

Business Deductions for Employees



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The Line Between Business and Pleasure

If planned properly, attendees at business meetings can deduct a portion of the expenses for establishing business relationships and gaining business knowledge while enjoying a mini-vacation. It is important to be aware of when deductions are legitimate as well as when they are not.

Business and Personal Travel

A taxpayer can deduct all travel expenses while away from home if the primary purpose of the trip was business-related. Expenses such as transportation, meals, lodging and incidentals are deductible provided they are not lavish or extravagant. If the taxpayer engages in both business and personal activities while away traveling, he can deduct the transportation expenses in their entirety if the primary purpose of the trip is business-related. Lodging and 50% of meals is also deductible. Where a companion, such as a spouse, accompanies the taxpayer, the companion's meals and travel expenses are generally not deductible. In addition, deductible-lodging expense is based upon the single occupancy rate.

Business Use of Your Automobile

You can generally determine the expense for the business use of your car in one of two ways: the standard mileage rate method or the actual expense method. If you qualify to use either method, figure the deduction both ways to see which gives you a larger deduction.

Standard Mileage Rate Method:

The standard mileage rate is available to self-employed individuals and employees if the following applies:

- They must own or lease the car,
- Cannot use it for hire, such as a taxi,
- Cannot operate five or more cars at the same time,
- Must not have claimed a depreciation deduction for the car in an earlier year, and
- Must have chosen to use it in the first year you placed the car in service at your business.

Then, for a car you own, in subsequent years, you can choose to use the standard mileage rate or actual expenses. However, if the car is leased, you must use the standard mileage rate method for the entire lease period. The standard mileage rate is determined by the government annually.

Actual Expenses Method: To use the actual expense method, you determine the entire actual cost of operating the car for the year and then determine the business portion attributable to the business miles driven. The business portion is calculated by dividing the business mileage of a vehicle by the total mileage. This percentage is then applied to the total actual expenses. Operating expenses include gas, oil, repairs, wash and wax, tires, insurance, registration fees, depreciation and lease payments (if applicable). The actual expense method can include interest paid on the car loan when deducted on business returns. However, the interest deduction is not allowed for employees deducting car expenses as part of their itemized deductions.

Keeping Records for Out-of-Town Business Travel

Out-of-town expenses are the ordinary and necessary expenses of traveling away from "home" overnight in pursuit of your employment, trade, or business. Your home is generally considered to be the entire city or general area where your principal place of business or employment is located. Out-of-town expenses include transportation, meals, lodging, tips, and miscellaneous items like laundry, valet, etc.

You should document away-from-home expenses by noting the date, destination, and business purpose of your trip. Record business miles if you drove to the out-of-town location. In addition, keep a detailed record of your expenses - lodging, public transportation, meals, etc. Be sure to list meals separately from other expenses in your records. Receipts must be retained for each lodging expense. However, if any other business expense is less than \$75, a receipt is not necessary if you record all the information in a timely diary. You must keep track of the full amount of meal expenses, even though only a portion of the amount may be deductible.

Keep Track of Meal & Entertainment Expenses

When looking for deductions to add to your taxes, don't overlook your meal and entertainment expenses. These types of expenses must be "ordinary" and "necessary" to your business or trade and must be "directly related to" or "associated with" the active conduct of business.

In order for the IRS to allow these deductions, good documentation is a requirement and should include the following items:

- The amount
- Date, time and place
- Business purpose
- Names of guests & business relationship

In addition, the surroundings must be conducive for a business meeting, and any discussion before, during or after any meal should be business-related for it to be considered for a deduction. An intimate and quiet location would be appropriate for a business discussion. Refrain from going to places with loud and distracting events that can interfere with the main objective: to talk about business.

A 50% deduction on entertainment expenses is allowed by the IRS if the purpose of the business is to conduct a specific business agenda. The 50% rule also covers the cost of meals during away-from-home business travel. In addition, deductions for expenses related to the meals (e.g., taxes, tips and cover charges) are also limited to 50% of cost; however, this is not true for costs of transportation to and from the meal or entertainment location.

Business Gifts

The deduction for gifts made in the course of a taxpayer's trade or business is limited to \$25 to any one individual per year. A gift to a family member of a customer is considered a gift to the customer unless there is a bona fide business relationship with the recipient family member. A married couple is considered one taxpayer for the purposes of the \$25 per person limit regardless of whether they are separately employed or have separate businesses.

The following are not subject to the \$25 annual limit:

- Items costing \$4 or less that contain an imprint with the taxpayer's name, and the item is one of a number of identical items the taxpayer widely distributes
- Signs, display racks or other promotional material to be used on the business premises of the recipient
- Incidental costs such as engraving, packaging, mailing or gift wrapping. A cost is incidental only if does not add substantial value to the gift
- Awards of tangible personal property costing \$400 or less given to an employee for length-of-service or safety achievement. If the award is part of an established written plan that does not discriminate in favor of highly compensated employees, the maximum is \$1,600.