



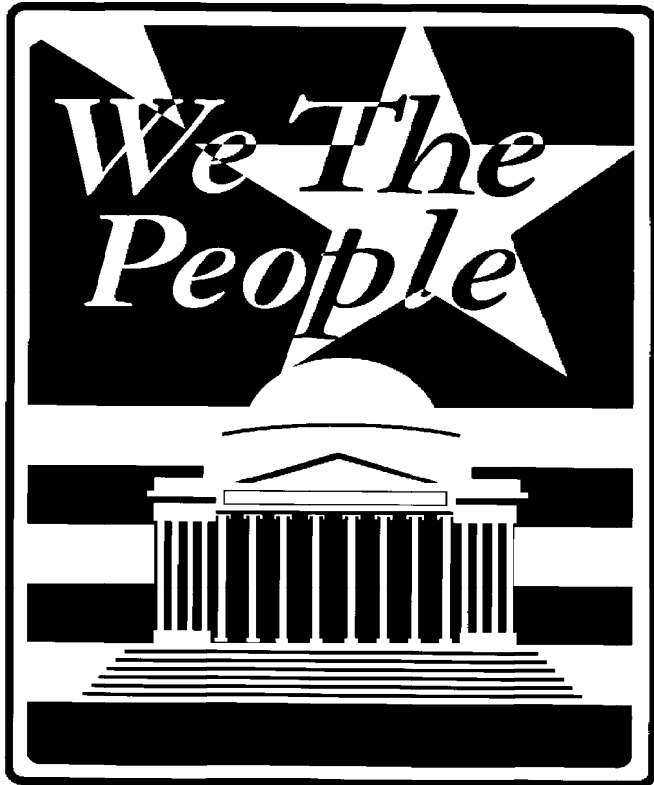
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Travel, Entertainment, and Gift Expenses

For use in preparing
1994 Returns



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Important Changes for 1994

Travel expenses paid for others. Beginning in 1994, you cannot deduct travel expenses you pay or incur for a spouse, dependent, or other individual who accompanies you (or your employee) on business travel unless the travel satisfies specific requirements. See *Travel expenses for another individual*.

Club dues. Beginning in 1994, you are not allowed a deduction for dues (including initiation fees) for membership in any club organized for business, pleasure, recreation, or other social purpose.

Business meals and entertainment. Beginning in 1994, the amount you can deduct for

business meals and entertainment expenses is reduced from 80% to 50%. See *50% Limit*.

Standard mileage rate. The standard mileage rate for the cost of operating your car in 1994 is 29 cents per mile for all business miles.

Form 2106-EZ. You may be able to use new Form 2106-EZ to claim your employee business expenses. See *Form 2106-EZ* under *Completing Forms 2106 and 2106-EZ* in Chapter 6.

Important Reminders

Tax incentives for clean-fuel vehicles. You may be entitled to a tax credit for an electric vehicle or a deduction from gross income for a part of the cost of a clean-fuel vehicle if you place one of these vehicles in service from July 1, 1993, through December 31, 2004. The vehicle must meet certain requirements, and you do not have to use it in your business to qualify for the credit or the deduction. For more information, see Chapter 15 of Publication 535, *Business Expenses*.

Limit on itemized deductions. If you are an employee, you can deduct certain work-related expenses as itemized deductions on Schedule A (Form 1040). The amount you can deduct is limited to the excess over 2% of your adjusted gross income. It may be further limited if your adjusted gross income is more than \$111,800 (\$55,900 if you are married filing separately). For more information, see the instructions for Form 1040.

Introduction

You may be able to deduct business-related expenses you have for travel away from home, entertainment, gifts, or local transportation. This publication explains what expenses are deductible, how to report them on your return, what records you must keep to prove your expenses, and how to treat any expense reimbursements you may receive.

This publication deals with expenses of employees and sole proprietors. Other businesses, such as partnerships, corporations, and trusts, should refer to their tax form instructions and Publication 535, *Business Expenses*, for information on deducting travel, entertainment, gift, and transportation expenses.

Expenses fully reimbursed. You will not need to read this publication if *all* of the following are true.

- 1) You fully accounted to your employer for your work-related expenses.
- 2) You received full reimbursement for your expenses.
- 3) Your employer required you to return any excess reimbursement and you did so.
- 4) Box 13 of your Form W-2 shows no amount with a code L.

If you meet these four conditions, there is no need to show the expenses or the reimbursements on your return. If you would like more information on reimbursements and accounting to your employer, see Chapter 6.

If you do not meet all of these conditions, you must complete Form 2106 or Form 2106-EZ and itemize your deductions on Schedule A (Form 1040) to claim your expenses. See Chapter 6.

Note: If you meet these conditions and your employer included reimbursements on your Form W-2 in error, ask your employer for a corrected Form W-2.

Employers. If you are an employer who reimburses entertainment, gift, or local transportation expenses incurred by your employees, you should get Publication 535, *Business Expenses*, or Publication 937, *Employment Taxes*, for information on how to deduct these expenses.

Volunteers. If you perform services as a volunteer worker, you may be able to deduct some of your costs as a charitable contribution. See *Out-of-Pocket Expenses in Giving Services* in Publication 526, *Charitable Contributions*, for information on the expenses you can deduct.

Useful Items

You may want to see:

Publication

- 225** Farmer's Tax Guide
- 334** Tax Guide for Small Business
- 529** Miscellaneous Deductions
- 535** Business Expenses
- 917** Business Use of a Car
- 937** Employment Taxes
- 1542** Per Diem Rates

Form (and Instructions)

- 1040** U.S. Individual Income Tax Return
- Schedule A (Form 1040)** Itemized Deductions
- Schedule C (Form 1040)** Profit or Loss From Business
- Schedule C-EZ (Form 1040)** Net Profit From Business
- Schedule F (Form 1040)** Profit or Loss From Farming
- 2106** Employee Business Expenses
- 2106-EZ** Unreimbursed Employee Business Expenses

Ordering publications and forms. To order free publications and forms, call our toll-free telephone number 1-800-TAX-FORM (1-800-829-3676). If you have access to TDD equipment, you can call 1-800-829-4059. See your tax package for the hours of operation. You can also write to

the IRS Forms Distribution Center nearest you. Check your income tax package for the address.

Asking tax questions. You can call the IRS with your tax question Monday through Friday during regular business hours. Check your telephone book or your tax package for the local number or you can call toll-free 1-800-829-1040 (1-800-829-4059 for TDD users).

1. Travel Expenses

If you temporarily travel away from your tax home, you can use this chapter to determine if you have deductible travel expenses. This chapter includes the definitions of "tax home" and "temporary" and a discussion of different types of travel expenses, including the standard meal allowance. You will also find a discussion of the rules for travel inside and outside the United States, luxury water travel, and deductible convention expenses.

Travel expenses defined. For tax purposes, travel expenses are ordinary and necessary expenses that you pay while traveling away from home for your business, profession, or job. An ordinary expense is one that is common and accepted in your field of business, trade, or profession. A necessary expense is one that is helpful and appropriate to your business. An expense does not have to be indispensable to be considered necessary. However, you cannot deduct expenses to the extent they are lavish or extravagant.

You will find examples of deductible travel expenses later in this chapter.

Traveling away from home. You are traveling away from home if:

- 1) Your duties require you to be away from the general area of your tax home (defined later) substantially longer than an ordinary day's work, and
- 2) You need to get sleep or rest to meet the demands of your work while away from home.

This rest requirement is not satisfied by merely napping in your car. You do not have to be away from your tax home for a whole day or from dusk to dawn as long as your relief from duty is long enough to get necessary sleep or rest.

Example 1. You are a railroad conductor. You leave your home terminal on a regularly scheduled round-trip run between two cities and return home 16 hours later. During the run, you have 6 hours off at your turnaround point where you eat two meals and rent a hotel room to get necessary sleep before starting

the return trip. You are considered to be away from home, and you can deduct travel expenses.

Example 2. You are a truck driver. You leave your terminal and return to it later the same day. You get an hour off at your turnaround point to eat. Because you are not off to get necessary sleep and the brief time off is not an adequate rest period, your trip is not considered as travel away from home. You cannot deduct travel expenses.

Tax Home

To deduct travel expenses, you must first determine the location of your tax home.

Generally, your tax home is your regular place of business or post of duty, regardless of where you maintain your family home. It includes the **entire city or general area** in which your business or work is located. If you have more than one regular place of business, your tax home is your main place of business. If you do not have a regular or a main place of business because of the nature of your work, then your tax home may be the place where you regularly live. See *No main place of business or work*, later.

If you do not fit any of these categories, you are considered a transient (an itinerant) and your tax home is wherever you work. As a transient, you cannot claim a travel expense deduction because you are never considered away from home.

Main place of business or work. If you have more than one place of work, you should use the following factors to determine your main place of business or work:

- 1) The total time you ordinarily spend working in each area,
- 2) The degree of your business activity in each area, and
- 3) The relative amount of your income from each area.

Example. You live in Cincinnati where you have a seasonal job for 8 months and earn \$15,000. You work the remaining 4 months in Miami, also at a seasonal job, and earn \$4,000. Cincinnati is your main place of work because you spend most of your time there and earn most of your income there.

No main place of business or work. You may have a tax home even if you do not have a regular or main place of work. Your tax home may be the home where you regularly live. If you do not have a regular or main place of business or work, use the following three factors to see if you have a tax home.

- 1) You have part of your business in the area of your main home and use that home for lodging while doing business there.
- 2) You have living expenses at your main home that you duplicate because your business requires you to be away from that home.

- 3) You have not left the area in which both your traditional place of lodging and your main home are located; you have a member or members of your family living at your main home; or you often use that home for lodging.

If you meet all three factors, your tax home is the home where you regularly live, and you may be able to deduct travel expenses. If you meet only two of the factors, you may have a tax home depending on all the facts and circumstances. If you meet only one factor, you are a transient; you do not have a tax home, and you cannot deduct travel expenses.

Example 1. You are an outside salesperson with a sales territory covering several states. Your employer's main office is in Denver, and you return there for one month each year for business and nonbusiness reasons. Your business work assignments are temporary, and you have no way of knowing where future assignments will be located.

You have lived in Denver for 14 years, first with your spouse in your own house until your divorce, and then with your married sister in her house. You pay your sister \$100 a month for a room in her house where you stay when you are in Denver. You also keep in the room your furniture and any clothing that you do not take on your out-of-town business trips.

You have met all three factors listed earlier, including the traditional lodging aspects of factor (3). Therefore, you have a tax home in Denver for travel expense deduction purposes.

Example 2. You are single and live in Boston in an apartment you rent. You have worked for your employer in Boston for a number of years. Your employer enrolls you in a 12-month executive training program. You do not expect to return to work in Boston after you complete your training.

During your training, you do not do any work in Boston. Instead, you receive classroom and on-the-job training throughout the United States. You keep your apartment in Boston and return to it frequently. You use your apartment to conduct your personal business. You also keep up your community contacts in Boston. When you complete your training, you are transferred to Los Angeles.

You have not satisfied factor (1) because you did not work in Boston. You have satisfied factor (2) because you have duplicate living expenses. You also satisfy factor (3) because you do not abandon your apartment in Boston as your traditional home, you keep your community contacts, and you frequently return to live in your apartment. You have a tax home in Boston for travel expense deduction purposes.

Example 3. You are an outside salesperson with a sales territory covering several states. Your employer's main office is in Newark, but you do not go there for business reasons. Your work assignments are temporary, and you have no way of knowing where your future assignments will be located. You have a room in your married sister's house in Dayton. You stay there for one or two weekends a year, but you do no work in the area. You do not pay your sister for the use of the room.

You have not met any of the three factors listed earlier. Therefore, you are a transient and have no tax home. Because you are never away from home, you cannot deduct the cost of your meals and lodging as travel expenses.

Transient workers. If you move from job to job, maintain no fixed home, and are not associated with any particular business locality, each place you work becomes your main place of business and your tax home. You cannot deduct your expenses for meals and lodging.

Living away from your tax home. If you (and your family) live in an area outside your tax home (main place of work), you cannot deduct travel expenses between your tax home and your family home. You also cannot deduct the cost of meals and lodging while at your tax home. See *Examples 1 and 2*, below.

If you are working temporarily in the same city where you and your family live, you may be considered as traveling away from home. See *Example 3*, below.

Example 1. You live with your family in Chicago, but work in Milwaukee, where you stay in a hotel and eat in restaurants during the week. You return to Chicago every weekend. You cannot deduct any of your expenses for travel, meals, and lodging in Milwaukee. This is because Milwaukee is your tax home and the travel on weekends is not for a business reason.

Example 2. You are a truck driver and you and your family live in Tucson. You are employed by a trucking firm that has its terminal in Phoenix. At the end of your long runs, you return to your home terminal in Phoenix and spend one night there before returning home. You cannot deduct any of your travel costs in Phoenix because Phoenix is your tax home.

Example 3. Your family home is in Pittsburgh, where you work 12 weeks a year. The rest of the year you work for the same employer in Baltimore. In Baltimore, you eat in restaurants and sleep in a rooming house. Your salary is the same whether you are in Pittsburgh or Baltimore.

Because you spend most of your working time and earn most of your salary in Baltimore, that city is your tax home. You cannot deduct any expenses you have for meals and lodging there. However, when you return to work in Pittsburgh, you are away from your tax home even though you stay at your family home. Therefore, you can deduct the cost of your round trip between Baltimore and Pittsburgh. You can also deduct your part of your family's living expenses for meals and lodging while you are living and working in Pittsburgh.

Temporary Assignment or Job

Although you regularly work or carry on your business activities within the city or general area of your tax home, you may have to work or conduct business at another location. It may not be practical to return home from this other location at the end of each day's work.

If your assignment or job away from your main place of work is **temporary**, your tax

home does not change. You are considered to be away from home for the whole period, and your travel expenses are deductible. Generally, a temporary assignment in a single location is one that is realistically expected to last (and does in fact last) for one year or less.

However, if your assignment or job is **indefinite**, that location becomes your new tax home and you cannot deduct your travel expenses while there. Your assignment or job in a single location is considered indefinite if it is realistically expected to last for more than one year, regardless of whether it actually exceeds one year.

If your assignment is indefinite, you must include in your income any amounts you receive from your employer for living expenses, even if they are called travel allowances and you account to your employer for them. You may be able to deduct the cost of relocating to your new tax home as a moving expense. See Publication 521, *Moving Expenses*, for more information.

Determining temporary or indefinite. You must determine whether your assignment is temporary or indefinite when you start work. If you expect employment to last for one year or less, it is temporary in the absence of facts and circumstances that indicate otherwise. Employment that is initially temporary may become indefinite due to changed circumstances. A series of assignments to the same location, all for short periods but that together cover a long period, may be considered an indefinite assignment.

The following examples illustrate when you can and cannot deduct travel expenses for a temporary assignment.

Example 1. You are a construction worker. You live and regularly work in Los Angeles. You are a member of a trade union in Los Angeles that helps you get work in the Los Angeles area. Because of a shortage of work, you took a job on a construction project in Fresno. Your job was scheduled to end in eight months, and you planned to return to Los Angeles at that time. In fact, the job lasted 10 months, after which time you returned to Los Angeles. Your family continued to live in your home in Los Angeles.

While in Fresno, you lived in a trailer you own. You returned to Los Angeles most weekends and maintained contact with the local union to see if you could get work in Los Angeles. You realistically expected the job in Fresno to last eight months, and it did in fact last less than one year. Because you expected to return home when it ended, your tax home is in Los Angeles for travel expense deduction purposes.

You can deduct the necessary travel expenses of first getting to your temporary assignment or job and then returning to your tax home after the assignment or job ends. Also, you can deduct your reasonable expenses for meals (subject to the 50% limit discussed later) and lodging, even for days off, while you are at the temporary location.

Example 2. The facts are the same as in Example 1, except that you realistically expected the work in Fresno to be completed in 18 months. In fact, the job was completed in 10 months.

Your job in Fresno is indefinite because you realistically expected the work to last longer than one year, even though it actually lasted less than one year. Therefore, you cannot deduct any travel expenses you paid or incurred in Fresno.

Example 3. The facts are the same as in Example 1, except that you realistically expected the work in Fresno to be completed in 9 months. After 8 months, however, you were asked to remain for 7 more months (for a total actual stay of 15 months).

Initially, you realistically expected the job in Fresno to last for only 9 months. However, due to changed circumstances occurring after 8 months, it was no longer realistic for you to expect that the job in Fresno would last for one year or less. Therefore, you can only deduct your travel expenses for the first 8 months. You cannot deduct any travel expenses you paid or incurred after that time.

Going home on days off. If you go back to your tax home from a temporary assignment on your days off, you are not considered away from home while you are in your hometown. You cannot deduct the cost of your meals and lodging there. However, you can deduct your travel expenses, including meals and lodging, while traveling from the area of your temporary place of work to your hometown and back to work. You can claim these expenses up to the amount it would have cost you for meals and lodging had you stayed at your temporary place of work.

If you keep your hotel room during your visit home, you can deduct the cost of your hotel room. In addition, you can deduct your expenses of returning home up to the amount you would have spent for meals had you stayed at your temporary place of work.

Probationary work period. If you take a job that requires you to move, with the understanding that you will keep the job if your work is satisfactory during a probationary period, the job is indefinite. You cannot deduct any expenses for meals and lodging for the probationary period.

Members of the Armed Forces. If you are a member of the U.S. Armed Forces on a permanent duty assignment overseas, you are not traveling away from home. Therefore, you cannot deduct your expenses for meals and lodging. You cannot deduct these expenses even if you are required to maintain a home in the United States for your family members who are not allowed to accompany you overseas. If you are transferred from one permanent duty station to another, you may have deductible moving expenses, which are explained in Publication 521.

A naval officer assigned to permanent duty aboard a ship that has regular eating and living facilities has a tax home aboard ship for travel expense purposes.

What Are Travel Expenses?

Once you have determined that you are traveling away from your tax home, you can determine what travel expenses are deductible on your tax return.

Records. When you travel away from home on business, you should keep records of all the expenses you incur and any advances you receive from your employer. You can use a log, diary, notebook, or any other written record to keep track of your expenses. The types of expenses you need to record, along with supporting documentation, are described in Chapter 5.

Examples of Deductible Travel Expenses

Deductible travel expenses include those ordinary and necessary expenses you incur while traveling away from home on business. The type of expense you can deduct depends on the facts and your circumstances. *Table 1* summarizes the expenses you may be able to deduct.

You can use the discussion that follows as a general guideline. You may have other deductible travel expenses that are not covered here, depending on the facts and your circumstances.

Transportation fares. You can generally deduct travel by airplane, train, or bus between your home and your business destination. Your cost is the amount you paid for your ticket. If you were provided with a ticket or you are riding free as a result of a "frequent flyer" or other similar program, you have no deduction.

If you travel by ship, the amount you can deduct may be limited. See *Luxury Water Travel* and *Cruise ships* (under *Conventions*) later in this chapter.

Taxi, commuter bus, and limousine fares. You can generally deduct the fares you pay for taxis, airport limousines, buses, or other types of transportation between the airport or station and your hotel. You can also deduct these fares when you are going between your hotel and the work location of your customers or clients, your business meeting place, or your temporary work location. You cannot deduct costs of sightseeing, shopping, or similar non-business activities.

Baggage and shipping costs. You can deduct the cost of sending baggage and sample or display material between your regular work location and your temporary work location.

