



Military Adjustments to Income



Introduction

This lesson will help you determine which members of the U.S. Armed Forces are entitled to an adjustment to income for certain business expenses or moving expenses. To do this, you will need to determine certain business expenses, qualifying moves, allowances and reimbursements, and deductible moving expenses.

To determine if the taxpayer has incurred any of these expenses, it is important to ask probing questions during the taxpayer interview.

Business expenses for Armed Forces reservists are deducted on Form 2106, Employee Business Expenses.

Unreimbursed moving expenses are deducted using Form 3903, Moving Expenses. Armed Forces members receive a variety of moving reimbursements and allowances that must be considered when determining if the expenses are deductible. The travel voucher will contain much of the information needed to compute the deduction. To deduct moving expenses, the taxpayer **must** be a member of the Armed Forces on active duty and the move is because of a permanent change of station.

See Publication 3, Armed Forces Tax Guide, for additional information on the topics discussed in this lesson.

Objectives

At the end of this lesson, using your resource materials, you will be able to:

- Determine if a taxpayer has military business expenses that can be deducted
- Determine if a move qualifies as a permanent change of station (PCS)
- Identify deductible moving expenses
- Determine when allowances and reimbursements must be included in income

What do I need?

- Form 13614-C
- Publication 4012
- Publication 3
- Form 2106
- Form 3903
- Optional:**
- Form 1040 Instructions

What are military employee business expenses?

Military employee business expenses are necessary work-related expenses incurred by active and reserve members of the U.S. Armed Forces. The U.S. Armed Forces includes commissioned officers, warrant officers, and enlisted personnel in all regular and reserve units under the control of the Secretaries of the Defense, Army, Navy, Air Force, and Coast Guard. Ready Reserve Corps of the Public Health Service (part of HHS) is also included as a reserve component. It does not include members of the Merchant Marines or the American Red Cross.

What are temporary active duty reservists' expenses?

Military reservists temporarily called to active duty who must remain away from home to perform their duties may claim unreimbursed travel expenses such as meals and lodging. This applies:

- As long as the duty occurred under competent orders and
- Whether or not the reservist was compensated

To claim unreimbursed travel expenses, reservists must be stationed away from the general area of their job or business and return to their regular jobs once released. Expenses are deductible only if the reservists pay for meals and lodging at their official military post and only to the extent the expenses exceed Basic Allowance for Housing (BAH) and Basic Allowance for Subsistence (BAS). This includes any reimbursement reported under Code L in Box 12 of Form W-2.

What is the 100-mile rule for reservists?

Military reservists who must travel more than 100 miles away from home and stay overnight to attend a drill or reserve meeting may be able to deduct their travel expenses as an adjustment to income. The amount of expenses that can be deducted is limited to the:

- Federal rate for per diem (for lodging, meals, and incidental expenses)
- Standard mileage rate (for car expenses) plus any parking fees, ferry fees, and/or tolls

example

Mary is in the Army Reserve. She lives in a town that is 120 miles from Base A, where she normally reports for reserve drills or meetings. During the current tax year, she occasionally traveled to Base B, which was only 40 miles from her home. Mary can claim the travel expenses she incurred going to Base A as an adjustment to income. She cannot claim the expenses for Base B as an adjustment.

What is a permanent change of station?

Moving expenses incurred as a result of a permanent change of station (PCS) are deductible only.

A permanent change of station includes a move from:

- Home to the area of the first post of duty.
- One permanent post of duty to another.
- The last post of duty to home or to a nearer point in the U.S. The Armed Forces member must move within one year of ending active duty or within the period allowed under the Joint Travel Regulations.

What does a permanent change of station include for spouses and dependents?

If the Armed Forces moves service members and their spouses or dependents to or from separate locations, the moves are treated as a single move and the qualified expenses of both moves are combined and deducted on the same tax return.



EXERCISES

Answers are at the end of the lesson summary.

Question 1: Which of the following is a permanent change of station?

