal effects. (Qualified moving expenses paid directly to a third-party are not reported on Form W-2.) Or, the employer may choose to reimburse the employee for all or some of his moving expenses. Employers should provide employees with a statement breaking down all payments included in the reimbursement.

When the reimbursement for qualified moving expenses is paid to the employee, the amount is reported in Box 12 of Form W-2 with the Code "P." When the reimbursement is for nondeductible (non-qualified) moving expenses, the amount is reported in Box 1, 3, and 5 of Form W-2 and income taxes, social security, and Medicare taxes are withheld.

Every individual who receives moving expense reimbursements must complete Form 3903 and attach it to Form 1040. An employee reimbursed for all qualified expenses must report that on Form 1040 and may not deduct the expenses. If the employee later relocates and invalidates the time test, the qualified expenses reported on Form W-2 in Box 12 must be included in income in the year the employee invalidates the time test. The employee must then file an amended Form 1040 for the year the original reimbursement was paid.

REGULATORY REFERENCES

In rendering this opinion, we reviewed the applicable Code, Regulations, and laws as cited below.

IRS Publication 15-B (2012) – Employer's Tax Guide To Fringe Benefits

http://www.irs.gov/publications/p15b/ar02.html

IRS Publication 521 – Moving Expenses – For use in preparing 2016 Returns

https://www.irs.gov/pub/irs-pdf/p521.pdf

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