Car expenses. You can deduct the cost of operating and maintaining your car when traveling away from home on business. See Publication 917 for information on how to figure this deduction.

Leasing a car. You can deduct the cost of leasing a car for business purposes while you

Table 1. Deductible Travel Expenses

Expense	Description
Transportation	The cost of travel by airplane, train, or bus between your home and your business destination.
Taxi, commuter bus, and limousine	Fares for these and other types of transportation between the airport or station and your hotel, or between the hotel and your work location away from home.
Baggage and shipping	The cost of sending baggage and sample or display material between your regular and temporary work locations.
Car	The costs of operating and maintaining your car when traveling away from home on business. You may deduct actual expenses or the standard mileage rate, including business-related tolls and parking. If you lease a car while away from home on business, you can deduct business-related expenses only.
Lodging	The cost of lodging if your business trip is overnight or long enough to require you to get substantial sleep or rest to properly perform your duties.
Meals	The cost of meals only if your business trip is overnight or long enough to require you to stop to get substantial sleep or rest. Includes amounts spent for food, beverages, taxes, and related tips.
Cleaning	Cleaning and laundry expenses while away from home overnight.
Telephone	The cost of business calls while on your business trip, including business communication by fax machine or other communication devices.
Tips	Tips you pay for any expenses in this chart.
Other	Other similar ordinary and necessary expenses related to your business travel such as public stenographer's fees and computer rental fees.

are traveling away from home. However, if you lease a car for 30 days or more, you may have to include an "inclusion amount" in your income. This inclusion amount is explained in Chapter 3 of Publication 917.

You can also deduct actual operating expenses for a car you lease. Examples are gas, oil, and repairs. However, you cannot claim the standard mileage rate.

Operating expenses. For a car you own, you may have a choice of deducting actual business-related expenses or claiming the standard mileage rate. The 1994 standard mileage rate is 29 cents a mile for all business miles. The rules and qualifications for these methods are discussed in Publication 917.

Lodging. You can deduct the cost of lodging if your business trip is overnight or long enough to require you to stop for sleep or rest to properly perform your duties.

Meals. You can deduct the cost of meals only if your business trip is overnight or long enough to require you to stop for sleep or rest to properly perform your duties. You cannot deduct the cost of meals if it is not necessary for you to rest. If you pay for a business meal when you are not traveling, you can deduct the cost only if you meet the rules for business entertainment. These rules are explained in Chapter 2.

The expense of a meal includes amounts you spend for your food, beverages, taxes, and tips relating to the meal. You can deduct either the actual cost or a standard amount. See *Standard Meal Allowance* later in this chapter.

50% limit on meals. You can deduct only 50% of the cost of your business-related meals unless you are reimbursed for these expenses. This limit applies whether the unreimbursed meal expense is for business travel or business entertainment. Chapter 2 discusses the 50% limit in more detail.

Lavish or extravagant. You cannot deduct expenses for meals to the extent they are lavish or extravagant. An expense is not considered lavish or extravagant if it is reasonable based on the facts and circumstances. Expenses will not be disallowed merely because they are more than a fixed dollar amount or take place at deluxe restaurants, hotels, night clubs, or resorts.

Cleaning and laundry expenses. You can deduct reasonable laundry expenses while traveling away from home on business.

Telephone expenses. You can deduct the cost of business calls while you are traveling away from home. This includes the cost of business communication by fax machine or other devices.

Tips. You can deduct tips you pay for any of the expenses in this section.

Other expenses. You can deduct other similar ordinary and necessary expenses that are related to your business travel. Such expenses might include the costs of operating and maintaining a house trailer, public stenographer's fees, and computer rental fees.

Travel expenses for another individual. If a spouse, dependent, or other individual goes with you (or your employee) on a business trip or to a business convention, you generally cannot deduct his or her travel expenses. You can only deduct the travel expenses you pay or incur for such an accompanying individual if that individual:

- 1) Is your employee,
- 2) Has a bona fide business purpose for the travel, **and**
- 3) Would otherwise be allowed to deduct the travel expenses.

For a bona fide business purpose to exist, you must prove a real business purpose for the individual's presence. Incidental services, such as typing notes or assisting in entertaining customers, are not enough to warrant a deduction.

Example. Jerry drives to Chicago on business and takes his wife, Linda, with him. Linda is not Jerry's employee, Linda's presence serves no business purpose, and Linda does not otherwise qualify to deduct the travel expenses. Jerry pays \$115 a day for a double room. A single room costs \$90 a day. He can deduct the total cost of driving his car to and from Chicago, but only \$90 a day for his hotel room. If he uses public transportation, he can deduct only his fare.

Standard Meal Allowance

You generally can deduct a standard amount for your daily meals and incidental expenses while you are traveling away from home on business. Incidental expenses include costs for laundry, cleaning, and tips for services. In this publication, the term "standard meal allowance" refers to meals and incidental expenses.

This method is an alternative to the actual cost method. It allows you to deduct a set amount, depending on where you travel, instead of keeping records of actual meal expenses. If you use the standard meal allowance, you still must keep records to prove the time, place, and business purpose of your travel. See the recordkeeping rules for travel in Chapter 5.

Who can use the standard meal allowance. You can use the standard meal allowance whether you are an employee or self-employed. You cannot use the standard meal allowance, however, if you are related to your employer as defined below.

You can use the standard meal allowance whether or not you are reimbursed for your

Table 2. (Continued)

KEY CITY ¹	COUNTY/LOCATION ^{2,3}	AMOUNT	KEY CITY ¹	COUNTY/LOCATION ^{2,3}	AMOUNT
LOUISIANA			MISSOURI		
Alexandria	Rapides	\$ 30	Branson	Taney	\$ 30
Baton Rouge	East Baton Rouge	30	Kansas City	Clay, Jackson, Platte	34
Bossier City	Bossier	30	Lake Ozark	Miller	34
Lafayette	Lafayette	30	Osage Beach	Camden	30
Lake Charles	Calcasieu	30	Springfield	Greene	30
New Orleans	Jefferson, Orleans, Plaquemines, St. Bernard	34	St. Louis	St. Charles, St. Louis	38
Shreveport	Caddo	30	NEBRASKA		
Slidell	St. Tammany	30	Omaha	Douglas	30
MAINE			NEVADA		
Auburn	Androscoggin	30	Las Vegas	Clark; Nellis AFB	38
Bangor	Penobscot	30	Reno	Washoe	30
Bar Harbor	Hancock	34	Stateline	Douglas	38
Kennebunk/Sanford	York	30	NEW HAMPSHIRE		
Kittery	Portsmouth Naval Shipyard	30	Conway	Carroll	30
Portland	Cumberland	30	Laconia	Belknap	30
Rockport	Knox	30	Lebanon/Hanover	Grafton	34
Wiscasset	Lincoln	30	Manchester	Hillsborough	30
MARYLAND (See also District of Columbia)			Portsmouth/Newington	Rockingham; Pease AFB	30
Annapolis	Anne Arundel	34	NEW JERSEY		
Baltimore	Baltimore, Harford	38	Atlantic City	Atlantic	38
Columbia	Howard	34	Belle Mead	Somerset	30
Easton	Talbot	30	Camden	Camden	34
Frederick	Frederick	34	Edison	Middlesex	38
Hagerstown	Washington	30	Freehold/Eatontown	Monmouth; Fort Monmouth	34
Lusby	Calvert	34	Millville	Cumberland	30
Ocean City	Worcester	34	Moorestown	Burlington	34
Salisbury	Wicomico	30	Newark	Bergen, Essex, Hudson, Passaic, Union	38
Tower Garden on Bay	Queen Anne's	30	Ocean City/Cape May	Cape May	34
Waldorf	Charles	30	Princeton/Trenton	Mercer	34
MASSACHUSETTS			Tom's River	Ocean	30
Andover	Essex	34	NEW MEXICO		
Boston	Suffolk	38	Albuquerque	Bernalillo	34
Cambridge/Lowell	Middlesex	38	Farmington	San Juan	30
Hyannis	Barnstable	30	Las Cruces/White Sands	Dona Ana	30
Martha's Vineyard/ Nantucket	Dukes, Nantucket	38	Los Alamos	Los Alamos	30
Pittsfield	Berkshire	34	Santa Fe	Santa Fe	34
Quincy	Norfolk	34	Taos	Taos	30
Springfield	Hampden	30	NEW YORK		
MICHIGAN			Albany	Albany	30
Ann Arbor	Washtenaw	30	Binghamton	Broome	30
Charlevoix	Charlevoix	30	Buffalo	Erie	34
Detroit	Wayne	38	Corning	Steuben	30
Flint	Genesee	30	Elmira	Chemung	30
Grand Rapids	Kent	30	Glens Falls	Warren	34
Kalamazoo	Kalamazoo	30	Ithaca	Tompkins	30
Mackinac Island	Mackinac	34	Jamestown	Chautauqua	30
Port Huron	St. Clair	34	Kingston	Ulster	30
Saginaw	Saginaw	30	Lake Placid	Essex	30
St. Joseph/Niles/ Benton Harbor	Berrien	30	Monticello	Sullivan	30
Traverse City	Grand Traverse	30	New York City	Manhattan, Staten Island, Bronx, Brooklyn, Queens; Nassau, Suffolk	38
Troy/Pontiac	Oakland	34	Niagara Falls	Niagara	34
MINNESOTA			Palisades/Nyack	Rockland	34
Bemidji	Beltrami	30	Plattsburgh	Clinton	30
Brainerd	Crow Wing	30	Rochester	Monroe	34
Duluth	St. Louis	34	Saratoga Springs	Saratoga	38
Grand Rapids	Itasca	30	Schenectady	Schenectady	34
Mendota Heights	Dakota	30	Syracuse	Onondaga	30
Minneapolis/St. Paul	Anoka, Hennepin, Ramsey; Detachment BRAVO at Fort Snelling, Rosemount	34	Troy	Rensselaer	30
Rochester	Olmsted	30	Utica	Oneida	30
St. Cloud	Stearns	30	Watertown	Jefferson	30
MISSISSIPPI			West Point	Orange	34
Biloxi/Bay St. Louis/ Gulfport/Pascagoula	Harrison, Jackson, Hancock	30	White Plains	Westchester	38
Jackson	Hinds	30	NORTH CAROLINA		
Natchez	Adams	30	Asheville	Buncombe	30
Ridgeland	Madison	38	Charlotte	Mecklenburg	34
Vicksburg	Warren	30	Duck	Dare	30
			Greensboro/High Point	Guilford	30
			Raleigh/Chapel Hill/ Durham	Wake, Durham, Orange	34
			Winston-Salem	Forsyth	30

Table 2. (Continued)

KEY CITY ¹	COUNTY/LOCATION ^{2,3}	AMOUNT	KEY CITY ¹	COUNTY/LOCATION ^{2,3}	AMOUNT
NORTH DAKOTA			TEXAS (cont'd)		
Bismarck/Mandan	Burleigh, Morton	\$ 30	Dallas/Fort Worth	Dallas, Tarrant	\$ 34
Fargo	Cass	30	El Paso	El Paso	30
OHIO			Galveston	Galveston	30
Akron	Summit	34	Houston	Harris; LBJ Space Center; Ellington AFB	38
Cincinnati/Evendale	Hamilton, Warren	30	Laredo	Webb	30
Cleveland	Cuyahoga	38	San Angelo	Tom Green	30
Columbus	Franklin	34	San Antonio	Bexar	30
Dayton/Fairborn	Montgomery, Greene; Wright-Patterson AFB	30	UTAH		
Port Clinton/Oakharbor	Ottawa	30	Cedar City	Iron	30
Sandusky	Erie	30	Provo	Utah	30
Springfield	Clark	30	Salt Lake City/Ogden	Salt Lake, Weber, Davis; Dugway Proving Ground; Tooele Army Depot	30
Toledo	Lucas	30	St. George	Washington	30
Warren	Trumbull	30	VERMONT		
OKLAHOMA			Burlington	Chittenden	30
Norman	Cleveland	30	Middlebury	Addison	30
Tulsa/Bartlesville	Osage, Tulsa, Washington	30	Rutland	Rutland	30
OREGON			White River Junction	Windsor	30
Ashland/Medford	Jackson	30	VIRGINIA (See also District of Columbia)		
Bend	Deschutes	30	Charlottesville		34
Eugene	Lane	30	Lynchburg		30
Lincoln City/Newport	Lincoln	30	Norfolk/Virginia Beach/ Portsmouth/Hampton/ Newport News/ Chesapeake	York; Naval Weapons Station, Yorktown	34
Portland	Multnomah	30	Richmond	Chesterfield, Henrico; Defense Supply Center	34
PENNSYLVANIA			Roanoke	Roanoke	30
Allentown	Lehigh	34	Warrenton/Amissville	Fauquier, Rappahonock	30
Bloomsburg	Columbia	30	Williamsburg		34
Chester/Radnor	Delaware	38	Wintergreen	Nelson	38
Gettysburg	Adams	30	WASHINGTON		
Harrisburg	Dauphin	34	Anacortes/Mt. Vernon	Skagit	30
King of Prussia/ Ft. Washington	Montgomery	34	Bellingham	Whatcom	30
Lancaster	Lancaster	30	Bremerton	Kitsap	30
Mechanicsburg	Cumberland	30	Kelso/Longview	Cowlitz	30
Philadelphia	Philadelphia	34	Lynnwood/Everett	Snohomish	30
Pittsburgh	Allegheny	34	Port Angeles	Clallam	30
Scranton	Lackawanna	30	Richland	Benton	34
Shippingport	Beaver	30	Seattle	King	34
Somerset	Somerset	30	Spokane	Spokane	30
State College	Centre	30	Tacoma	Pierce	30
Stroudsburg	Monroe	30	Tumwater/Olympia	Thurston	34
Valley Forge	Chester	38	Vancouver	Clark	34
Warminster	Bucks; Naval Air Center	30	Whidbey Island	Island	30
Wilkes-Barre	Luzerne	30	Yakima	Yakima	30
York	York	30	WEST VIRGINIA		
RHODE ISLAND			Charleston	Kanawha	30
East Greenwich	Kent; Naval Construction Center in Davisville	34	Martinsburg	Berkeley	30
Newport	Newport	38	Morgantown	Monongalia	30
Providence	Providence	34	Parkersburg	Wood	30
SOUTH CAROLINA			WISCONSIN		
Charleston	Charleston, Berkeley	30	Brookfield	Waukesha	34
Columbia	Richland	30	Eau Claire	Eau Claire	30
Hilton Head	Beaufort	34	La Crosse	La Crosse	30
Myrtle Beach	Horry; Myrtle Beach AFB	30	Lake Geneva	Walworth	34
TENNESSEE			Madison	Dane	30
Gatlinburg	Sevier	30	Milwaukee	Milwaukee	30
Johnson City	Washington	30	Oshkosh	Winnebago	30
Kingsport/Bristol	Sullivan	30	Wisconsin Dells	Columbia	30
Knoxville	Knox; city of Oak Ridge	30	WYOMING		
Memphis	Shelby	30	Casper	Natrona	30
Nashville	Davidson	30	Cheyenne	Laramie	30
TEXAS			Jackson	Teton	34
Amarillo	Potter	30			
Austin	Travis	34			
Brownsville	Cameron	30			
Corpus Christi/Ingleside	Nueces, San Patricio	30			

¹ Includes all locations within, or entirely surrounded by, the corporate limits of the key city, including independent entities within those boundaries.

² Includes all locations within, or entirely surrounded by, the corporate limits of the key city as well as the boundaries of the listed counties (including parishes or boroughs). This includes independent entities within those boundaries.

³ Military installations or Government-related facilities located partly within the city or county boundary shall include all locations that are geographically part of the installation/facility, even though part(s) may be outside the boundary.

traveling expenses. However, if you are not reimbursed for meal expenses, you can deduct only 50% of the standard meal allowance. This 50% limit is figured when you complete Form 2106, Form 2106-EZ, or Schedule C. If you file Schedule C-EZ, enter the total amount of your business expenses on line 2. You can only include 50% of the standard meal allowance in that total. If you file Schedule F, enter the total amount of your travel, meals and entertainment expenses on line 34. You can only include 50% of the standard meal allowance in that total.

Related to employer. You are related to your employer if:

- 1) Your employer is your brother or sister, half-brother or half-sister, spouse, ancestor, or lineal descendent,
- 2) Your employer is a corporation in which you own, directly or indirectly, more than 10% in value of the outstanding stock, or
- 3) Certain fiduciary relationships exist between you and your employer involving grantors, trusts, beneficiaries, etc.

You may be considered to indirectly own stock, for purposes of (2) above, if you have an interest in a corporation, partnership, estate, or trust that owns the stock or if a family member or partner owns the stock.

Amount of standard meal allowance. The standard meal allowance is **\$26 a day** for most areas in the United States. Other locations in the United States are designated as high-cost areas, qualifying for higher standard meal allowances. *Table 2* shows the locations qualifying for rates of \$30, \$34, or \$38 a day for travel on or after January 1, 1994.

If you travel to more than one location in one day, use the rate in effect for the area where you stop for sleep or rest. If you work in the transportation industry, however, see *Special rate for transportation workers*, later in this section.

Example. You regularly live and work in Chicago. You sometimes travel overnight to Des Moines for business. Your employer expects you to pay your expenses out of your regular salary and does not separately or specifically reimburse your expenses for business trips. You must keep receipts to prove the amount of your lodging expense. You can claim the standard meal allowance for Des Moines, \$30, on your Form 2106 or Form 2106-EZ. You are subject to the 50% limit on meal and entertainment expenses. You are also subject to the 2% of adjusted gross income limit that applies to most other miscellaneous itemized deductions.

Standard meal allowance for areas outside the continental United States. The previously mentioned standard meal allowance rates do not apply to travel in Alaska, Hawaii, or any other nonforeign locations outside the continental United States. They also do not apply to foreign locations. The federal per diem rates for these locations are published monthly in the *Maximum Travel Per Diem Allowances for Foreign Areas*.

Your employer may have these rates available, or you can purchase the publication from the:

Superintendent of Documents
U.S. Government Printing Office
P.O. Box 371954
Pittsburgh, PA 15250-7954

You can also order it by calling the Government Printing Office at (202)512-1800 (not a toll-free number). To find out the rate for a specific foreign location, you can call the Department of State at (703)875-7900 (not a toll-free number).

Special rate for transportation workers.

You may be able to use a special standard meal allowance if you work in the transportation industry. You are in the transportation industry if your work:

- 1) Directly involves moving people or goods by airplane, barge, bus, ship, train, or truck, and
- 2) Regularly requires you to travel away from home and, during any single trip, usually involves travel to areas eligible for different standard meal allowance rates.

If this applies to you, you can claim a **\$32 a day** standard meal allowance (\$36 for travel outside the continental United States).

Using the special rate for transportation workers eliminates the need for you to determine the standard meal allowance for every area where you stop for sleep or rest. If you choose to use the special rate for any trip, however, you must continue to use the special rate (and not use the regular standard meal allowance rates) for all trips you take that year.

Travel for less than 24 hours. If you are not traveling for the entire 24-hour day, you must prorate the standard meal allowance. You may do so by dividing the day into 6-hour quarters. The 6-hour quarters are:

- 1) Midnight to 6 a.m.,
- 2) 6 a.m. to noon,
- 3) Noon to 6 p.m., and
- 4) 6 p.m. to midnight.