- A. A move by an Air Force pilot to an airbase for a six-month detail
- B. A move by an Army sergeant to his home two years after he ended active duty
- C. A move by a new enlistee from her home to her first post of duty
- D. A temporary move by a U.S. Marine to attend a six-month training program

What expenses are included in the moving expense adjustment?

Qualifying military moving expenses fall into the following two categories, the cost of:

- Moving household goods and personal effects
- Reasonable travel and lodging expenses

To qualify as “reasonable,” the route taken must be the shortest, most direct route available, from the former home to the new home. Additional expenses for stopovers, side trips, or pre-move house hunting expenses are not deductible as moving expenses.

Qualifying expenses that exceed government allowances and reimbursements are deductible.

How do I handle military reimbursements?

Determine whether any moving allowances or reimbursements provided by the government should be included in a service member’s income, and how to accurately report the deduction on Form 1040.

What is a Personally Procured Move (PPM)?

Typically, Armed Forces members move their own household items in a personal or rented vehicle; this is called a Personally Procured Move (PPM), formerly known as a Do-It-Yourself (DITY) move. The Armed Forces provides an incentive payment equal to 95% of the estimated cost to the government for PPM. When the move is completed, the Armed Forces member provides receipts and paperwork to substantiate authorized expenses. The net financial profit is taxable and is reported on a separate Form W-2.

How do I report a PPM?

PPM payments are reported on Form W-2 and are entered as wages on Form 1040.

Armed Forces members may not take a moving expense deduction based on the expenses approved by the finance office when settling the PPM, as they have already been used to reduce taxable income.

example

Captain Cook receives orders for a PCS. He chooses to pack and drive his household goods to the new duty station in his own vehicle. The Air Force estimates that the move would have cost the government \$2,500. Captain Cook’s actual expenses for the move were \$1,750. He receives a payment for \$2,375 (95% of the government’s estimate), but Form W-2, Box 1, will show only \$625 (\$2,375 minus \$1,750) for the PPM. Captain Cook cannot deduct any of his expenses, since he’s already been reimbursed.

What forms of reimbursement are *not* included as income?

Certain forms of reimbursement provided by the government are *not* to be included as income on the Armed Forces member’s tax return.

- Moving or storage services furnished to the Armed Forces member
- Nontaxable allowances such as:
 - Dislocation allowance
 - Temporary lodging allowance
 - Mileage allowance in lieu of transportation
 - Per diem allowance
 - Move-in housing allowance (MIHA)



EXERCISES (continued)

Question 2: Sgt. Bishop received Form W-2 for \$1,000 as a result of a PPM to a new Permanent Duty Station (PDS). In addition, the government paid her a mileage allowance of \$300, a lodging allowance of \$200, and a dislocation allowance of \$1,200. How much should Sgt. Bishop include in her wages on Form 1040?

- A. \$1,500
- B. \$1,000
- C. \$300
- D. \$200

How do I calculate the adjustment?

Deductions can only be claimed for expenses not covered by a nontaxable reimbursement or moving allowance. If the taxpayers have allowable expenses that exceed the amount they were reimbursed, Form 3903 should be completed. Form 3903 is not needed if all the taxpayers' reimbursements were nontaxable allowances that were greater than their expenses.



Tax Software Hint: The tax software addresses the Armed Forces PCS move and calculates the standard mileage amount based on miles traveled for the move. See the Volunteer Resource Guide for the standard mileage rate.

Taxpayer Interview and Tax Law Application

Here's how a volunteer could help Mrs. Fannin determine if she had any deductible moving expenses:

SAMPLE INTERVIEW

VOLUNTEER SAYS...

You said you just moved here during June of this year. Was this a PCS move?

If your expenses were more than the Armed Forces reimbursement, you may be able to use the difference to reduce your gross income. We'll complete Form 3903 to see how it comes out. Did you bring your travel voucher with you?

Did you drive directly here, or did you take any side trips?

MRS. FANNIN RESPONDS...

Yes, my husband was transferred here in March, shortly before he deployed. I have family close by, so I'd rather stay here while he's overseas.

It's right here. We drove our own car 1,000 miles to get here, and paid \$120 for gas. We paid \$300 for motels and \$135 for meals on the way. The military moved our household goods, and we didn't have any overweight.

