



OFFICE OF THE CHIEF COUNSEL

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
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The Honorable Joe Donnelly
Member, U.S. House of Representatives
207 West Colfax
South Bend, IN 48601

Attention:

Dear Congressman Donnelly:

I apologize for the delay in responding to your inquiry dated June 29, 2010, on behalf of your constituent, . asked about the tax treatment of reimbursed union dues. is an officer in a local janitor's union. He pays dues, and the union reimburses him for the amount of the dues.

Taxpayers can deduct all ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business (section 162(a) of the Internal Revenue Code (the Code)). The taxpayer can deduct dues and other payments, which otherwise meet the requirements of the regulations under section 162 of the Code, to organizations such as labor unions (section 1.162-15(c) of the Income Tax Regulations).

If an employee incurs a deductible expense while performing services for his or her employer, reimbursement of the expense is taxable unless the reimbursement is made under an accountable plan. The accountable plan rules apply only for reimbursements to employees. Amounts treated as paid under an accountable plan are excluded from an employee's gross income. The employer does not report these amounts as wages on the employee's Form W-2, and they are exempt from withholding and payment of employment taxes. Conversely, employers must include amounts treated as paid under a nonaccountable plan in the employee's gross income and must report them as wages or other compensation on the employee's Form W-2. These amounts are subject to withholding and payment of employment taxes.

An accountable plan is a reimbursement or other expense allowance arrangement that meets the requirements of business connection, substantiation, and return of excess (section 62(c) of the Code and section 1.62-2(c) of the Income Tax Regulations). Publication 15 (Circular E), *Employer's Tax Guide* has information on accountable plans.

Business Connection Requirement

An arrangement meets the business connection requirement if the employer pays advances, allowances, or reimbursements only for deductible business expenses that the employee pays or incurs while performing services for the employer. If, however, an employer pays an employee regardless of whether the employee incurs (or is reasonably expected to incur) bona fide business expenses, the arrangement does not satisfy the business connection requirement and the amounts are treated as paid under a nonaccountable plan and are subject to employment taxes. An employer may not treat as a nontaxable expense reimbursement an amount that he or she would otherwise pay as wages.

Substantiation Requirement

To meet the substantiation requirement, an arrangement must require the employee to substantiate each business expense to the payor within a reasonable period of time. The employee must submit enough information to allow the employer to identify the specific nature of each expense and attribute the expense to the employer's business activity. Generally, the employee must submit an expense account or other written statement to the employer showing the business nature and amount of each of his or her expenses. Combining expenses into broad categories or reporting individual expenses using vague, non-descriptive terms such as "miscellaneous expenses" is not sufficient.

Return of Excess Requirement

To meet the return of excess requirement, the employee must return to the employer within a reasonable period of time any amount the employer paid in excess of the employee's substantiated expenses.

I hope this information is helpful. If you have any questions, please contact me or
, Identification Number , at .

Sincerely,

Thomas D. Moffitt
Chief, Branch 2
Office of Associate Chief Counsel
(Income Tax & Accounting)