You can claim one-fourth of the full day standard meal allowance for each 6-hour quarter of the day during part of which you are traveling away from home.

Example 1. You live and work in Los Angeles. Your employer sends you to San Francisco on a temporary assignment. You leave home at 8 a.m. on March 23. Your assignment is completed on March 26. You arrive home at 4 p.m. of that day. You are considered to be traveling for 3½ days (a ¼ day on March 23 + 2 full days + a ¾ day on March 26). Your standard meal allowance is \$133 (3½ × \$38) while on this assignment.

Example 2. Maria is employed in Milwaukee as a convention planner. In April she went on a one-week business trip. She left her home in Milwaukee at 7 a.m. on April 5 and flew to Washington, DC, where she spent two

nights. She then went to Albany, NY, arriving there at 4 p.m. on April 7. After three nights in Albany, she went to New York City to attend a planning seminar at her employer's request. She arrived at 1 p.m. on April 10. On April 12, she flew back to Milwaukee, arriving at her home at 5:45 p.m.

Maria decides to use the standard meal allowance and arrives at her expense as follows:

City	Number	Allowance	Total
	of Days	Amount	
Washington, DC	1½	\$38	\$ 66.50
Albany, NY	3	\$30	90.00
New York City	2½	\$38	104.50
			\$261.00

Maria's total standard meal allowance for the trip is \$261.00 (\$66.50 + \$90.00 + \$104.50). If her employer does not reimburse her for her meals, Maria will be able to deduct 50% of her unreimbursed meals as an itemized deduction. She will figure this limit on Form 2106 or Form 2106-EZ.

Investment and education expenses. You can also use the standard meal allowance to prove meal expenses you incurred in connection with investment and other income-producing property and/or qualifying educational expenses while traveling away from home.

Standard meal allowance not allowed. You cannot use the standard meal allowance to prove the amount of your meals if you are traveling for medical or charitable purposes.

Travel in the United States

The following discussion applies to travel in the United States. For this purpose, the United States includes the 50 states and the District of Columbia. The treatment of your travel expenses depends on how much of your trip was business related and on how much of your trip occurred within the United States.

Trip Primarily for Business

You can deduct all of your travel expenses if your trip was entirely business related. If your trip was primarily for business and, while at your business destination, you extended your stay for a vacation, made a nonbusiness side trip, or had other nonbusiness activities, you can deduct your business-related travel expenses. These expenses include the travel costs of getting to and from your business destination and any business-related expenses at your business destination.

Example. You work in Atlanta and take a business trip to New Orleans. On your way home, you stop in Mobile to visit your parents. You spend \$630 for the 9 days you are away from home for travel, meals, lodging, and other travel expenses. If you had not stopped in Mobile, you would have been gone only 6 days, and your total cost would have been \$580. You can deduct \$580 for your trip, including the cost of round-trip transportation to and from New Orleans. The cost of your meals is subject to the 50% limit on meals discussed earlier.

Trip Primarily for Personal Reasons

If your trip was primarily for personal reasons, such as a vacation, the entire cost of the trip is a nondeductible personal expense. However, you can deduct any expenses you have while at your destination that are directly related to your business.

A trip to a resort or on a cruise ship may be a vacation even if the promoter advertises that it is primarily for business. The scheduling of incidental business activities during a trip, such as viewing videotapes or attending lectures dealing with general subjects, will not change what is really a vacation into a business trip.

Part of Trip Outside the United States

If part of your trip is outside the United States, use the rules described later in this chapter under *Travel Outside the United States* for that part of the trip. For the part of your trip that is inside the United States, use the rules in this section. Travel outside the United States does not include travel from one point in the United States to another point in the United States. The following discussion can help you determine whether your trip was entirely within the United States.

Public transportation. If you travel by public transportation, any place in the United States where that vehicle makes a scheduled stop is a point in the United States. Once the vehicle leaves the last scheduled stop in the United States on its way to a point outside the United States, you apply the rules under *Travel Outside the United States*.

Example 1. You fly from New York to Puerto Rico with a scheduled stop in Miami. You return to New York nonstop. The flight from New York to Miami is in the United States, so only the flight from Miami to Puerto Rico is outside the United States. All of the return trip is outside the United States, as there are no scheduled stops between Puerto Rico and New York.

Example 2. You travel by train from New York to Montreal. The travel from New York to the last scheduled stop in the United States is travel in the United States.

Private car. Travel by private car in the United States is travel between points in the United States, even though you are on your way to a destination outside the United States.

Example. You travel by car from Denver to Mexico City and return. Your travel from Denver to the border and from the border back to Denver is travel in the United States, and the rules in this section apply. The rules under *Travel Outside the United States* apply to your trip from the border to Mexico City and back to the border.

Private plane. If you travel by private plane, any trip, or part of a trip, for which both your takeoff and landing are in the United States is

travel in the United States. This is true even if part of your flight is over a foreign country.

Example. You fly nonstop from Seattle to Juneau. Although the flight passes over Canada, the trip is considered to be travel in the United States.

Travel Outside the United States

If any part of your business travel is outside the United States, some of your deductions for the cost of getting to and from your destination may be limited. For this purpose, the United States includes the 50 states and the District of Columbia.

How much of your travel expenses are deductible depends in part upon how much of your trip outside the United States was business related.

Travel Entirely for Business

If you travel outside the United States and you spend the entire time on business activities, all your travel expenses of getting to and from your business destination are deductible.

In addition, even if you did not spend your entire time on business activities, your trip is considered entirely for business, and you can deduct all of your business-related travel expenses if you meet at least one of the following four conditions.

- 1) You did not have substantial control over arranging the trip. You are not considered to have substantial control merely because you have control over the timing of your trip.

You are considered not to have substantial control over your trip if you:

- a) Are an employee who was reimbursed or paid a travel expense allowance, and
- b) Are not related to your employer, and
- c) Are not a managing executive.

“Related to your employer” was defined earlier in this chapter under *Standard Meal Allowance*. A “managing executive” is an employee who has the authority and responsibility, without being subject to the veto of another, to decide on the need for the business travel.

A self-employed person is generally regarded as having substantial control over arranging business trips.

- 2) You were outside the United States for a week or less, combining business and nonbusiness activities. One week means seven consecutive days. In counting the days, do not count the day you leave the United States, but count the day you return to the United States.

Example. You traveled to Paris primarily for business. You left Denver on Tuesday and flew to New York. On Wednesday, you flew from New York to Paris, arriving the next morning. On Thursday and Friday, you had business discussions, and from Saturday until Tuesday, you were sightseeing. You flew back to New York, arriving Wednesday afternoon.

On Thursday, you flew back to Denver. Although you were away from your home in Denver for more than a week, you were not outside the United States for more than a week. This is because the day of departure does not count as a day outside the United States. You can deduct your cost of the round-trip flight between Denver and Paris. You can also deduct the cost of your stay in Paris for Thursday and Friday while you conducted business. However, you cannot deduct the cost of your stay in Paris from Saturday through Tuesday because those days were spent on nonbusiness activities.

- 3) You spent less than 25% of the total time you were outside the United States on nonbusiness activities, even if the trip outside the United States was for more than a week. For this purpose, count both the day your trip began and the day it ended.

Example. You flew from Seattle to Tokyo, where you spent 14 days on business and 5 days on personal matters. You then flew back to Seattle. You spent one day flying in each direction. Because only $\frac{1}{21}$ (less than 25%) of your total time abroad was for nonbusiness activities, you can deduct as travel expenses what it would have cost you to make the trip if you had not engaged in any nonbusiness activity. The amount you can deduct is the cost of the round-trip plane fare and 16 days of meals (subject to the 50% limit), lodging, and other related expenses.

- 4) You can establish that a personal vacation was not a major consideration, even if you have substantial control over arranging the trip.

If you do not meet any of these conditions, you may still be able to deduct some of your expenses. See *Travel Primarily for Business*, next.

Travel Primarily for Business

If you traveled outside the United States primarily for business purposes, but spent 25% or more of your time on nonbusiness activities, your travel expense deductions are limited unless you meet one of the four conditions listed earlier under *Travel Entirely for Business*. If your deductions are limited, you must allocate your travel expenses of getting to and from your destination between your business and nonbusiness activities to determine your deductible amount.

Travel allocation rules. If your trip was not entirely for business, you must allocate your travel expenses on a day-to-day basis between days you conducted business and days you did not conduct business.

To figure the deductible amount of your round-trip travel expenses between the United States and your business destination, multiply the total cost by the following fraction. The numerator (top number) is the total number of business days outside the United States. The

denominator (bottom number) is the total number of all days outside the United States. The day of your departure from the United States and the day you return to the United States are both counted as days outside the United States.

Counting business days. Your business days include transportation days, days your presence was required, days you spent on business, and certain weekends and holidays.

Transportation day. Count as a business day any day you spend traveling to or from a business destination. However, if because of a nonbusiness activity you do not travel by a direct route, your business days are the days it would take you to travel a reasonably direct route to your business destination. Extra days for side trips or nonbusiness activities cannot be counted as business days.

Presence required. Count as a business day any day that your presence is required at a particular place for a specific business purpose, even if you spend most of the day on nonbusiness activities.

Day spent on business. If your principal activity during working hours is in pursuit of your trade or business, the day is counted as a business day. Also, count as a business day any day you are prevented from working because of circumstances beyond your control.

Certain weekends and holidays. Weekends, holidays, and other necessary standby days are counted as business days if they fall between business days. But if they follow your business meetings or activity and you remain at your business destination for nonbusiness or personal reasons, they are not business days.

Example 1. Your tax home is New York City. You travel to Quebec where you have a business appointment on Friday. You have another appointment on the following Monday. Because you had a business activity on Friday and had another business activity on Monday, the days in between are counted as business days. This is true even though you use that time for sightseeing, personal visiting, or other nonbusiness activity.

Example 2. If, in *Example 1*, you had no other business in Quebec after Friday, but stayed until Monday before starting home, Saturday and Sunday would be nonbusiness days.

Nonbusiness activity on the route to or from your business destination. If you had a vacation or other nonbusiness activity between the United States and your business destination, or between your business destination and the United States, you must allocate your travel expenses between business and nonbusiness days. You can do so as follows:

- 1) Divide the number of business days by the total number of travel days.
- 2) Multiply the result in (1) by the cost of round-trip travel between the United States and your nonbusiness destination.
- 3) Add to the result in (2) the round-trip cost of travel between the United States and

your business destination minus the round-trip cost of travel between the United States and your nonbusiness destination. This is the deductible part of your cost of getting to and from your business destination.

- 4) Add to the result in (3) your business travel expenses while at your business destination. These are your total allowable travel expenses.

Example. You live in New York and flew to Brussels on Thursday, May 19, to attend a conference with a customer that began at noon Friday, May 20. The conference ended at noon Monday, May 23. That evening you flew to Dublin where you visited with friends until the afternoon of June 5, when you flew home to New York. The primary purpose for the trip was to attend the conference.

If you had not stopped in Dublin, you would have arrived home the evening of May 23. You were outside the United States more than a week, and you are unable to show that you had no substantial control over arranging the trip, or that a personal vacation was not a major consideration in making the trip. May 19 through May 23 (5 days) are business days and May 24 through June 5 (13 days) are nonbusiness days. You cannot deduct your expenses while in Dublin. You also cannot deduct $\frac{1}{8}$ of the cost of round-trip airfare and any other expenses from New York to Dublin.

You can deduct the cost of your meals (subject to the 50% limit), lodging, and other business-related travel expenses while in Brussels. You figure the deductible part of your travel between the United States and Brussels as follows:

- 1) $\frac{1}{8}$ of the round-trip airfare and other expenses between New York and Dublin, **plus**
- 2) The cost of the round-trip fare and any other expenses between New York and Brussels minus the cost of the round-trip fare and any other expenses between New York and Dublin.

Assume the round-trip plane fare and other expenses between New York and Brussels are \$800 and the expenses between New York and Dublin are \$600. Your deductible plane fare and other expenses are \$366.67 [$(\frac{1}{8} \times \$600) + (\$800 - \$600)$].

Nonbusiness activity at or beyond business destination. If you had a vacation or other nonbusiness activity at or beyond your business destination, you must allocate your travel expenses between your business and nonbusiness days. None of your travel expenses for nonbusiness activities at or beyond your business destination are deductible. You must also allocate your round-trip transportation and other costs between the United States and your business destination as follows.

Multiply the cost of your round-trip travel between the United States and your business destination by a fraction. The numerator (top number) is the number of business days. The

denominator (bottom number) is the total number of travel days. Add to this result your other business-related travel expenses at your business destination. The sum is your total deductible travel expenses.

Example. Assume that the dates are the same as in the prior example but that instead of going to Dublin for your vacation, you fly to Venice, Italy, for a vacation. You cannot deduct any part of the cost of your trip from Brussels to Venice and return to Brussels. In addition, you cannot deduct $\frac{1}{8}$ of the airfare and other expenses from New York to Brussels and back to New York. You may deduct $\frac{7}{8}$ of the round-trip plane fare and other expenses from New York to Brussels, plus your meals, lodging, and any other business expenses you had in Brussels. If the round-trip plane fare and other expenses are \$800 from New York to Brussels, you can deduct travel costs of \$222.22 ($\frac{7}{8} \times \800).

Other methods. You can use another method of counting business days if you establish that it more clearly reflects the time spent on nonbusiness activities outside the United States.

Travel Primarily for Vacation

If your travel was primarily for vacation, or for investment purposes, and you spent some time attending brief professional seminars or a continuing education program, the entire cost of the trip is a nondeductible personal expense. You may, however, deduct your registration fees and any other expenses incurred that were directly related to your business.

Example 1. You are a doctor practicing medicine and are a member of a professional association. The association sponsored a 2-week trip to two foreign countries with three professional seminars in each country. Each seminar was 2 hours long and was held in a different city. You also made an optional side trip to a well-known tourist attraction in each of the countries visited. At the end of the trip, you received a Certificate of Continuing Education in Medicine.

You paid the cost of airfare, hotel accommodations, meals, a special escort, transportation to and from hotels, and tips. No part of the cost you paid was specifically stated for the seminars, which were arranged for you by the sponsoring professional association.

Your participation in the professional seminars did not change what was essentially a vacation into a business trip. Your travel expenses were not related primarily to your business. You had no other expenses that were directly for your business. Therefore, you cannot deduct the cost of your trip as an ordinary and necessary business expense.

Example 2. The university from which you graduated has a continuing education program for members of its alumni association. This program consists of trips to various foreign countries where academic exercises and conferences are set up to acquaint individuals in most occupations with selected facilities in several regions of the world. However, none of the conferences are directed toward specific occupations or professions. It is up to each

participant to seek out specialists and organizational settings appropriate to his or her occupational interests.

Three-hour sessions are held each day over a 5-day period at each of the selected overseas facilities where participants can meet with individual practitioners. These sessions are composed of a variety of activities including workshops, mini-lectures, role playing, skill development, and exercises. Professional conference directors schedule and conduct the sessions. Participants can choose those sessions they wish to attend.

You can participate in this program since you are a member of the alumni association. You and your family take one of the trips. You spend about 2 hours at each of the planned sessions. The rest of the time you go touring and sightseeing with your family. The trip lasts less than 1 week.

Your travel expenses for the trip are not deductible since the trip was primarily a vacation. However, registration fees and any other incidental expenses incurred by you for the five planned sessions you attended that are directly related and beneficial to your business are deductible business expenses. These expenses should be specifically stated to ensure proper allocation of your deductible business expenses.

Luxury Water Travel

Your deduction for travel by ocean liner, cruise ship, or other form of luxury water transportation for the purpose of carrying on your trade or business may be limited.

You cannot deduct more than **twice** the federal per diem rate allowable at the time of your travel. For purposes of this limit, the federal per diem is the highest amount allowed as a daily allowance for living expenses to employees of the executive branch of the federal government while they are away from home but in the United States. The highest per diem amount allowed and the daily limit for luxury water travel in 1994 is shown in the following table.

1994 Dates	Highest Federal Per Diem	Daily Limit on Luxury Water Travel
Jan. 1- Mar. 31	\$ 189	\$ 378
Apr. 1- Dec. 14	180	360
Dec. 15- Dec. 31	186	372

Example. Caroline, a travel agent, took an ocean liner from New York to London, England, on business in May. Her expense for the 6-day cruise was \$2,300. Caroline's deduction for the cruise cannot exceed \$2,160 (6 days × \$360 daily limit).

Meals and entertainment. If your expenses for luxury water travel include separately stated amounts for meals or entertainment, those amounts are subject to the 50% limit on meals and entertainment before you apply the daily limit. For a discussion of the 50% limit, see Chapter 2.

Example. In the previous example, Caroline's luxury water travel had a total cost

of \$2,300. Of that amount, \$1,400 was separately stated as meals and entertainment. Caroline, who is self-employed, is not reimbursed for any of her travel expenses. Caroline computes her deductible travel expenses as follows.

Meals and entertainment	\$1,400	
50% limit	× .50	
Allowable meals/enter.	\$ 700	
Other luxury water travel expenses	+ 900	
Allowable cost before the daily limit		\$1,600
Daily limit for May 1994	\$ 360	
Times number of days	× 6	
Maximum luxury water travel deduction ...		\$2,160
Amount of allowable deduction		<u>\$1,600</u>

Caroline's deduction for her cruise is limited to \$1,600, even though the per diem rate is higher.

Not separately stated. If your meal or entertainment charges are not separately stated or are not clearly identifiable, you are not required to allocate any portion of the total charge to meals or entertainment.

Exceptions

The per diem rule does not apply to expenses you incurred to attend a convention, seminar, or meeting on board a cruise ship. See *Cruise ships*, under *Conventions*, next.

Conventions

You can deduct your travel expenses when you attend a convention if you can show that your attendance benefits your trade or business. You cannot deduct the travel expenses for your family. If the convention is for investment, political, social, or other purposes unrelated to your trade or business, you cannot deduct the expenses. Nonbusiness expenses, such as social or sightseeing expenses, are personal expenses and are not deductible.

Your appointment or election as a delegate does not, in itself, entitle you to or deprive you of a deduction. Your attendance must be connected to your own trade or business.

Convention agenda. The agenda of the convention does not have to deal specifically with your official duties or the responsibilities of your position or business. It is enough if the agenda is so related to your active trade or business and your responsibilities that attendance for a business purpose is justified.

Conventions Held Outside the North American Area

You cannot deduct expenses for attending a convention, seminar, or similar meeting held outside the North American area **unless** the meeting is directly related to your trade or business. Also, it must be as reasonable to hold the meeting outside the North American area as in it. If the meeting meets these requirements, you also must satisfy the rules for deducting expenses for business trips in general, discussed earlier under *Travel Outside the United States*.

North American area. The North American area includes:

American Samoa	Kingman Reef
Baker Island	Marshall Islands
Barbados	Mexico
Bermuda	Micronesia
Canada	Midway Islands
Costa Rica	Northern Mariana Islands
Dominica	Palau
Dominican Republic	Palmyra
Grenada	Puerto Rico
Guam	Saint Lucia
Guyana	Trinidad and Tobago
Honduras	USA
Howland Island	U.S. Virgin Islands
Jamaica	Wake Island
Jarvis Island	
Johnston Island	

Reasonableness test. The following factors must be taken into account to determine if it was reasonable to hold the meeting outside the North American area:

- 1) The purpose of the meeting and the activities taking place at the meeting,
- 2) The purposes and activities of the sponsoring organizations or groups,
- 3) The residences of the active members of the sponsoring organization and the places at which other meetings of the sponsoring organizations or groups have been or will be held, and
- 4) Other relevant factors you may present.