We came right here so we could settle in before he deployed.

SAMPLE INTERVIEW

VOLUNTEER SAYS...

MRS. FANNIN RESPONDS...

The IRS will let you use the standard mileage rate for a military move. To determine the standard mileage rate, let's look at Publication 4012 and multiply the rate times the number of miles.

Okay.

The IRS allows lodging costs, but not food. So your total allowable expenses includes \$300 for the motels and your mileage expenses. The travel voucher shows a total of \$400 in reimbursements – did you receive any other reimbursements or allowances?

No, that's it.

Then you'll get to deduct the amount you spent that was more than your reimbursement.

[On the intake and interview sheet, be sure to note that you've addressed this adjustment.]

When should an Armed Forces member claim the deduction?

Armed Forces members who use the cash method of accounting (the most common) and have qualified expenses exceeding their reimbursement can deduct the expenses either in the year they paid them or in the year reimbursement was received. If taxpayers choose to deduct their moving expenses in the year of reimbursement, they can deduct:

- Expenses paid in a year before the year of reimbursement, or
- Expenses paid in the year immediately after the year of reimbursement but by the due date, including extensions, for filing the return for the reimbursement year.

If expenses are deducted and reimbursement is received in a later year, the reimbursement must be included in income.



EXERCISES (continued)

Question 3: In November of the current year, Petty Officer Wharton moved from California to Washington. The move qualified as a PCS. He incurred \$800 in mileage expenses and \$1,600 in lodging. He paid \$1,400 to ship household goods over the allowed weight limit, and \$500 to ship his dog. The following year, he filed his travel voucher and received \$2,400 mileage and travel allowance. He also received a \$1,500 dislocation allowance.

For what tax year(s) can Petty Officer Wharton claim his moving expenses on Form 3903?

- A. Next year only
- B. Current year only
- C. Either current year or next year

Taxpayer Interview and Tax Law Application

Amanda was relocated to another Air Force base. Here's how a volunteer could help Amanda determine if she had any deductible moving expenses:

SAMPLE INTERVIEW

VOLUNTEER SAYS...

So, you were transferred from Maxwell Air Force Base to Scott Air Force Base last year, right?

Did you receive any other allowances?

Well the reimbursements were not reported on your W-2. You can only deduct expenses that are larger than your combined reimbursements and allowances. First, let's add all your qualified expenses. How much was your travel and lodging?

Any other expenses?

Only the travel and lodging en route can be claimed on Form 3903. The security deposit and meals are not deductible expenses. Your reimbursement and dislocation allowances add up to \$1,400. Since that's more than your expenses, you don't have anything to deduct. But, you don't have to include any of the excess reimbursement as income, either.

AMANDA RESPONDS...

Yes, I was reimbursed \$400 for travel expenses on the way to Scott Air Force Base.

Yes, I also received a \$1,000 dislocation allowance.

I spent \$575 on travel and lodging and another \$200 for meals along the way.

Yes, I gave a \$350 security deposit to my new landlord.

Summary

This lesson described the types of expenses that members of the Armed Forces can deduct as an adjustment to income. These expenses are deductible on Form 1040, Schedule 1.



TAX LAW APPLICATION

To gain a better understanding of the tax law, complete the practice returns(s) for your course of study using the Practice Lab on L<.

You may not be able to complete the entire exercise if some of the technical issues in the exercise are not covered until later lessons. In these instances, complete as much of the exercise as you can. Come back later to finish the exercise after you cover all the technical topics.



EXERCISE ANSWERS

Answer 1: C. A move by a new enlistee from her home to her first post of duty is considered a PCS.

Answer 2: B. The \$1,000 PPM payment should be included as wages. However, nontaxable allowances such as dislocation allowances, temporary lodging allowances and mileage allowances provided by the Armed Forces should not be included as gross income on the service member's tax return, even if they exceed allowable expenses.

Answer 3: C. Because Petty Officer Wharton paid for moving expenses in the year prior to the year of reimbursement, he can claim all of his moving expenses on Form 3903 in either the year he paid or the year he was reimbursed.