Cruise ships. You can deduct up to \$2,000 per year of the expenses of attending conventions, seminars, or similar meetings held on cruise ships. You must, however, establish that the meeting is directly related to your trade or business. All ships that sail are considered cruise ships.

You can deduct these expenses if all of the following are true.

- 1) The cruise ship is a vessel registered in the United States.
- 2) All of the cruise ship's ports of call are located in the United States or in possessions of the United States.
- 3) You attach to your return a written statement signed by you that includes:
 - a) The total days of the trip, excluding the days of transportation to and from the cruise ship port,
 - b) The number of hours each day that you devoted to scheduled business activities, and
 - c) A program of the scheduled business activities of the meeting.
- 4) You attach to your return a written statement signed by an officer of the organization or group sponsoring the meeting that includes:
 - a) A schedule of the business activities of each day of the meeting, and
 - b) The number of hours you attended the scheduled business activities.

2.

Entertainment Expenses

You may be able to deduct business-related entertainment expenses you have for entertaining a client, customer, or employee.

To be deductible, the expense must be both ordinary and necessary. An ordinary expense is one that is common and accepted in your field of business, trade, or profession. A necessary expense is one that is helpful and appropriate for your business. An expense does not have to be indispensable to be considered necessary.

In addition, the entertainment expense must meet one of two tests:

- 1) Directly-related test, or
- 2) Associated test.

You must also meet the recordkeeping requirements discussed in Chapter 5.

Even if you meet all the requirements for claiming a deduction for entertainment expenses, the amount you can deduct may be limited. Generally, you can deduct only 50% of your unreimbursed entertainment expenses. This limit is discussed later under *50% Limit*.

Club dues and membership fees. Beginning in 1994, you are not allowed a deduction for dues (including initiation fees) for membership in any club organized for business, pleasure, recreation, or other social purpose.

Entertainment facilities. Generally, you cannot deduct any expenses for the cost of using an entertainment facility. This includes expenses for depreciation and operating costs such as rent, utilities, maintenance and protection.

An entertainment facility is any property you own, rent, or use for entertainment. Examples include a yacht, hunting lodge, fishing camp, swimming pool, tennis court, bowling alley, car, airplane, apartment, hotel suite, or home in a vacation resort.

Out-of-pocket expenses. You can deduct out-of-pocket expenses, such as for food and beverages, catering, gas, and fishing bait, that you provided during entertainment at a facility. These are not expenses for the use of an entertainment facility. However, these expenses are subject to the directly-related and associated tests, and the 50% limit, all discussed later.

What Entertainment Expenses Are Deductible?

This section explains different types of entertainment expenses that you may be able to deduct.

Entertainment. Entertainment includes any activity generally considered to provide entertainment, amusement, or recreation. Examples include entertaining guests at night clubs; at social, athletic, and sporting clubs; at theaters; at sporting events; on yachts; or on hunting, fishing, vacation, and similar trips.

Entertainment also may include meeting personal, living, or family needs of individuals, such as providing meals, a hotel suite, or a car to business customers or their families.

A meal as a form of entertainment. Entertainment includes the cost of a meal you provide to a customer, or client, whether the meal is a part of other entertainment or by itself. A meal sold in the normal course of your business is not entertainment. Generally, to deduct an entertainment-related meal, you or your employee must be present when the food or beverages are provided.

A meal expense includes the cost of food, beverages, taxes, and tips for the meal.

No double deduction allowed for meals. You cannot claim the cost of your meal as an entertainment expense if you are also claiming the cost of your meal as a travel expense.

Deduction may depend on your type of business. Your kind of business may determine if a particular activity constitutes entertainment. For example, if you are a dress designer and have a fashion show to introduce your new designs to store buyers, the show generally is not considered entertainment because fashion shows are typical in your business. But, if you are an appliance distributor and hold a fashion show for the spouses of your retailers, the show generally is considered entertainment.

Taking turns paying for meals or entertainment. Expenses are *not* deductible when a group of business acquaintances take turns picking up each other's meal or entertainment checks without regard to whether any business purposes are served.

Lavish or extravagant expenses. You cannot deduct expenses for entertainment to the extent they are lavish or extravagant. An expense is not considered lavish or extravagant if it is reasonable considering the facts and circumstances. Expenses will not be disallowed merely because they are more than a fixed dollar amount or take place at deluxe restaurants, hotels, night clubs, or resorts.

Allocating between business and nonbusiness expenses. If you entertain business and nonbusiness individuals at the same event, you must divide your entertainment expenses between business and nonbusiness. You can deduct only the business part. If you cannot

establish the part of the expense for each person participating, allocate the expense to each participant on a pro rata basis. For example, if you entertain a group of individuals that includes yourself, three business prospects, and seven social guests, only $\frac{1}{11}$ of the expense qualifies for the deduction. You cannot deduct the expenses for the seven social guests because those costs are considered nonbusiness expenses.

Trade association meetings. You can deduct expenses for entertainment that are directly related to and necessary for attending business meetings or conventions of certain exempt organizations. These organizations include business leagues, chambers of commerce, real estate boards, trade associations, and professional associations. The expenses of your attendance must be related to your active trade or business. These expenses are subject to the 50% limit on entertainment expenses.

Entertainment tickets. This section discusses the limits on the amount you can deduct for entertainment tickets.

When figuring your deduction, you can only take into account the face value of the ticket even if you paid a higher price. For example, you cannot include amounts in excess of face value that you pay to scalpers, ticket agencies, and ticket brokers.

However, different rules apply when the cost of a ticket to a sports event benefits a charitable organization. You can take into account the full cost you pay for the ticket, even if it is more than the face value, if:

- 1) The event's main purpose is to benefit a qualified charitable organization,
- 2) The entire net proceeds go to the charity, and
- 3) The event uses volunteers to perform substantially all the event's work.

The 50% limit on entertainment does not apply to any expense covered by a package deal involving a ticket to such a charitable sports event.

Example 1. A golf tournament is organized by the local volunteer fire company with all of the net proceeds from the event going to the acquisition of new fire equipment. The volunteers will run the tournament. You can deduct the entire cost of tickets to this event if they otherwise qualify as an entertainment expense.

Example 2. You purchase tickets to a college football game through a ticket broker. After having a business discussion, you take a client to the game. Net proceeds from the game go to colleges that qualify as charitable organizations. However, since the colleges also pay individuals to perform services, such as coaching and recruiting, you can only use the face value of the tickets in determining your deduction. Also, your deduction is subject to the 50% limit.

Table 3. When Are Entertainment Expenses Deductible?

General Rule	You can deduct ordinary and necessary expenses to entertain a client, customer, or employee if the expenses meet the directly-related test or the associated test.
Definitions	<ul style="list-style-type: none"> • Entertainment includes any activity generally considered to provide entertainment, amusement, or recreation, and includes meals provided to a customer or client. • An <u>ordinary</u> expense is one that is common and accepted in your field of business, trade, or profession. • A <u>necessary</u> expense is one that is helpful and appropriate, although not necessarily indispensable, for your business.
Tests to be met	<p>Directly-related test</p> <ul style="list-style-type: none"> • Entertainment took place in a clear business setting, or • Main purpose of entertainment was the active conduct of business, and You did engage in business with the person during the entertainment period, and You had more than a general expectation of getting income or some other specific business benefit. <p>Associated test</p> <ul style="list-style-type: none"> • Entertainment is associated with your trade or business, and • Entertainment directly precedes or follows a substantial business discussion.
Other rules	<ul style="list-style-type: none"> • You cannot deduct the cost of your meal as an entertainment expense if you are claiming the meal as a travel expense. • You can deduct expenses only to the extent they are not lavish or extravagant under the circumstances. • You generally can deduct only 50% of your unreimbursed entertainment expenses (see <i>50% Limit</i>).

Skyboxes and other private luxury boxes. Restrictions generally apply to the amount of entertainment expense you can deduct for the rental of skyboxes and other private luxury boxes for more than one event at the same sports arena. Even if the restrictions explained below do not apply, the deduction is generally subject to the 50% limit on entertainment expenses.

In determining whether a skybox has been rented for more than one event, each game or other performance counts as one event. Therefore, renting a skybox for a series of games, such as the World Series, counts as renting it for more than one event. In addition, all skyboxes that you rent in the same arena, along with any rentals by related parties, are considered in making this determination. Related parties include:

- 1) Family members (spouses, ancestors, and lineal descendants),
- 2) Parties who have made a reciprocal arrangement involving the sharing of skyboxes,
- 3) Related corporations,
- 4) A partnership and its principal partners, and

- 5) A corporation and a partnership with common ownership.

If you rent a skybox for more than one event, your deduction is limited to the price of a regular nonluxury box seat ticket.

Example. You pay \$3,000 to rent a 10-seat skybox at X Stadium for three baseball games. The cost of regular nonluxury box seats at each event is \$20 a seat. The allowable amount (subject to the 50% limit) is \$600 [(10 seats × \$20 each) × 3 events].

Food and beverages in skybox seats. If expenses for food and beverages are separately stated, these expenses can be deducted in addition to the amounts allowable for the skybox, subject to the applicable requirements and limits. The amounts separately stated for food and beverages must be reasonable. You cannot inflate the charges for food and beverages to circumvent the limited deduction for skybox rentals.

Directly-Related Test

To meet the directly-related test for entertainment expenses (including entertainment-related meals), you must show that:

- 1) The main purpose of the combined business and entertainment was the active conduct of business,
- 2) You did engage in business with the person during the entertainment period, and
- 3) You had more than a general expectation of getting income or some other specific business benefit at some future time.

Business is not considered to be the main purpose when business and entertainment are combined on hunting or fishing trips, or on yachts or other pleasure boats, unless you can show otherwise. Even if you show that business was the main purpose, you generally cannot deduct the expenses for the use of an entertainment facility. See *Entertainment facilities* earlier in this chapter.

You must consider all the facts including the nature of the business transacted and the reasons for conducting business during the entertainment. It is not necessary to devote more time to business than to entertainment. However, if the business discussion is only incidental to the entertainment, it is not directly related.

You are not required to show that business income or other business benefit actually resulted from each entertainment expense.

Clear business setting. If the entertainment takes place in a clear business setting and is for your business or work, the expenses are considered directly related to your business or work. The following situations are examples of entertainment in a clear business setting:

- 1) Entertainment in a hospitality room at a convention where business goodwill is created through the display or discussion of business products,
- 2) Entertainment that is mainly a price rebate on the sale of your products (such as a restaurant owner providing an occasional free meal to a loyal customer), and
- 3) Entertainment of a clear business nature occurring under circumstances where there is no meaningful personal or social relationship between you and the persons entertained. An example is entertainment of business and civic leaders at the opening of a new hotel or play when the purpose is to get business publicity rather than to create or maintain the goodwill of the persons entertained.

Expenses not considered directly related.

Expenses generally are not considered directly related when entertainment occurs where, because of substantial distractions, there is little or no possibility of engaging in the active conduct of business. Examples are meetings at night clubs, theaters, sporting events, or essentially social gatherings. This includes cocktail parties, or meetings with a group that includes persons other than business associates at places such as cocktail lounges, country clubs, golf clubs, athletic clubs, or vacation resorts. You may prove that

the entertainment is directly related by showing that you engaged in a substantial business discussion during the entertainment.

Associated Test

Even if your expenses do not meet the directly-related test, they may meet the associated test.

To meet the associated test for entertainment expenses (including entertainment-related meals), you must show that the entertainment is associated with your trade or business and that it directly precedes or follows a substantial business discussion (defined below).

Generally, any ordinary and necessary expense is associated with the active conduct of your trade or business if you can show that you had a clear business purpose for having the expense. The purpose may be to get new business or to encourage the continuation of an existing business relationship. However, if part of the entertainment expense is for persons not closely connected with your guests who attended the substantial business discussion, that part of the expense would not qualify for the associated test.

Substantial business discussion. Whether a business discussion is substantial depends on all the facts of each case. You must show that you or your representative actively engaged in a discussion, meeting, negotiation, or other business transaction to get income or some other specific business benefit. You may be able to deduct goodwill entertainment.

The meeting does not have to be for any specified length of time, but you must show that the business discussion was substantial in relation to the meal or entertainment. It is not necessary that you devote more time to business than to entertainment. You do not have to discuss business during the meal or entertainment.

Meetings at conventions. You are considered to have a substantial business discussion if you attend meetings at a convention or similar event, or at a trade or business meeting sponsored and conducted by a business or professional organization. However, you must attend the convention or meeting to further your trade or business. In addition, the organization that sponsors the convention or meeting must schedule a program of business activities that is the main activity of the convention or meeting.

Directly before or after business discussion. Entertainment that is held on the same day as the business discussion is considered to be held directly before or after the business discussion. However, if the entertainment and the business discussion are not held on the same day, you must consider the facts of each case to see if the associated test is met. Among the facts to consider are the place, date, and duration of the business discussion.

Also, if you or your business associates are from out of town, you must consider the dates of arrival and departure, and the reasons the entertainment and the discussion did not take place on the same day.

Example. A group of business associates comes from out of town to your place of business to hold a substantial business discussion. If you entertain those business guests and their spouses on the evening before the business discussion, or on the evening of the day following the business discussion, the entertainment generally is considered to be held directly before or after the discussion. The expense meets the associated test.

Expenses for spouses. You generally cannot deduct the cost of entertainment for your spouse or for the spouse of a business customer. However, you can deduct these costs if you can show that you had a clear business purpose, rather than a personal or social purpose, for providing the entertainment.

Example. You entertain a business customer. The cost is an ordinary and necessary business expense and is allowed under the entertainment rules. The customer's spouse joins you because it is impractical to entertain the customer without the spouse. You can deduct the cost of entertaining the customer's spouse as an ordinary and necessary business expense. Furthermore, if your spouse joins the party because the customer's spouse is present, the cost of the entertainment for your spouse is also an ordinary and necessary business expense.

50% Limit

In general, you can deduct only 50% of your business-related meal and entertainment expenses. This limit applies to employees or their employers, and to self-employed persons (including independent contractors) or their clients, depending on whether the expenses are reimbursed.

The 50% limit applies to business meals or entertainment expenses incurred while:

- 1) Traveling away from home (whether eating alone or with others) on business,
- 2) Entertaining business customers at your place of business, a restaurant, or other location, or
- 3) Attending a business convention or reception, business meeting, or business luncheon at a club.

Taxes and tips relating to a business meal or entertainment activity are included in the amount that is subject to the 50% limit. Expenses such as cover charges for admission to a night club, rent paid for a room in which you hold a dinner or cocktail party, or the amount paid for parking at a sports arena are subject to the 50% limit. However, the cost of transportation to and from a business meal or a business-related entertainment activity is not subject to the 50% limit.

If you pay or incur an expense for goods and services consisting of meals, entertainment, and other services (such as lodging or transportation), you must allocate that expense between the cost of meals and entertainment and the cost of the other services. You must have a reasonable basis for making

this allocation. For example, you must allocate your expenses if a hotel includes one or more meals in its room charge, or if you are provided with one per diem amount to cover both your lodging and meal expenses.

Application of 50% limit. The 50% limit on meal and entertainment expenses applies if the expense is otherwise deductible and is not covered by one of the exceptions discussed later.

The 50% limit also applies to activities that are not a trade or business. It applies to meal and entertainment expenses incurred for the production of income, including rental or royalty income. It also applies to deductible educational expenses.

When to apply the 50% limit. You apply the 50% limit after determining the amount that would otherwise qualify for a deduction. You first have to determine the amount of meal and entertainment expenses that would be deductible under the rules discussed in this publication.

You then apply the 50% limit. If you are an employee, use Form 2106 or Form 2106-EZ to figure the limit. If you are self-employed, figure the limit on Schedule C. If you file Schedule C-EZ, enter the total amount of your business expenses on line 2. You can only include 50% of your meal and entertainment expenses in that total. If you file Schedule F, enter 50% of your meal and entertainment expenses on line 34.

Finally, to determine the actual amount you can deduct if you are an employee, you must apply the 2% of adjusted gross income limit on Schedule A (Form 1040).

Example 1. You spend \$100 for a business-related meal. If \$40 of that amount is not allowable because it is considered lavish and extravagant, the remaining \$60 is subject to the 50% limit. Your deduction cannot be more than \$30 (.50 × \$60).

Example 2. You purchase two tickets to a concert and give them to a client. You purchased the tickets through a ticket agent. You paid \$150 for the two tickets, which had a face value of \$60 each (\$120 total). Your deduction cannot be more than \$60 (.50 × \$120).

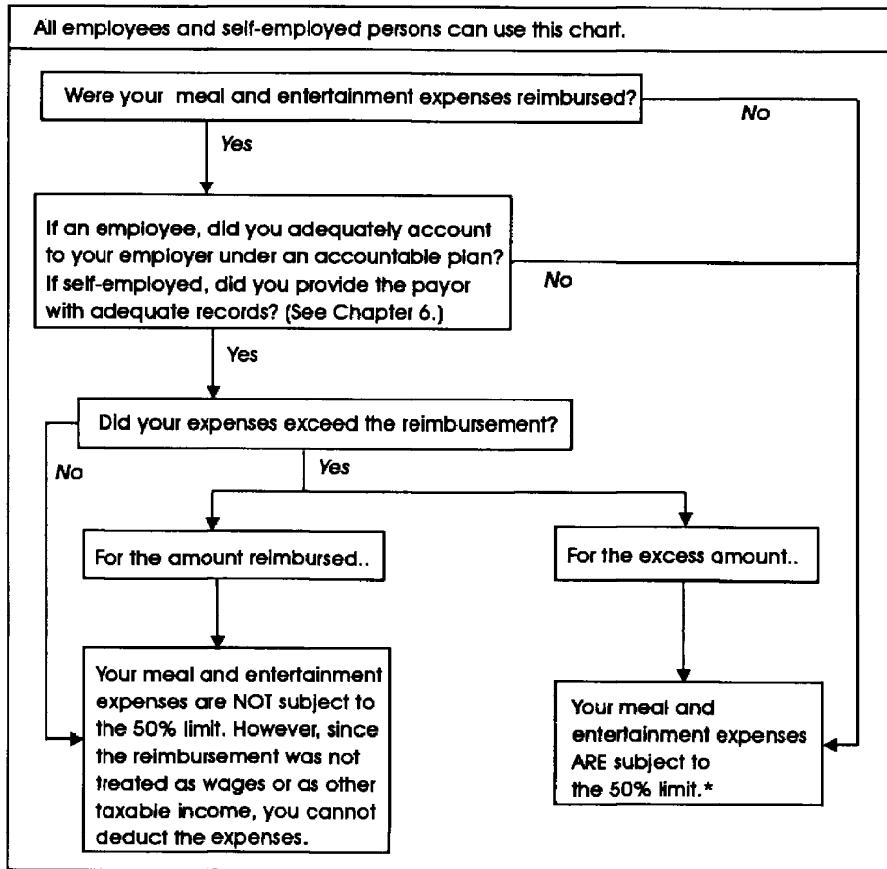
Exceptions to the 50% Limit

The 50% limit on meal and entertainment expenses applies if the expense is otherwise deductible based on the tests and rules explained in this chapter or in Chapter 1.

You can use *Figure A* to help you determine if the 50% limit applies to you. Your meal or entertainment expense is **not** subject to the 50% limit if the expense meets one of the following exceptions.

Employee's reimbursed expenses. As an employee, you are not subject to the 50% limit if your employer reimburses you under an accountable plan and does not treat your reimbursement as wages. Accountable plans are discussed in Chapter 6.

Figure A. Does the 50% Limit Apply to Your Expenses?



* There are exceptions to this rule. For example, you are not subject to the 50% limit on meals and entertainment if:

- A) You incur the expenses as a means of advertising to, or promoting goodwill in, the general community,
- B) You pay the expenses as part of a package deal that includes a ticket to a charitable sports event (see *Entertainment tickets*), or
- C) Your business involves the sale of meals and/or entertainment to the public.

Self-employed. If you are self-employed, your deductible meal and entertainment expenses are generally subject to the 50% limit. However, your expenses are not subject to the 50% limit if you incur these expenses as an independent contractor, and:

- 1) Your customer or client reimburses you, or gives you an allowance for these expenses in connection with services you perform, **and**
- 2) You provide adequate records of these expenses to your customer or client. (Recordkeeping is discussed in Chapter 5.)

Your client or customer is subject to the 50% limit if he or she can otherwise deduct these expenses.

Example. You are a self-employed attorney who adequately accounts for meal and entertainment expenses to a client who reimburses you for these expenses. You are not subject to the directly-related or associated tests, nor are you subject to the 50% limit. If the client can deduct the expenses, the client is subject to the 50% limit.

If you (the contractor) pay or incur expenses for meals and entertainment related to

providing services for a client but do not adequately account for and seek reimbursement from the client for those expenses, you must prove that your expenses meet either the directly-related test or the associated test. Your expenses will also be subject to the 50% limit.

Advertising expenses. You can deduct the cost of providing meals, entertainment, or recreational facilities to the general public as a means of advertising or promoting goodwill in the community. For example, the expense of sponsoring a television or radio show is deductible, as is the expense of distributing free food and beverages to the general public. Expenses under this exception are **not** subject to the 50% limit.

Sale of meals or entertainment. You can deduct the cost of providing meals, entertainment, goods and services, or use of facilities that you actually sell to the public. For example, if you run a night club, your expense for the entertainment you furnish to your customers, such as a floor show, is a business expense. Expenses under this exception are **not** subject to the 50% limit.

3.

Business Gift Expenses

If you give business gifts in the course of your trade or business, you can deduct the cost subject to the limits and rules in this chapter.

Limit on business gifts. You can deduct no more than \$25 for business gifts you give directly or indirectly to any one person during your tax year. A gift to a company that is intended for the eventual personal use or benefit of a particular person or a limited class of people will be considered an indirect gift to that particular person or to the individuals within that class of people who receive the gift.

A gift to the spouse of a business customer or client is an indirect gift to the customer or client. However, if you have an independent bona fide business connection with the spouse, the gift generally will not be considered an indirect gift to the other spouse. It will, however, be considered an indirect gift to the other spouse if it is intended for that spouse's eventual use or benefit. These rules also apply to gifts you give to any other family member.

If you and your spouse both give gifts, both of you are treated as one taxpayer. It does not matter whether you have separate businesses, are separately employed, or whether each of you has an independent connection with the recipient. If a partnership gives gifts, the partnership and the partners are treated as one taxpayer.

Incidental costs. Incidental costs, such as engraving on jewelry, or packaging, insuring, and mailing, are generally not included in determining the cost of a gift for purposes of the \$25 limit.

A related cost is considered incidental only if it does not add substantial value to the gift. For example, the cost of gift wrapping is considered an incidental cost. However, the purchase of an ornamental basket for packaging fruit is not considered an incidental cost of packaging if the basket has a substantial value compared to the value of the fruit.

Exceptions. The following items are not subject to the \$25 limit for business gifts.

- 1) An item that costs \$4 or less and:
 - a) Has your name clearly and permanently imprinted on the gift, and
 - b) Is one of a number of identical items you widely distribute.

Examples include pens, desk sets, and plastic bags and cases.

- 2) Signs, display racks, or other promotional material to be used on the business premises of the recipient.

Employee achievement awards. Employee achievement awards are not treated as gifts. For information on the requirements you must meet in order to deduct the cost of these awards, see *Bonuses and Awards* in Chapter 2 of Publication 535.

Gift or entertainment. Any item that might be considered either a gift or an entertainment expense generally will be considered an entertainment expense. However, if you give a customer packaged food or beverages that you intend the customer to use at a later date, treat it as a gift expense.

If you give tickets to a theater performance or sporting event to a business customer and you do not go with the customer to the performance or event, you can choose to treat the tickets as either a gift or entertainment expense, whichever is to your advantage.

You can change your treatment of the tickets at a later date, but not after the time allowed for the assessment of income tax. In most instances, this assessment period ends 3 years after the due date of your income tax return. But if you go with the customer to the event, you must treat the cost of the tickets as an entertainment expense. You cannot choose, in this case, to treat the tickets as a gift expense.

4.

Local Transportation Expenses

This chapter discusses expenses you can deduct for local business transportation. It introduces deductions you can take for business use of your car. However, it does not discuss tax treatment of car expenses. For information on rules for deducting actual operating expenses, the standard mileage rate, partial business use, car leasing rules, reimbursements, etc., get Publication 917.

Local transportation expenses include the ordinary and necessary expenses of getting from one workplace to another in the course of your business or profession when you are traveling within your tax home area. Tax home is defined in Chapter 1.

The following discussion applies to you if you have a regular or main job away from your residence. If your principal place of business is in your home, see *Office in the home*, later.

Local transportation expenses also include the cost of getting from your home to a temporary workplace when you have one or more regular places of work. These temporary workplaces can be either within the area of your tax home or outside that area.

Local business transportation does *not* include expenses you have while traveling away

from home overnight. Expenses for transportation while traveling away from home overnight are deductible as travel expenses and are discussed in Chapter 1.

Local business transportation expenses include the cost of transportation by air, rail, bus, taxi, etc., and the cost of driving and maintaining your car.

You can deduct your expenses for local business transportation if the expenses are ordinary and necessary. An ordinary expense is one that is common and accepted in your field of trade, business, or profession. A necessary expense is one that is helpful and appropriate for your business. An expense does not have to be indispensable to be considered necessary.

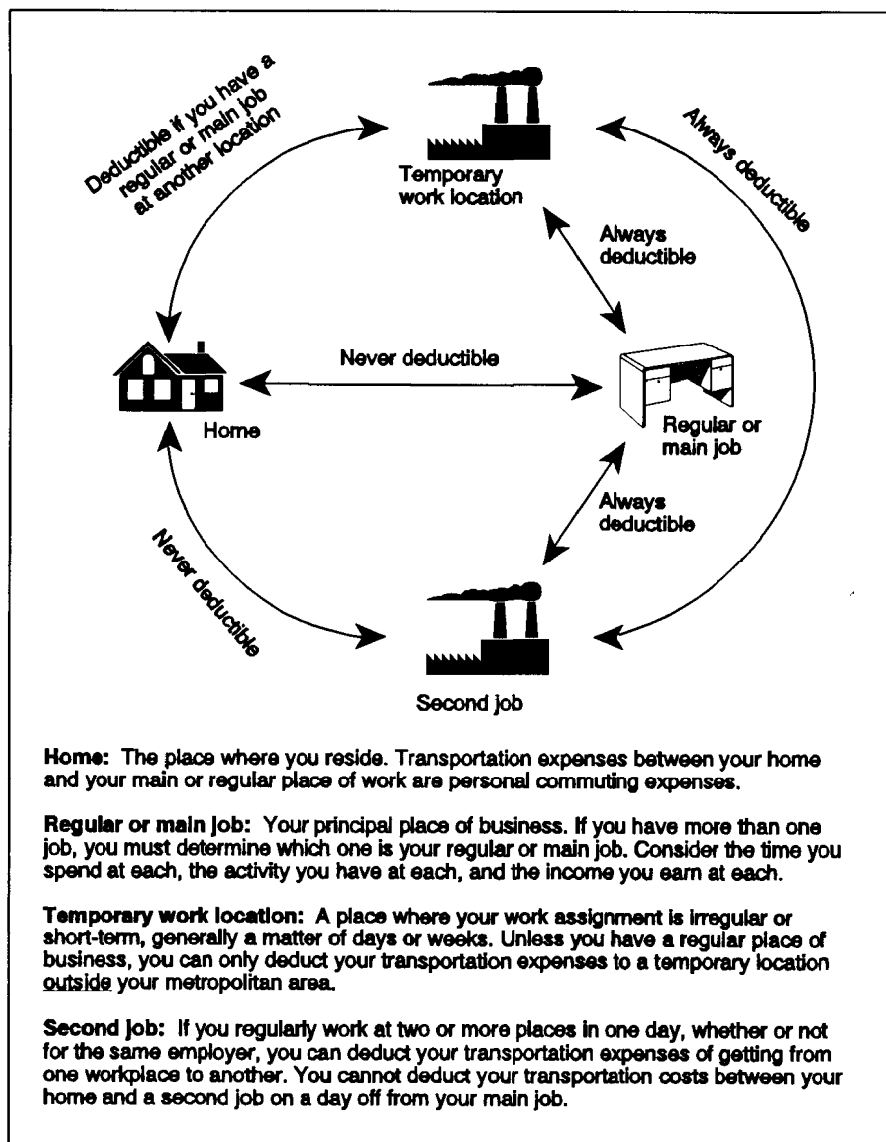
Temporary work location. If you have one or more regular places of business and commute to a temporary work location, you can deduct

the expenses of the daily round-trip transportation between your residence and the temporary location. The temporary work must be irregular or short term (generally a matter of days or weeks).

If the temporary work location is beyond the general area of your regular place of work, and you stay overnight, you are traveling away from home and may have deductible travel expenses as discussed in Chapter 1.

If you do not have a regular place of work, but you ordinarily work at different locations in the metropolitan area where you live, you can deduct daily transportation costs between your home and a temporary work site *outside* your metropolitan area. Generally, a metropolitan area includes the area within the city limits and the suburbs that are considered part of that metropolitan area. You cannot deduct daily transportation costs between your home and temporary work sites *within* your metropolitan

Figure B. When Are Local Transportation Expenses Deductible?
(Do not use this chart if your home is your principal place of business. See *Office in the home*.)



area. These are nondeductible commuting costs.

Two places of work. If you work at two places in a day, whether or not for the same employer, you can deduct the expense of getting from one workplace to the other. However, if for some personal reason you do not go directly from one location to the other, you can deduct only the amount it would have cost you to go directly from the first location to the second. Transportation expenses you have in going between home and a part-time job on a day off from your main job are commuting expenses. You cannot deduct them.

Commuting expenses. You cannot deduct the costs of taking a bus, trolley, subway, or taxi, or driving a car between your home and your main or regular place of work. These costs are personal commuting expenses. You cannot deduct commuting expenses no matter how far your home is from your regular place of work. You cannot deduct commuting expenses even if you work during the commuting trip.

Example. You had a telephone installed in your car. You sometimes use that telephone to make business calls while commuting to and from work. Sometimes business associates ride with you to and from work, and you have a business discussion in the car. These activities do not change the trip's expenses from commuting to business. You cannot deduct your commuting expenses.

Parking fees. Fees you pay to park your car at your place of business are nondeductible commuting expenses. You can, however, deduct business-related parking fees when visiting a customer or client.

Advertising display on car. The use of your car to display material that advertises your business does not change the use of your car from personal use to business use. If you use this car for commuting or other personal uses, you cannot deduct your expenses for such uses. Commuting or personal expenses are not deductible.

Office in the home. If you have an office in your home that qualifies as a **principal place of business**, you can deduct your daily transportation costs between your home and another work location in the same trade or business. (See Publication 587, *Business Use of Your Home*, for information on determining if your home office qualifies as a principal place of business.)

If your home office does not qualify as a principal place of business, follow the rules explained earlier.

Examples of deductible local transportation. The following examples illustrate when you can deduct local transportation expenses based on the location of your work and your home.

Example 1. Your office is in the same city as your home. You cannot deduct the cost of transportation between your home and your office. This is a personal commuting expense.

You can deduct the cost of round-trip transportation between your office and a client's or customer's place of business.

Example 2. You regularly work in an office in the city where you live. Your employer requires that you attend a one-week training session at a different office in the same city. You travel directly from your home to the training location and return each day. You can deduct the cost of your daily round-trip transportation between your home and the training location.

Example 3. Your principal place of business is in your home. (The rules for "principal place of business" are discussed in Publication 587, *Business Use of Your Home*.) You can deduct the round-trip business-related local transportation expenses between your qualifying home office and your client's or customer's place of business. You must, however, distinguish between business and personal transportation.

Example 4. You have no regular office, and you do not have an office in your home. In this case, the location of your first business contact is considered your office. Transportation expenses between your home and this first contact are nondeductible commuting expenses. In addition, transportation expenses between your last business contact and your home are also nondeductible commuting expenses. Although you cannot deduct the costs of these trips, you can deduct the costs of going from one client or customer to another.

Illustration of local transportation. *Figure B* illustrates the rules for when you can deduct local transportation expenses when you have a regular or main job away from your residence. You may want to refer to it when deciding whether you can deduct your local business transportation expenses.

Car Expenses

If you use your car for business purposes, you may be able to deduct car expenses. You generally can use one of two methods to figure your expenses: actual expenses or the standard mileage rate.

Note: You may be entitled to a tax credit for an electric vehicle or a deduction from gross income for a part of the cost of a clean-fuel vehicle if you place one of these vehicles in service from July 1, 1993, through December 31, 2004. The vehicle must meet certain requirements, and you do not have to use it in your business to qualify for the credit or the deduction. For more information, see Chapter 15 of Publication 535.

Actual Expenses

If you choose to deduct actual expenses, you can deduct the cost of the following items:

Depreciation	Lease fees	Rental fees
Garage rent	Licenses	Repairs
Gas	Oil	Tires
Insurance	Parking fees	Tolls

Business and personal use. If you use your car for both business and personal purposes, you must divide your expenses between business and personal use.

Leasing a car. If you lease a car that you use in your business, you can deduct the part of each lease payment that is for the use of the car in your business. You cannot deduct any part of a lease payment that is for commuting to your regular job or for any other personal use of the car.

You must spread any advance payments over the entire lease period. You cannot deduct any payments you make to buy a car even if the payments are called lease payments.

If you lease a car for 30 days or more, you may have to include an "inclusion amount" in your income. For more information, see Chapter 3 of Publication 917.

Additional information. See Chapter 2 of Publication 917 for information on depreciation and the section 179 deduction.

Standard Mileage Rate

Instead of figuring actual expenses, you may be able to use the standard mileage rate to figure the deductible cost of operating your car, van, pickup, or panel truck for business purposes. You can use the standard mileage rate only for a car that you own. For 1994, the standard mileage rate is **29 cents** a mile for all business miles (43.5 cents a mile for U.S. Postal Service employees with rural routes).

Choosing the standard mileage rate. If you want to use the standard mileage rate for a car, you must choose to use it in the first year you place the car in service in business. Then in later years, you can choose to use the standard mileage rate or actual expenses.

If you choose to use the standard mileage rate, you must follow certain rules. These rules are explained in Chapter 2 of Publication 917.

Parking fees and tolls. In addition to using the standard mileage rate, you can deduct any business-related parking fees and tolls. (Parking fees that you pay to park your car at your place of work are nondeductible commuting expenses.)

5.

Recordkeeping

This chapter discusses the written records you need to keep if you plan to deduct an expense discussed in this publication. By keeping timely and accurate records, you will have support to show the IRS if your tax return is ever examined. Or, your employer may require

proof of expenses for which you are reimbursed under an accountable plan, as discussed in Chapter 6 under *Adequate Accounting*.

If you use your car for work or business, see Chapter 4 of Publication 917 for information on records necessary to prove car expenses.

Proof required. You must be able to prove (substantiate) your deductions for travel, entertainment, business gift, and local transportation expenses. You should keep adequate records or have sufficient evidence that will support your own statement. Estimates or approximations do not qualify as proof of an expense.

Timely recordkeeping. You do not need to write down the elements of every expense at the time of the expense. However, a record of the elements of an expense or of a business use made at or near the time of the expense or use, and supported by sufficient documentary evidence, has more value than a statement prepared later when generally there is a lack of accurate recall. A log maintained on a weekly basis, which accounts for use during the week, is considered a record made at or near the time of the expense or use.

Duplicate information. You do not have to record information in your account book or other record that duplicates information shown on a receipt as long as your records and receipts complement each other in an orderly manner. You do not have to record amounts your employer pays directly for any ticket or other travel item. However, if you charge these items to your employer, through a credit card or otherwise, you must keep a record of the amounts you spend.

Expense accounts. An expense account statement you give your employer, client, or customer is considered to have been made at or near the time of the expense or use. The statement must be copied from your account book, diary, statement of expense, or similar record.

How to Prove Expenses

You can deduct the expenses described in this publication only if you can prove certain elements of expense. This section discusses items you need to prove depending on which expense you are deducting.

You cannot deduct amounts that you approximate or estimate or amounts that are considered lavish or extravagant. A receipt is ordinarily the best evidence to prove the amount of an expense.

Chart that shows proof required. *Table 4* summarizes the factors to use in proving the elements of your expenses for travel, entertainment, gifts, and local business transportation.

To deduct these expenses, you must be able to prove the elements listed in column 1 of

the chart. You prove these elements by having the information and receipts (where required) for the expenses listed in columns 2, 3, 4, or 5, whichever apply.

Adequate records. You should keep the proof you need for these items in an account book, diary, statement of expense, or similar record, and keep adequate documentary evidence (such as receipts, canceled checks, or bills), that together will support each element of an expense. Written evidence has considerably more value than oral evidence alone.

Proof of Travel Expenses

To deduct travel expenses, you must be able to prove the following four elements:

- 1) Each separate amount you spent for travel away from home, such as the cost of your transportation or lodging. You may total the daily cost of your breakfast, lunch, and dinner, and other incidental elements of such travel if they are listed in reasonable categories, such as meals and taxi fares. If your employer reimburses you using a per diem allowance (including a meals only allowance), you may not need proof of separate amounts spent for meals, lodging, or incidental expenses. See *Proving your expenses with a per diem allowance* in Chapter 6 under *Adequate Accounting*.
- 2) The dates you left and returned home for each trip, and the number of days spent on business while traveling away from home.
- 3) The destination or the area of your travel, described by the name of the city, town, or similar designation.
- 4) The business reason for your travel or the business benefit gained (or expected to be gained) from your travel.

You must also follow the rules explained later under *Additional Recordkeeping Rules*.

Proof of Entertainment Expenses

To deduct entertainment expenses, including entertainment-related meals, you must be able to prove the following six elements:

- 1) The amount of each separate entertainment expense. Incidental items, such as taxi fares and telephone calls, may be totaled on a daily basis.
- 2) The date the entertainment took place.
- 3) The name (if any), address or location, and the type of entertainment, such as dinner or theater, if the information is not apparent from the name of the place.
- 4) The business reason for the entertainment, or the business benefit gained or expected to be gained, and the nature of any business discussion or activity that took place.

- 5) The occupation or other information about the person or persons for whom the entertainment expense is being claimed. Include name, title, or other designation sufficient to establish the business relationship to you.
- 6) The presence of you or your employee at a business meal given for a client.

You must also follow the rules explained later under *Additional Recordkeeping Rules*.

If you entertain a large number of people, you do not have to record each person's name in a readily identifiable group of people. It is enough to designate the class. For example, if you entertain all stockholders of a small corporation, an entry such as "all stockholders of the Acme Corporation" is enough. However, if the identity of the class is not enough to identify the persons entertained, then each person's name must be listed.

Before or after business discussion. To deduct the cost of meals or entertainment directly before or after a business discussion, you must be able to:

- 1) Prove items (1), (2), (3), (5), and (6) just listed,
- 2) Prove the date, place, and duration of the business discussion,
- 3) Show the nature of the business discussion and the business reason for the entertainment or the business benefit gained (or expected to be gained), and
- 4) Identify the people who participated in both the business discussion and in the entertainment activity.

Season or series tickets. Treat each ticket in the series as a separate item. To determine the cost of individual tickets, divide the total cost (but not more than face value) by the number of games or performances in the series. You must keep records to show whether each ticket is used as a gift or entertainment. Also, you must be able to prove the cost of nonluxury box seat tickets if you rent a skybox or other private luxury box for more than one event. See *Entertainment tickets* in Chapter 2.

Proof of Gift Expenses

To deduct gift expenses, you must be able to prove the following five elements:

- 1) The cost of the gift,
- 2) The date you gave the gift,
- 3) A description of the gift,
- 4) The reason for giving the gift or the business benefit gained (or expected to be gained from giving it), and
- 5) The occupation or other information about the person receiving the gift, including name, title, or other designation to establish his or her business relationship to you.

If you have receipts for your gift expenses, you can record the information for elements (4)

Table 4. Elements To Prove Certain Business Expenses

Element to be proved (1)	Expense			
	Travel (2)	Entertainment (3)	Gift (4)	Transportation (car) (5)
Amount	Amount of each separate expense for travel, lodging, and meals. Incidental expenses may be totaled in reasonable categories, such as taxis, daily meals for traveler, etc.	Amount of each separate expense. Incidental expenses such as taxis, telephones, etc., may be totaled on a daily basis.	Cost of gift.	1) Amount of each separate expense including cost of the car, 2) Mileage for each business use of the car, and 3) Total miles for the tax year.
Time	Date you left and returned for each trip, and number of days for business.	Date of entertainment. For meals or entertainment directly before or after a business discussion, the date and duration of the business discussion.	Date of gift.	Date of the expense or use.
Place	Name of city or other designation.	Name and address or location of place of entertainment. Type of entertainment if not otherwise apparent. Place where business discussion was held if entertainment is directly before or after a business discussion.	Not applicable.	Name of city or other designation if applicable.
Description	Not applicable.	Not applicable.	Description of gift.	Not applicable.
Business Purpose	Business reason for travel or the business benefit gained or expected to be gained.	Business reason or the business benefit gained or expected to be gained. Nature of business discussion or activity.	Business reason for giving the gift or the business benefit gained or expected to be gained.	Business reason for the expense or use of the car.
Business Relationship	Not applicable.	Occupations or other information—such as names or other designations—about persons entertained that shows their business relationship to you. If all people entertained did not take part in business discussion, identify those who did. You must also prove that you or your employee was present if entertainment was a business meal.	Occupation or other information—such as name or other designation—about recipient that shows his or her business relationship to you.	Not applicable.

and (5) on your receipts. The receipts should include the information for elements (1) through (3).

Name of recipient. The name of the recipient of a business gift does not always have to be recorded. A general listing will be enough if it is evident that you are not trying to avoid the \$25 annual limit on the amount you can deduct for gifts to any one person. For example, if you buy a large number of tickets to local high school basketball games and give one or two tickets to each of a number of customers, it is usually enough to record a general description of the recipients.

You must also follow the rules explained later under *Additional Recordkeeping Rules*.

Proof of Local Business Transportation Expenses

To deduct local business transportation expenses, you must be able to prove the following four elements:

- 1) The cost of the transportation,
- 2) The date of the transportation,
- 3) Your business destination, and
- 4) The reason for the expense, unless the business purpose, such as a sales route, is clear from the surrounding circumstances.

You must also follow the rules explained later under *Additional Recordkeeping Rules*.

Business use of a car. If you use your car or other vehicle for business purposes, you must keep written records of other items. These additional requirements are discussed in Chapter 4 of Publication 917.

Additional Recordkeeping Rules

This section discusses rules that may apply to more than one type of expense.

Separating expenses. Each separate payment usually is considered a separate expense. If you entertain a customer or client at dinner and then go to the theater, the dinner expense and the cost of the theater tickets are two separate expenses. You must record them separately in your records.

Totaling items. You may make one daily entry for reasonable categories of expenses such as taxi fares, telephone calls, or other incidental travel costs. Meals should be in a separate category. You should include tips with the costs of the services you received.

Expenses of a similar nature occurring during the course of a single event are considered

a single expense. For example, if during entertainment at a cocktail lounge, you pay separately for each serving of refreshments, the total expense for the refreshments is treated as a single expense.

Documentary evidence. You generally must have documentary evidence, such as receipts, canceled checks, or bills, to support your expenses. However, this evidence is not required if:

- 1) You have meals or lodging expenses while traveling away from home for which you account to your employer under an accountable plan and you use a per diem allowance method that includes meals and/or lodging,
- 2) Your expense, other than lodging, is less than \$25, **or**
- 3) You have a transportation expense for which a receipt is not readily available.

Accountable plans and per diem allowances are discussed in Chapter 6.

Adequate evidence. Documentary evidence ordinarily will be considered adequate if it shows the amount, date, place, and essential character of the expense.

For example, a hotel receipt is enough to support expenses for business travel if it has:

- 1) The name and location of the hotel,
- 2) The dates you stayed there, and
- 3) Separate amounts for charges such as lodging, meals, and telephone calls.

A restaurant receipt is enough to prove an expense for a business meal if it has:

- 1) The name and location of the restaurant,
- 2) The number of people served, and
- 3) The date and amount of the expense.

If a charge is made for items other than food and beverages, the receipt must show that this is the case.

Canceled check. A canceled check, together with a bill from the payee, ordinarily establishes the cost. However, a canceled check by itself does not prove a business expense without other evidence to show that it was for a business purpose.

Business purpose. A written statement of the business purpose of an expense is generally needed. However, the degree of proof varies according to the circumstances in each case. If the business purpose of an expense is clear from the surrounding circumstances, a written explanation is not needed.

Example. A sales representative who calls on customers on an established sales route does not have to submit a written explanation of the business purpose for traveling that route.

Confidential information. Confidential information relating to an element of a deductible expense, such as the place, business purpose, or business relationship, need not be put in your account book, diary, or other record.

However, the information has to be recorded elsewhere at or near the time of the expense and be available to fully prove that element of the expense.

Incomplete records. If you prove the total cost of travel or entertainment but you cannot prove how much it cost for each person, you must divide the cost among you and your guests if such a determination is necessary. To do so, divide the total cost by the total number of persons. The result is the amount you use to figure your deductible expense for each qualifying person. See *Allocating between business and nonbusiness expenses* in Chapter 2.

Inadequate records. If you do not have adequate records to prove an element of an expense, then you must prove the element by:

- 1) Your own statement, whether written or oral, that contains specific information about the element, and
- 2) Other supporting evidence that is sufficient to establish the element.

If the element is the description of a gift, or the cost, time, place, or date of an expense, there must be direct evidence. This evidence may be a written statement or the oral testimony of your guests or a witness, which gives detailed information about the element or documentary evidence. If the element is either the business relationship of your guests or the business purpose of the amount spent, the evidence may be circumstantial.

Exceptional circumstances. Other evidence may be allowed if, because of the nature of the situation in which an expense is made, you cannot get a receipt. This applies if **all** the following are true.

- 1) You were unable to obtain evidence for an element of the expense or use that conforms fully to the adequate records requirements.
- 2) You are unable to obtain evidence for an element that conforms fully to the rules listed earlier under *Inadequate records*.
- 3) You have presented other evidence for the element that is the best proof possible under the circumstances.

In this case, such other evidence is considered to satisfy the substantiation requirements.

Destroyed receipts. You can prove a deduction by reconstructing your expenses if you cannot produce a receipt for reasons beyond your control, such as fire, flood, or other casualty.

Additional information for the IRS. The IRS may require additional information to clarify or to establish the accuracy or reliability of information contained in your records, statements, testimony, or documentary evidence before a deduction is allowed.

How Long to Keep Records and Receipts

You must keep proof to support your claim to a deduction as long as your income tax return

can be examined. Generally, it will be necessary for you to keep your records for 3 years from the date you file the income tax return on which the deduction is claimed. A return filed early is considered as filed on the due date.

Employees who give their records and documentation to their employers and are reimbursed for their expenses generally do not have to keep duplicate copies of this information. However, you may have to prove your expenses if:

- 1) You claim deductions for expenses that are more than reimbursements,
- 2) Your expenses are reimbursed under a nonaccountable plan,
- 3) Your employer does not use adequate accounting procedures to verify expense accounts, or
- 4) You are related to your employer as defined under *Standard Meal Allowance* in Chapter 1.

See Chapter 6 for a discussion of reimbursements, adequate accounting, and nonaccountable plans.

Examples

Examples 1 through 3 show the information you need to keep for different types of expenses.

Example 1. You are a vice president of Zave Mfg. Corp. and you live in Chicago, where the home office of the company is located. On March 9, you travel by airplane from Chicago to Dallas, where you inspect a company plant. You return to Chicago the evening of March 10. During the stay in Dallas, you entertain Charles Young, the purchasing agent of the Sharpe Co., a prospective customer of the company. You prepare the following statement of expenses:

Travel Expenses:

Trip to Dallas to inspect Dallas plant		
Date	Item	Amount
March 9	Air fare, round trip	\$250.00
	Lunch & tip	12.00
	Lodging	66.00
March 10	Meals & tips	35.50
	Auto rental, 2 days	46.00
	Telephone	6.50

Entertainment Expenses:

Date	Item/Place	Amount
March 9	Dinner & tip/Ajax Grill, Dallas	\$ 62.50
	Purpose/Relationship	
	Discussed purchase contract with C. Young, Purchasing Agent for Sharpe Co.	

You have receipts for your expenses for lodging, air travel, auto rental, meals, and entertainment. If Zave Mfg. Corp. reimburses you for the exact amount you spent, requires a statement of expenses with the receipts, and verifies and keeps the records and receipts, Zave is subject to the 50% limit and will be responsible for proving the expenses for which it

reimbursed you. You ordinarily will not be required to prove this expense account information again.

Example 2. You are an architect and have submitted plans to the Modern Real Estate Investment Trust for an apartment building that the trust wants to build. To discuss and promote these plans, you invite the president of the trust to lunch. You prepare, at or near the time of your expense, the following statement of expenses:

Entertainment Expenses:

Apr. 6—Lunch and tip (\$24.00); Cafe Plaza, Rome, N.Y., with president of Modern R.E. Investment Trust concerning plans for Claremont Village Apts.

You do not have to get a receipt from the Cafe Plaza because the amount is less than \$25.

Example 3. You are the president of Yates Corp., and you have a substantial business discussion with three officers of Acme Corp. Afterward, all of you go to the Quantum Club where you pay \$24 for drinks at the bar, including tip. All of you then go to the club's dining room where you pay \$118 for dinner, taxes, and tip. You prepare the following statement of expenses:

Entertainment Expenses:

Jan. 14—Taxi and tip (\$8.55); Drinks at bar and tip (\$24); dinner (\$98) and tip (\$20) at Quantum Club, Wash., D.C.; Entertainment of the pres., v. pres., and treas. of the Acme Corp., following our business meeting at my office all afternoon re distributorship arrangements between Yates and Acme Corps.

You should get a receipt for the dinner bill because it is more than \$25. If Yates Corp. reimburses you for the exact amount you spent, requires a statement of expenses, and verifies and keeps the records, then the Yates Corp. is subject to the 50% limit on entertainment and will be responsible for proving the expenses for which it reimbursed you. You ordinarily will not be required to prove this expense account information again.

6. How to Report

This chapter explains how to report on your tax return the expenses that are discussed in this publication. It discusses reimbursements, including treatment of accountable and nonaccountable plans, adequate accounting, and per diem allowances. The chapter ends by showing you how to complete Form 2106.

General Information

This section provides general information on where to report the expenses discussed in this publication.

Self-employed. If you are self-employed, you must report your income and expenses on Schedule C or C-EZ (Form 1040) if you are a sole proprietor, or on Schedule F (Form 1040) if you are a farmer. You do not use Form 2106 or Form 2106-EZ.

If you file Schedule C, report:

- 1) Your travel expenses, except meals, on line 24a,
- 2) Your meals (actual cost or standard meal allowance) and entertainment on line 24b,
- 3) Your business gift expenses on line 27, and
- 4) Your local business transportation expenses, other than car and truck expenses, on line 27.

See Publication 917 for information about car and truck expenses.

If you file Schedule C-EZ, report the total of all business expenses on line 2.

If you file Schedule F, see Publication 225 for information on how to complete your tax return.

Both self-employed and an employee. If you are both self-employed and an employee, you must keep separate records for each business activity. Report your business expenses for self-employment on Schedule C, Schedule C-EZ, or on Schedule F, as discussed earlier. Report your business expenses for your work as an employee on Form 2106 or Form 2106-EZ, as discussed next.

Employees. If you are an employee, you generally must complete Form 2106 to deduct your travel, transportation, and entertainment expenses. However, you can use Form 2106-EZ instead of Form 2106 if you meet both of the following conditions.

- 1) You were not reimbursed for your expenses or, if you were reimbursed, the reimbursements were included in your income (box 1 of your Form W-2).
- 2) If you claim car expenses, you use the standard mileage rate.

For more information on how to report your expenses on Forms 2106 and 2106-EZ, see *Completing Forms 2106 and 2106-EZ*, later.

Gifts. If you did not receive any reimbursements (or the reimbursements were all included in box 1 of your Form W-2) and the only business expense you are claiming is for business gifts, do not complete Form 2106 or 2106-EZ. Instead, claim the amount of your deductible business gifts directly on Schedule A. Otherwise, you must complete Form 2106 or 2106-EZ.

Statutory employees. If you received a Form W-2 and the "Statutory employee" box in box 15 was checked, report your income

and expenses related to that income on Schedule C or C-EZ (Form 1040). Do not complete Form 2106 or Form 2106-EZ. See your Form 1040 instructions for more information.

Statutory employees include full-time life insurance salespersons, certain agent or commission drivers, traveling salespersons, and certain homeworkers.

Unclaimed reimbursement. If you are entitled to a reimbursement from your employer but you do not claim it, you cannot claim a deduction for the expenses to which that reimbursement applies.

Reimbursement for personal expenses. If your employer reimburses you for nondeductible personal expenses, such as for vacation trips, you must report the reimbursement as wage income on your tax return. You cannot deduct personal expenses.

Income-producing property. If you have travel or transportation expenses for income-producing property, report your deductible expenses on the form appropriate for that activity.

For example, if you have rental income and expenses, report your expenses on Schedule E, *Supplemental Income and Loss*. See Publication 527, *Residential Rental Property*, for more information on the rental of real estate. If you have deductible investment-related transportation expenses, report them on line 22 of Schedule A (Form 1040).

Reimbursements

This section explains what to do when you receive an advance or are reimbursed for any of the employee business expenses discussed in this publication.

If you received an advance, allowance, or reimbursement for your expenses, how you report this amount and your expenses depends on whether the reimbursement was paid to you under an accountable plan or a nonaccountable plan.

This section explains the two types of plans, how per diem allowances simplify proving the amount of your expenses, and the tax treatment of your reimbursements and expenses. It also covers rules for independent contractors.

Reimbursement, allowance, or advance. A reimbursement or other expense allowance arrangement is a system or plan that an employer uses to pay, substantiate, and recover the expenses, advances, reimbursements, and amounts charged to the employer for employee business expenses. It can also be a system used to keep track of amounts you receive from your employer's agent or a third party. Arrangements include per diem and mileage allowances. If a single payment includes both wages and an expense reimbursement, the amount of the reimbursement must be specifically identified.

Table 5. Reporting Travel, Entertainment, and Gift Expenses and Reimbursements

Type of Reimbursement (or Other Expense Allowance) Arrangement	Employer Reports on Form W-2	Employee Shows on Form 2106 ¹
Accountable		
Actual expense reimbursement Adequate accounting and excess returned	Not reported	Not shown if expenses do not exceed reimbursement
Actual expense reimbursement Adequate accounting and return of excess both required but excess not returned	Excess reported as wages in box 1. ² Amount adequately accounted for is reported only in box 13—it is <i>not</i> reported in box 1.	All expenses (and reimbursements reported on Form W-2, box 13) <i>only</i> if some or all of the excess expenses are claimed. ³ Otherwise, form is not filed.
Per diem or mileage allowance (up to federal rate) Adequate accounting and excess returned	Not reported	All expenses and reimbursements <i>only</i> if excess expenses are claimed. ³ Otherwise, form is not filed.
Per diem or mileage allowance (exceeds federal rate) Adequate accounting up to the federal rate only and excess not returned	Excess reported as wages in box 1. ² Amount up to the federal rate is reported only in box 13—it is <i>not</i> reported in box 1.	All expenses (and reimbursements equal to the federal rate) <i>only</i> if expenses in excess of the federal rate are claimed. ³ Otherwise, form is not filed.
Nonaccountable		
Either adequate accounting or return of excess, or both, not required by plan	Entire amount is reported as wages in box 1. ²	All expenses ³
No reimbursement	Normal reporting of wages, etc.	All expenses ³

¹ You may be able to use Form 2106-EZ. See *Completing Forms 2106 and 2106-EZ* in Chapter 6.

² Excess is also reported in boxes 3 and 5, if applicable.

³ Any allowable business expense is carried to line 20 of Schedule A (Form 1040) and deducted as a miscellaneous itemized deduction.

Mileage allowances are discussed in Chapter 5 of Publication 917.

Your employer has different options for reimbursing you for business-related travel expenses:

- 1) Reimbursing you for your actual expenses, as discussed throughout this publication,
- 2) Using the meals only allowance (discussed later) to reimburse your meals and incidental expenses and reimbursing you for your actual lodging expenses,
- 3) Using the regular federal per diem rate (discussed later),
- 4) Using the high-low method (discussed later), or
- 5) Reimbursing you under any other method that is acceptable to the IRS.

Your employer should tell you what method of reimbursement is used and what records you must submit.

No reimbursement. You are not reimbursed or given an allowance for your expenses if you are paid a salary or commission with the understanding that you will pay your own expenses. In this situation, you have no reimbursement or allowance arrangement, and you deduct your expenses using either Form 2106 or Form 2106-EZ and Schedule A (Form 1040), or only Schedule A (Form 1040) if you are only claiming business gift expenses. You do not have to read this section on reimbursements. Instead, see *Completing Forms 2106 and 2106-EZ*, later, for information on completing your tax return.

Employers. If you are an employer and you reimburse employee business expenses, how you treat this reimbursement on your employee's Form W-2 depends in part on whether you have an accountable plan. Reimbursements treated as paid under an accountable plan, as explained next, are not reported as compensation. Reimbursements treated as paid under nonaccountable plans, as explained later, are

reported as compensation. See Publication 15, *Circular E, Employer's Tax Guide*, for information on employee compensation.

Accountable Plans

To be an accountable plan, your employer's reimbursement or allowance arrangement must include all three of the following rules:

- 1) Your expenses must have a business connection — that is, you must have paid or incurred deductible expenses while performing services as an employee of your employer,
- 2) You must adequately account to your employer for these expenses within a reasonable period of time, and
- 3) You must return any excess reimbursement or allowance within a reasonable period of time.

"Adequate accounting" and "returning excess reimbursements" are discussed later.

An **excess reimbursement or allowance** is any amount you are paid that is more than the business-related expenses that you adequately accounted for to your employer. See *Returning Excess Reimbursements* later in this chapter for information on how to handle these excess amounts.

Reasonable period of time. The definition of "reasonable period of time" depends on the facts of your situation. The IRS will consider it reasonable for you to:

- 1) Receive an advance within 30 days of the time you have an expense,
- 2) Adequately account for your expenses within 60 days after they were paid or incurred, and
- 3) Return any excess reimbursement within 120 days after the expense was paid or incurred.

If you are given a periodic statement (at least quarterly) that asks you to either return or adequately account for outstanding advances and you comply within 120 days of the statement, the IRS will consider the amount adequately accounted for or returned within a reasonable period of time.

Employee meets accountable plan rules. If you meet the three rules for accountable plans, your employer should not include any reimbursements in your income in box 1 of your Form W-2. If your expenses equal your reimbursement, you do not complete Form 2106. You have no deduction since your expenses and reimbursement are equal.

Note: If your employer included reimbursements in box 1 of your Form W-2 and you meet all three rules for accountable plans, ask your employer for a corrected Form W-2.

Employee does not meet accountable plan rules. You may be reimbursed under your employer's accountable plan but only part of your expenses may meet all three rules.

If your expenses are reimbursed under an otherwise accountable plan but you do not return, within a reasonable period of time, any reimbursement of expenses for which you did not adequately account, then only the amount for which you did adequately account is considered as paid under an accountable plan. The remaining expenses are treated as having been reimbursed under a nonaccountable plan (discussed later in this chapter).

If you receive an allowance or advance that is higher than the federal rate, see *Returning Excess Reimbursements*, later.

Reimbursement of nondeductible expenses. You may be reimbursed under your employer's accountable plan for expenses related to that employer's business, some of which are deductible as employee business expenses and some of which are not deductible. The reimbursements received for the nondeductible expenses are treated as paid under a nonaccountable plan.

Example. Your employer's plan may reimburse you for travel expenses while away from home on business, and for meals when you work late, even though you are not away from home. The part of the arrangement that reimburses you for the nondeductible meals when you work late at the office is treated as a second arrangement. The payments under this second arrangement are treated as paid under a nonaccountable plan.

Per diem allowances. If you are reimbursed by a per diem allowance (daily amount) that you received under an accountable plan, two facts affect your reporting:

- 1) The federal rate for the area where you traveled, and
- 2) Whether the allowance or your actual expenses were more than the federal rate.

For this purpose, the **federal rate** can be figured by using any one of three methods:

- 1) The regular federal per diem rate (discussed later),
- 2) The high-low method (discussed later), or
- 3) The standard meal allowance (discussed in Chapter 1).

The following discussions explain where to report your expenses depending upon how the amount of your per diem allowance compares to the federal rate.

Per diem allowance LESS than or EQUAL to the federal rate. If your per diem allowance is less than or equal to the federal rate, the allowance will not be included in boxes 1, 3, and 5 of your Form W-2. You do not need to report the related expenses or the per diem allowance on your return if your expenses are equal to or less than the allowance.

However, if your actual expenses (or your expenses using the standard meal allowance) are more than your per diem allowance, you can complete Form 2106 and deduct the excess amount on Schedule A (Form 1040). If you are using actual expenses, you must be

able to prove to the IRS the total amount of your expenses and reimbursements for the entire year. If you are using the standard meal allowance, you do not have to prove that amount.

Example 1. In April Jeremy takes a 2-day business trip to Boston. The federal rate in Boston is \$139 per day. As required by his employer's accountable plan, he accounts for the time (dates), place, and business purpose of the trip. His employer reimburses him \$139 a day (\$278 total) for living expenses. Jeremy's living expenses in Boston are not more than \$139 a day.

Jeremy's employer does not include any of the reimbursement on his Form W-2 and Jeremy does not deduct the expenses on his return.

Example 2. The facts in Matt's case are the same as those in *Example 1* above. However, Matt's employer uses the high-low method (discussed later) to reimburse employees. Since Boston is a high-cost area, Matt is given an advance of \$152 a day (\$304 total) for his lodging, meals, and incidental expenses. Matt's actual expenses totaled \$390.

Matt is reimbursed under an accountable plan. However, since his \$390 of expenses exceed his \$304 advance, Matt itemizes his deductions in order to claim the excess expenses. Matt completes Form 2106 (showing **all** of his expenses and reimbursements). He must also allocate his reimbursement between his meals and other expenses as discussed later under *Completing Forms 2106 and 2106-EZ*.

Per diem allowance MORE than the federal rate. If your per diem allowance is more than the federal rate, your employer is required to include the allowance amount up to the federal rate in box 13 (code L) of your Form W-2. This amount is not taxable. However, the per diem allowance in excess of the federal rate will be included in box 1 (and in boxes 3 and 5 if applicable) of your Form W-2. You must report this part of your allowance as if it were wage income.

If your actual expenses are less than or equal to the federal rate, you do not complete Form 2106 or claim any of your expenses on your return.

However, if your actual expenses are more than the federal rate, you can complete Form 2106 and deduct those expenses that are more than the federal rate on Schedule A (Form 1040). You must report on Form 2106 your reimbursements up to the federal rate (as shown in box 13 of your Form W-2) and all your expenses. You should be able to prove these amounts to the IRS.

Example 1. Laura lives and works in Austin. Her employer sent her to Dallas for 2 days on business. Laura's employer paid the hotel directly for her lodging and reimbursed Laura \$40 a day (\$80 total) for meals and incidental expenses. Laura's actual meal expenses did not exceed the federal rate for Dallas which is \$34 per day.

Her employer included the \$12 excess over the federal rate [$(\$40 - \$34) \times 2$] in boxes 1, 3, and 5 of Laura's Form W-2. Her employer

shows \$68 ($\$34 \text{ a day} \times 2$) in box 13 of her Form W-2. This amount is not included in Laura's income. Laura does not have to complete Form 2106; however, she must include the \$12 excess in her gross income as wages (by reporting the total amount shown in box 1 of her Form W-2).

Example 2. Joe also lives in Austin and works for the same employer as Laura. In May the employer sent Joe to Washington, DC, and paid the hotel directly for Joe's hotel bill. The employer reimbursed Joe \$45 a day for his meals and incidental expenses. The federal rate for Washington, DC, is \$38 a day.

Joe can prove that his actual meal expenses totaled \$120. His employer's accountable plan will not pay more than \$45 a day for travel to Washington, DC, so Joe does not give his employer the records that prove that he actually spent \$120. However, he does account for the time, place, and business purpose of the trip. This is Joe's only business trip in 1994.

Joe was reimbursed \$90 ($\45×2 days), which is \$14 more than the federal rate of \$76 ($\38×2 days). The employer includes the \$14 as income on Joe's Form W-2 in boxes 1, 3, and 5. The employer also enters \$76 in box 13 of Joe's Form W-2, along with a code L.

Joe completes Form 2106 to figure his deductible expenses. He enters the total of his actual expenses for the year (\$120) on Form 2106. He also enters the reimbursements that were not included in his income (\$76). His total deductible expense, before the 50% limit, is \$44. After he figures the 50% limit on his unreimbursed meals and entertainment, he will enter the balance, \$22, on line 20 of Schedule A (Form 1040).

Employer's plan. The employer makes the decision whether to reimburse employees under an accountable plan or a nonaccountable plan. If you are an employee who receives payments under a nonaccountable plan, you cannot convert these amounts to payments under an accountable plan by voluntarily accounting to your employer for the expenses and voluntarily returning excess reimbursements to the employer.

Adequate Accounting

One of the three rules (listed earlier) for a reimbursement or other expense allowance arrangement to qualify as an accountable plan was that you adequately account to your employer for your expenses. You adequately account by giving your employer documentary evidence of your travel and other employee business expenses, along with a statement of expense, an account book, a diary, or a similar record in which you entered each expense at or near the time you had it. Documentary evidence includes receipts, canceled checks, and bills. See Chapter 5 for a discussion of the aspects or elements of each expense that you must prove.

You must account for **all** amounts received from your employer during the year as advances, reimbursements, or allowances for travel, entertainment, gifts, or any other expenses. This includes amounts that were

charged to your employer by credit card or other method. You must give your employer the same type of records and supporting information that you would have to give to the IRS if the IRS questioned a deduction on your return. You must pay back the amount of any reimbursement or other expense allowance for which you do not adequately account or that exceeds the amount for which you accounted.

Per diem allowance or reimbursement. You may be able to prove the amount of your expense by using a per diem allowance amount. If your employer reimburses you for your lodging, meal, and incidental expenses at a fixed amount per day of business travel, that amount is called a per diem allowance.

The term "incidental expenses" includes, but is not limited to, laundry expenses, cleaning and pressing expenses, and fees and tips for persons who provide services, such as food servers and luggage handlers. Incidental expenses do not include taxicab fares or the costs of telegrams or telephone calls.

A per diem allowance satisfies the adequate accounting requirements for the amount in question if:

- 1) Your employer reasonably limits payments of the travel expenses to those that are ordinary and necessary in the conduct of the trade or business,
- 2) The allowance is similar in form to and not more than the federal per diem (that is, your allowance varies based on where and how long you were traveling),
- 3) You are not related to your employer (as defined under *Standard Meal Allowance* in Chapter 1), and
- 4) The time, place, and business purpose of the travel are proved, as explained in Chapter 5.

If the IRS finds that an employer's travel allowance practices are not based on reasonably accurate estimates of travel costs, including recognition of cost differences in different areas, you will not be considered to have accounted to your employer. In this case, you may be required to prove your expenses to the IRS.

Allowance for meals. These rules also apply if you are reimbursed only for your meal expenses or get a separate per diem allowance for meals and incidental expenses. Your reimbursement or allowance must not be more than the standard meal allowance. A per diem allowance is paid separately for meals and incidental expenses if your employer furnishes lodging in kind, pays you a meal allowance plus the actual cost of your lodging, or pays the hotel, motel, etc., directly for your lodging. A per diem allowance is also paid separately for meals and incidental expenses if your employer does not have a reasonable belief that you incurred lodging expenses, such as when you stay with friends or relatives or sleep in the cab of your truck.

Proving your expenses with a per diem allowance. If your employer pays for your expenses using a per diem allowance, including

a meals only allowance, you can generally use the allowance as proof for the amount of your expenses. However, the amount of expense that can be proven this way cannot be more than the regular federal per diem rate or the high-low method, both discussed below.

The per diem allowance can only be used as proof of the cost of meals and/or lodging under the adequate accounting requirements. You must still provide other proof of the time, place, and business purpose for each expense.

Regular federal per diem rate. The regular federal per diem rate is the highest amount that the federal government will pay to its employees for lodging, meal, and incidental expenses (or meal and incidental expenses only) while they are traveling away from home in a particular area. The rates are different for different locations. You must use the rate in effect for the area where you stop for sleep or rest. Your employer should have these rates available. (Employers can get Publication 1542, which gives the rates in the continental United States for the current year.)

The federal rates for meal and incidental expenses are the same as those rates discussed under *Standard Meal Allowance* in Chapter 1.

High-low method. This is a simplified method of computing the federal per diem rate for travel within the continental United States. It eliminates the need to keep a current list of the per diem rate in effect for each city in the continental United States.

Under the high-low method, the per diem amount for travel on or after January 1, 1994, is \$152 for certain locations. All other areas have a per diem amount of \$95. The areas eligible for the \$152 per diem amount under the high-low method for all of the year or the portion of the year specified in parentheses under the key city name are listed in *Table 6*.

Allocation of per diem on partial days of travel. The federal per diem rate or the federal meal and incidental expenses rate is for a full 24-hour day of travel. If you travel for part of a day, the full day rate must be allocated. Either of the following methods can be used to figure the federal per diem for that day.

- 1) Count one-fourth of the federal rate for each 6-hour quarter of the day during any portion of which you are traveling away from home for business. The 6-hour quarters are midnight to 6 a.m.; 6 a.m. to noon; noon to 6 p.m.; and 6 p.m. to midnight.

Table 6. Locations Eligible for \$152 Per Diem Amount

Key City	County/Location*	Key City	County/Location*
California		Michigan	
Death Valley	Inyo	Mackinac Island (June 1-Sept. 30)	Mackinac
Gualala/Point Arena	Mendocino		
Los Angeles	Los Angeles, Kern, Orange, Ventura; Edwards AFB, China Lake Naval Center	Nevada	
	San Francisco	Steline (June 1-Sept. 30)	Douglas
San Francisco	El Dorado		
South Lake Tahoe (June 1-Sept. 30)		New Jersey	
Colorado		Atlantic City (June 1-Oct. 14)	Atlantic
Aspen	Pitkin	Newark	Bergen, Essex, Hudson, Passaic, Union Cape May
(Jan. 15-March 31)		Ocean City/Cape May (May 15-Sept. 30)	
Keystone/ Silverthorne	Summit		
Vail (Jan. 1-March 31)	Eagle	New Mexico	
District of Columbia		Santa Fe (May 1-Oct. 31)	Santa Fe
Washington, DC	Virginia counties of Arlington, Loudoun, and Fairfax and cities of Alexandria, Falls Church, and Fairfax. Maryland counties of Montgomery and Prince George's	New York	
Florida		Lake Placid (June 1-Nov. 14)	Essex
Fort Myers	Lee	New York City	Bronx, Brooklyn, Manhattan, Staten Island, Queens; Nassau, Suffolk Westchester
(Jan. 1-April 30)		White Plains	
Key West	Monroe	North Carolina	
Naples (Dec. 15-April 14)	Collier	Duck (May 1-Sept. 30)	Dare
Illinois		Pennsylvania	
Chicago	Cook, Lake, Du Page	Chester/Radnor Philadelphia	Delaware Philadelphia; city of Bala Cynwyd
Maryland (see also District of Columbia)		Rhode Island	
Ocean City (May 1-Sept. 30)	Worcester	Newport (May 1-Oct. 14)	Newport
Massachusetts		Virginia	See District of Columbia
Boston	Suffolk		
Cambridge/Lowell	Middlesex		
Hyannis (June 1-Sept. 30)	Barnstable		
Martha's Vineyard/ Nantucket	Nantucket, Dukes		

* Includes parishes, boroughs, military installations, etc.

- 2) Prorate the federal rate using any method that is consistently applied and is in accordance with reasonable business practice. For example, an employer can treat 2 full days of per diem paid for travel away from home from 9 a.m. of one day to 5 p.m. of the next day as being no more than the federal rate. This is true even though a federal employee would be limited to a reimbursement for only 1½ days.

These rules apply whether your employer uses the regular federal per diem rate or the high-low method.

Returning Excess Reimbursements

Under an accountable plan, you must be required to return any excess reimbursement or other expense allowances for your business expenses to the person paying the reimbursement or allowance. **Excess reimbursement** means any amount for which you did not adequately account within a reasonable period of time. For example, if you received a travel advance and you did not spend all the money on business-related expenses, or you do not have proof of all your expenses, you have an excess reimbursement.

“Adequate accounting” and “reasonable period of time” were discussed earlier in this chapter.

Travel advance. If your employer provides you with an expense allowance before you actually have the expense, and the allowance is reasonably calculated not to exceed your expected expenses, you have received a travel advance. Under an accountable plan, you must be required to adequately account to your employer for this advance and be required to return any excess within a reasonable period of time. See *Reasonable period of time*, earlier. If you do not adequately account for or do not return any excess advance within a reasonable period of time, the amount you do not account for or return will be treated as having been paid under a nonaccountable plan (discussed later).

Unproven amounts. If you do not prove that you actually traveled on each day for which you received a per diem allowance (proving the elements described in Chapter 5 under *Proof of Travel Expenses*), you must return this unproven amount of the travel advance within a reasonable period of time. If you fail to do this, your employer will include as income in boxes 1, 3, and 5 of your Form W-2 the unproven amount of per diem allowance as excess reimbursement. This unproven amount is considered paid under a nonaccountable plan (discussed later).

Per diem allowance MORE than federal rate. If your employer’s accountable plan pays you a per diem or similar allowance that is higher than the federal rate for the area you traveled to, you do not have to return the difference between the two rates for the period you can prove business-related travel expenses. However, the difference will be reported as wages on your Form W-2. This excess

amount is considered paid under a nonaccountable plan (discussed later).

Example. Your employer sends you on a 5-day business trip to Miami and gives you a \$200 ($\40×5 days) advance to cover your meals and incidental expenses. The federal per diem for meals and incidental expenses in Miami is \$34. Your trip lasts only 3 days. Under your employer’s accountable plan, you must return the \$80 ($\40×2 days) advance for the 2 days you did not travel. You do not have to return the \$18 difference [$(\$40 - \$34) \times 3$ days]. However, the \$18 will be reported on your Form W-2 as wages.

Nonaccountable Plans

A **nonaccountable plan** is a reimbursement or expense allowance arrangement that does not meet the three rules listed earlier under *Accountable Plans*.

In addition, the following payments made under an accountable plan will be treated as being paid under a nonaccountable plan:

- 1) Excess reimbursements you fail to return to your employer, and
- 2) Reimbursement of nondeductible expenses related to your employer’s business. See *Reimbursement of nondeductible expenses* earlier under *Accountable Plans*.

An arrangement that repays you for business expenses by reducing the amount reported as your wages, salary, or other compensation will be treated as a nonaccountable plan. This is because you are entitled to receive the full amount of your compensation regardless of whether you incurred any business expenses.

If you are not sure if the reimbursement or expense allowance arrangement is an accountable or nonaccountable plan, see your employer.

Your employer will combine the amount of any reimbursement or other expense allowance paid to you under a nonaccountable plan with your wages, salary, or other compensation. Your employer will report the total in box 1 (and boxes 3 and 5 if they apply) of your Form W-2.

You must complete Form 2106 or 2106-EZ and itemize your deductions on Schedule A (Form 1040) to deduct your expenses for travel, transportation, meals, or entertainment. Your meal and entertainment expenses will be subject to the 50% limit discussed in Chapter 2. Also, your total expenses will be subject to the 2% of adjusted gross income limit that applies to most miscellaneous itemized deductions. This 2% limit is figured on line 25 of Schedule A (Form 1040).

Example 1. Kim’s employer gives her \$500 a month (\$6,000 total this year) for her business expenses. Kim does not have to provide any proof of her expenses to her employer, and Kim can keep any funds that she does not spend.

Kim is being reimbursed under a nonaccountable plan. Her employer will include the \$6,000 on Kim’s Form W-2 as if it were wages.

If Kim wants to deduct her business expenses, she must complete Form 2106 or 2106-EZ and itemize her deductions on Schedule A (Form 1040). The 50% limit applies to her meal and entertainment expenses, and the 2% of adjusted gross income limit applies to her total employee business expenses.

Example 2. Kevin is paid \$2,000 a month by his employer. On days that he travels away from home on business, his employer designates \$50 a day of his salary as paid to reimburse his travel expenses. Because his employer would pay Kevin his monthly salary regardless of whether he was traveling away from home, the arrangement is a nonaccountable plan. No part of the \$50 a day designated by his employer is treated as paid under an accountable plan.

Part of reimbursement paid under accountable plan. If your expenses are reimbursed under an otherwise accountable plan but you do not return, within a reasonable period of time, any reimbursement for which you do not adequately account is considered as paid under a nonaccountable plan. The remainder is treated as having been paid under an accountable plan (as discussed earlier in this chapter).

Rules for Independent Contractors

This section provides rules for reporting and substantiating certain expenses for travel, entertainment, or gifts paid or incurred by an independent contractor on behalf of a client or customer. The rules in this section affect both clients or customers and independent contractors.

You are considered an independent contractor if you are self-employed and you perform services for a customer or client.

Accounting to Your Client

If you received a reimbursement or an allowance for travel, entertainment, or gift expenses that you incurred on behalf of a client, you should provide an adequate accounting of these expenses to your client. If you do not account to your client for these expenses, you must include any reimbursements or allowances in income. You must keep adequate records of these expenses regardless of whether you account to your client for such expenses.

If you do not separately account for and seek reimbursement for meals and entertainment in connection with providing services for a client, you are subject to the 50% limit on such expenses. See *50% Limit* in Chapter 2.

Adequate accounting. As a self-employed person, you adequately account by reporting your actual expenses. You should follow the recordkeeping rules in Chapter 5.

How to report. For information on how to report expenses on your tax return, see *Self-employed* at the beginning of this chapter.

Required Records for Clients or Customers

If you are a client or customer, you generally are not required to keep records to prove the reimbursements or allowances you give, in the course of your business, to an independent contractor for travel or gift expenses incurred on your behalf. However, you must keep records if:

- 1) You reimburse the contractor for entertainment expenses incurred on your behalf, **and**
- 2) The contractor adequately accounts to you for these expenses.

Contractor adequately accounts. If the contractor does adequately account to you for entertainment expenses, you (the client or customer) must keep records documenting each element of the expense, as explained in Chapter 5. Use your records as proof for a deduction on your tax return. If entertainment expenses are accounted for separately, you are subject to the 50% limit on entertainment. You do not, however, have to file an information return to report amounts for which you reimbursed the contractor, as long as he or she adequately accounted to you for these expenses.

Contractor does not adequately account. If the contractor does not adequately account to you for allowances or reimbursements of entertainment expenses, then you (the client or customer) do not have to keep your own separate records of these items incurred by the contractor on your behalf. You are not subject to the 50% limit on entertainment in this case. You can deduct the reimbursements or allowances as compensation if they are ordinary and necessary business expenses. However, you must file Form 1099-MISC, *Miscellaneous Income*, to report amounts paid to the independent contractor if the total of the reimbursements and any other fees is \$600 or more during the calendar year.

Completing Forms 2106 and 2106-EZ

This section briefly describes how employees complete Forms 2106 and 2106-EZ. Table 5 explains what the employer reports on Form W-2 and what the employee reports on Form 2106. The instructions for the forms have more information on completing them.

Form 2106-EZ. You may be able to use new Form 2106-EZ to claim your employee business expenses. You qualify to use this form if you meet both of the following conditions.

- 1) You were not reimbursed for your expenses or, if you were reimbursed, the reimbursement was included in your income (box 1 of your Form W-2).
- 2) If you claimed car expenses, you use the standard mileage rate.

Car expenses. If you used a car or other vehicle to perform your job as an employee, you may be able to deduct certain vehicle expenses. For information on deducting vehicle expenses, see Publication 917. Vehicle expenses are generally figured in Part II of Form 2106, and then claimed on line 1, Column A, of Part I of Form 2106. Vehicle expenses using the standard mileage rate can also be figured on Form 2106-EZ by completing Part III and line 1 of Part II.

Local transportation expenses. Show your local business transportation expenses that did not involve overnight travel on line 2, Column A, of Form 2106 or on line 2, Part II, of Form 2106-EZ. Also include on this line business expenses you have for parking fees and tolls. Do not include expenses of operating your car or expenses of commuting between your home and work.

Employee business expenses other than meals and entertainment. Show your other employee business expenses on lines 3 and 4, Column A, of Form 2106 or Form 2106-EZ. Do not include expenses for meals and entertainment on those lines. Line 4 is for expenses such as business gifts, educational expenses (tuition and books), office-in-the-home expenses, and trade and professional publications.

Note: If these are the only expenses you are claiming and you received no reimbursements (or the reimbursements were all included in box 1 of your Form W-2), do not complete Form 2106 or 2106-EZ. Instead, claim these amounts directly on Schedule A. List the type and amount of each expense on the dotted lines next to line 20 and include the total on line 20.

Meal and entertainment expenses. Show the full amount of your expenses for business-related meals and entertainment on line 5, Column B, of Form 2106. Include meals while away from your tax home overnight and other business meals and entertainment. Enter 50% of the line 8 meal and entertainment expenses on line 9, Column B, of Form 2106.

If you file Form 2106-EZ, enter the full amount of your meals and entertainment on the line to the left of line 5 and multiply the total by 50%. Enter the result on line 5.

Reimbursements. Enter on line 7 of Form 2106 the amounts your employer (or third party) reimbursed you that were **NOT** reported to you in box 1 of your Form W-2. (You cannot use Form 2106-EZ.) This includes any amount reported under code L in box 13 of Form W-2.

Allocating your reimbursement. If you were reimbursed under an accountable plan and want to deduct excess expenses that were not reimbursed, you may have to allocate your reimbursement. If your employer paid you a single amount which covers meals and/or entertainment, as well as other business expenses, you must allocate the reimbursement

so that you know how much to enter in Column A and Column B of line 7 of Form 2106.

Use the following worksheet to allocate your reimbursement.

1. Enter the total amount of the reimbursements your employer gave you that **were not** reported to you in box 1 of Form W-2
2. Enter the total amount of your expenses for the periods covered by this reimbursement
3. Of the amount on line 2, enter your total expense for meals and entertainment
4. Divide line 3 by line 2. Enter the result as a decimal (to at least two places) ...
5. Multiply line 1 by line 4. Enter the result here and in Column B, line 7
6. Subtract line 5 from line 1. Enter this result here and in Column A, line 7

Example. Assume your employer paid you an expense allowance of \$5,000 during 1994 under an accountable plan. It is not clear how much of the allowance is for the cost of deductible meals. You actually spent \$6,500 during the year (\$2,000 for meals and \$4,500 for car expenses). First, divide your meal expenses by your total expenses ($\$2,000 \div \$6,500$). The result is .31. Multiply your reimbursement by this decimal ($\$5,000 \times .31$). The result is \$1,550 (the amount of reimbursement attributable to your meals). Enter this amount on line 7, Column B of Form 2106. Enter the remainder of the reimbursement, \$3,450 ($\$5,000 - \$1,550$), on line 7, Column A of Form 2106.

Schedule A (Form 1040). After you have completed your Form 2106 or 2106-EZ, follow the directions on that form to deduct your expenses on the appropriate line of your tax return. For most taxpayers this is on line 20 of Schedule A (Form 1040). However, if you are a performing artist or a disabled employee with impairment-related work expenses, see *Special Rules*, later.

Limits on employee business expenses. Your employee business expenses may be subject to any of the three limits described below. They are figured in the following order on the specified form.

1. Limit on meals and entertainment. Certain meal and entertainment expenses are subject to a 50% limit. If you are an employee, you figure this limit on line 9 of Form 2106 or line 5 of Form 2106-EZ. (See *50% Limit* in Chapter 2.)

2. Limit on employee business expenses. If you are an employee, deduct your employee business expenses (as figured on Form 2106 or 2106-EZ) on line 20 of Schedule A (Form 1040). Most miscellaneous itemized deductions, including employee business expenses, are subject to a 2% of adjusted gross income limit. This limit is figured on line 25 of Schedule A.

3. Limit on total itemized deductions. If your adjusted gross income (line 32 of Form 1040) is more than \$111,800 (\$55,900 if you

are married filing separately), the total of certain itemized deductions, including employee business expenses, may be limited. See the Schedule A (Form 1040) instructions for information on how to figure this limit.

Special Rules

This section discusses special rules that apply only to performing artists and disabled employees with impairment-related work expenses.

Expenses of Certain Performing Artists

If you are a performing artist, you may qualify to deduct your employee business expenses as an adjustment to gross income rather than as a miscellaneous itemized deduction. To qualify, you must meet **all** of the following requirements.

- 1) During the tax year, you perform services in the performing arts for at least two employers.
- 2) You receive at least \$200 each from any two of these employers.
- 3) Your related performing-arts business expenses are more than 10% of your gross income from the performance of such services.
- 4) Your adjusted gross income is not more than \$16,000 before deducting these business expenses.

Special rules for married persons. If you are married, you must file a joint return unless you lived apart from your spouse at all times during the tax year.

If you file a joint return, you must figure requirements (1), (2), and (3) separately for both you and your spouse. However, requirement (4) applies to your and your spouse's combined adjusted gross income.

Where to report. If you meet all of the above requirements, you should first complete Form

2106 or 2106-EZ. Then you include your performing-arts-related expenses from line 10 of Form 2106 or line 6 of Form 2106-EZ in the total on line 30 of Form 1040. Write "QPA" and the amount of your performing-arts-related expenses on the dotted line next to line 30 (Form 1040).

If you do not meet all of the above requirements, you do not qualify to deduct your expenses as an adjustment to gross income. Instead, you must complete Form 2106 or 2106-EZ and deduct your employee business expenses on line 20 of Schedule A (Form 1040).

Expenses of Disabled Employees

If you are an employee with a physical or mental disability, your impairment-related work expenses are not subject to the 2% of adjusted gross income limit that applies to most other employee business expenses. After you complete Form 2106 or 2106-EZ, enter your impairment-related work expenses from line 10 of Form 2106 or line 6 of Form 2106-EZ on line 28 of Schedule A (Form 1040). Enter your employee business expenses that are **unrelated** to your disability from line 10 of Form 2106 or line 6 of Form 2106-EZ on line 20 of Schedule A (Form 1040).

Impairment-related work expenses are your allowable expenses for attendant care at your workplace and other expenses in connection with your workplace that are necessary for you to be able to work. For more information, see Publication 502, *Medical and Dental Expenses*, or Publication 529.

Illustrated Example

Bill Wilson is an employee of Fashion Clothing Co. in Manhattan, NY. In a typical week, Bill leaves his home on Long Island on Monday morning and drives to Albany to exhibit the Fashion line for 3 days to prospective customers. Then he drives to Troy to show X Department Store, an old customer, Fashion's new line of merchandise. While in Troy, he talks

with Tom Brown, purchasing agent for X Department Store, to discuss the new line. He later takes John Smith of Y Co., Troy, out to dinner to discuss Y Co.'s buying Fashion's new line of clothing.

Bill uses the standard mileage rate for car expense purposes. He records his total mileage, business mileage, parking fees, and tolls for the year. Bill records his expenses and other pertinent information in his *Weekly Traveling Expense and Entertainment Record*, shown in *Table 7*. He obtains receipts for his expenses for lodging and for any other expenses of \$25 or more.

During the year, Bill drove a total of 25,000 miles of which 20,000 miles were for business. Following the instructions for Part II of Form 2106, he answers all the questions and figures his vehicle expense to be \$5,800 (20,000 business miles × 29 cents standard mileage rate).

His total employee business expenses are shown in the following table.

Type of Expense	Amount
Parking fees and tolls	\$ 400
Vehicle expenses	5,800
Meals	2,632
Lodging, laundry, cleaning	10,000
Entertainment	1,870
Gifts, education, etc.	400
Total	\$21,102

Bill received a reimbursement of \$300 per month to help offset his car expenses. The reimbursement was figured at 25 cents per mile for up to 1,200 miles. Bill accounted to his employer for at least 1,200 business miles each month, and he received \$3,600 in reimbursements for 1994. Because the reimbursement was less than the standard mileage rate, Bill's employer did not include the \$3,600 in box 1 of Bill's Form W-2.

Bill files Form 2106 with his tax return. His filled-in form is shown at the end of this publication.

THIS IS NOT AN OFFICIAL INTERNAL REVENUE FORM

Table 7. Weekly Traveling Expense and Entertainment Record

From: August 7, 1994 **To:** August 13, 1994

Name: Bill Wilson

Expenses	Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday	Total
1. Travel Expenses:								
Airlines								
Excess baggage								
Bus - Train								
Cab and Limousine								
Tips								
Porter								
2. Meals and Lodging:								
Breakfast			6 75	6 00	5 25	7 00		25 00
Lunch		9 75	10 00	9 25	8 25	8 50		45 75
Dinner		22 00	18 25	17 50				57 75
Hotel and Motel (Detail in Schedule B)		50 00	50 00	50 00	45 00			195 00
3. Entertainment (Detail in Schedule C)					50 00			50 00
4. Other Expenses:								
Postage								
Telephone & Telegraph		1 50				1 00		2 50
Stationery & Printing								
Stenographer								
Sample Room			15 00	15 00				30 00
Advertising								
Assistant(s) & Model(s)			20 00	20 00				40 00
Trade Shows								
5. Car Expenses: (List all car expenses - the division between business and personal expenses may be made at the end of the year.) (Detail mileage in Schedule A.)								
Gas, oil, lube, wash								
Repairs, parts								
Tires, supplies								
Parking fees, tolls		4 00			3 00	3 00		10 00
6. Other (Identify)								
Total		87 25	120 00	117 75	111 50	19 50		456 00
NOTE: Attach receipted bills for (1) ALL lodging and (2) any other expenses of \$2 5.00 or more.								
Schedule A - Car								
Mileage: End		57,600	57,620	57,650	57,660	57,840		//////////
Start		57,445	57,600	57,620	57,650	57,660		//////////
Total		155	20	30	10	180		395
Business Mileage		155	20	30	10	170		385
Schedule B - Lodging								
Hotel or Motel	Name		Bay Hotel	Bay Hotel	Bay Hotel	Modern Hotel		//////////
	City		Albany	Albany	Albany	Troy		//////////
Schedule C - Entertainment								
Date	Item	Place	Amount	Business Purpose	Business Relationship			
August 11, 1994	Bar	John's Steak House	\$ 15 00	Discuss purchases	Smith-Y Co.			
	Dinner	Troy	\$ 35 00					

WEEKLY REIMBURSEMENTS:

Travel and transportation expenses N/A
 Other reimbursements
TOTAL

Employee Business Expenses

OMB No. 1545-0139

1994

Attachment
 Sequence No. **54**

▶ See separate instructions.

▶ Attach to Form 1040.

Your name Bill Wilson Social security number 555 00 5555 Occupation in which expenses were incurred Sales

Part I Employee Business Expenses and Reimbursements

STEP 1 Enter Your Expenses	Column A Other Than Meals and Entertainment	Column B Meals and Entertainment
1 Vehicle expense from line 22 or line 29	1 5,800	
2 Parking fees, tolls, and transportation, including train, bus, etc., that did not involve overnight travel	2 400	
3 Travel expense while away from home overnight, including lodging, airplane, car rental, etc. Do not include meals and entertainment	3 10,000	
4 Business expenses not included on lines 1 through 3. Do not include meals and entertainment	4 400	
5 Meals and entertainment expenses (see instructions)		4,502
6 Total expenses. In Column A, add lines 1 through 4 and enter the result. In Column B, enter the amount from line 5	6 16,600	4,502

Note: If you were not reimbursed for any expenses in Step 1, skip line 7 and enter the amount from line 6 on line 8.

STEP 2 Enter Amounts Your Employer Gave You for Expenses Listed in STEP 1

7 Enter amounts your employer gave you that were not reported to you in box 1 of Form W-2. Include any amount reported under code "L" in box 13 of your Form W-2 (see instructions)	7 3,600	-0-
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STEP 3 Figure Expenses To Deduct on Schedule A (Form 1040)

8 Subtract line 7 from line 6	8 13,000	4,502
Note: If both columns of line 8 are zero, stop here. If Column A is less than zero, report the amount as income on Form 1040, line 7.		
9 In Column A, enter the amount from line 8 (if zero or less, enter -0-). In Column B, multiply the amount on line 8 by 50% (.50)	9 13,000	2,251
10 Add the amounts on line 9 of both columns and enter the total here. Also, enter the total on Schedule A (Form 1040), line 20. (Qualified performing artists and individuals with disabilities, see the instructions for special rules on where to enter the total.) ▶	10	15,251

For Paperwork Reduction Act Notice, see instructions.

Cat. No. 11700N

Form **2106** (1994)

Part II Vehicle Expenses (See instructions to find out which sections to complete.)

Section A.—General Information

	(a) Vehicle 1	(b) Vehicle 2
11 Enter the date vehicle was placed in service	11 1/2/92	1/1
12 Total miles vehicle was driven during 1994	12 25,000 miles	miles
13 Business miles included on line 12	13 20,000 miles	miles
14 Percent of business use. Divide line 13 by line 12	14 80 %	%
15 Average daily round trip commuting distance	15 10 miles	miles
16 Commuting miles included on line 12	16 2,600 miles	miles
17 Other personal miles. Add lines 13 and 16 and subtract the total from line 12	17 2,400 miles	miles
18 Do you (or your spouse) have another vehicle available for personal purposes?	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No	
19 If your employer provided you with a vehicle, is personal use during off duty hours permitted? <input type="checkbox"/> Yes <input type="checkbox"/> No <input checked="" type="checkbox"/> Not applicable		
20 Do you have evidence to support your deduction?	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No	
21 If "Yes," is the evidence written?	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No	

Section B.—Standard Mileage Rate (Use this section only if you own the vehicle.)

22 Multiply line 13 by 29¢ (.29). Enter the result here and on line 1. (Rural mail carriers, see instructions.)	22 5,800
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Section C.—Actual Expenses

	(a) Vehicle 1	(b) Vehicle 2
23 Gasoline, oil, repairs, vehicle insurance, etc.	23	
24a Vehicle rentals	24a	
b Inclusion amount (see instructions)	24b	
c Subtract line 24b from line 24a	24c	
25 Value of employer-provided vehicle (applies only if 100% of annual lease value was included on Form W-2—see instructions)	25	
26 Add lines 23, 24c, and 25	26	
27 Multiply line 26 by the percentage on line 14	27	
28 Depreciation. Enter amount from line 38 below	28	
29 Add lines 27 and 28. Enter total here and on line 1	29	

Section D.—Depreciation of Vehicles (Use this section only if you own the vehicle.)

	(a) Vehicle 1	(b) Vehicle 2
30 Enter cost or other basis (see instructions)	30	
31 Enter amount of section 179 deduction (see instructions)	31	
32 Multiply line 30 by line 14 (see instructions if you elected the section 179 deduction)	32	
33 Enter depreciation method and percentage (see instructions)	33	
34 Multiply line 32 by the percentage on line 33 (see instructions)	34	
35 Add lines 31 and 34	35	
36 Enter the limitation amount from the table in the line 36 instructions	36	
37 Multiply line 36 by the percentage on line 14	37	
38 Enter the smaller of line 35 or line 37. Also, enter this amount on line 28 above	38	

