

Maximizing Deductions Part 1

This self-study course will guide you through the ins and outs of maximizing business deductions for travel, and meals and entertainment expense. It includes detailed explanations and practical examples of how the tax law is applied. This is a Basic tax course with no prerequisites, and qualifies for 2 CE credit in the Tax Law category.

TABLE OF CONTENTS

INTRODUCTION	3
Chapter 1: Travel.....	5
I. Traveling Away From Home	5
II. Temporary Assignment Or Job.....	7
III. What Travel Expenses Are Deductible	8
Chapter 2: Meals And Entertainment	23
I. Entertainment.....	23
II. Meals	24
III. 50% Limit	24
Chapter 3: Gifts	28
GLOSSARY	30
FINAL EXAM	32

NOTICE

This course is sold with the understanding that the publisher is not engaged in rendering legal, accounting, or other professional advice and assumes no liability whatsoever in connection with its use. Since laws are constantly changing, and are subject to differing interpretations, we urge you to do additional research and consult appropriate experts before relying on the information contained in this course to render professional advice

INTRODUCTION

Chapter Objective

After completing this chapter, you should be able to:

- Identify current information related to transportation expenses.

The goal of this course is to teach the CPA or Enrolled Agent the ins and outs of the tax laws relating to travel, entertainment, gift, car expenses and home office deduction. The starting point will be important changes that became effective during the year and important reminders that you should know about. After this, we jump right into the law.

Important Information

Standard mileage rate. For 2019, the standard mileage rate for the cost of operating your car for business use is 58 cents per mile. For 2020, this rate decreases to 57.5 cents per mile.

Depreciation limits on cars, trucks, and vans. For 2019, the first-year limit on depreciation, special depreciation allowance, and section 179 deduction for vehicles acquired before September 28, 2017, and placed in service during 2019 is \$14,900. The first-year limit on depreciation, special depreciation allowance, and section 179 deduction for vehicles acquired after September 27, 2017, and placed in service during 2019 is \$18,100. If you elect not to claim a special depreciation allowance for a vehicle placed in service in 2019, the amount is \$10,100.

Section 179 deduction. The maximum amount you can elect to deduct for most section 179 property (including cars, trucks, and vans) you placed in service in tax years beginning in 2019 is \$1,020,000. This limit is reduced by the amount by which the cost of section 179 property placed in service during the tax year exceeds \$2,550,000.

Special depreciation allowance. For 2019, the special ("bonus") depreciation allowance on qualified property (including cars, trucks, and vans) is 100% for qualified property acquired and placed in service after September 27, 2017 and placed in service before January 2023, and is reduced 20% each year after for property placed in service before January 2027.

INTRODUCTION: TEST YOUR KNOWLEDGE

The following question is designed to ensure that you have a complete understanding of the information presented in the chapter (assignment). It is included as an additional tool to enhance your learning experience and does not need to be submitted in order to receive CPE credit.

We recommend that you answer the question and then compare your response to the suggested solution on the following page before answering the final exam question(s) related to this chapter (assignment).

1. What is the first-year limit on depreciation, special depreciation allowance, and section 179 deduction for vehicles acquired and placed in service during 2019:

- A. \$10,100
- B. \$14,900
- C. \$16,400
- D. \$18,100

INTRODUCTION: SOLUTION AND SUGGESTED RESPONSES

Below is the solution and suggested responses for the question on the previous page. If you choose an incorrect answer, you should review the page(s) as indicated for the question to ensure comprehension of the material.

1.

- A. Incorrect. If the taxpayer elects not to claim a special depreciation allowance for the vehicle placed in service in 2019, the amount would be \$10,100.
- B. Incorrect. The limit is \$14,900 for a vehicle acquired before September 28, 2017 and placed in service during 2019, but not if purchased after September 27, 2017.
- C. Incorrect. The limit is \$16,400 for a vehicle acquired before September 28, 2017 and placed in service during 2018, but not if purchased after September 27, 2017.
- D. **CORRECT**. This limit is reduced if the special depreciation allowance is not claimed.

Chapter 1: Travel

Chapter Objectives

After completing this chapter, you should be able to:

- Recognize what travel expenses are deductible.

If you temporarily travel away from your tax home, you can use this chapter to determine if you have deductible travel expenses.

This chapter discusses:

- Traveling away from home,
- Temporary assignment or job, and
- What travel expenses are deductible.

It also discusses the standard meal allowance, 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 the ordinary and necessary expenses of traveling away from home for your business, profession, or job.

An ordinary expense is one that is common and accepted in your trade or business. A necessary expense is one that is helpful and appropriate for your business. An expense does not have to be required to be considered necessary.

You will find examples of deductible travel expenses in Table 1-1, later.

I. Traveling Away From Home

You are traveling away from home if:

- 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
- You need to 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

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, you are not traveling away from home.

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. You cannot deduct your expenses for meals and lodging. You cannot deduct these expenses even if you have 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. 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.

TAX HOME

To determine whether you are traveling away from home, 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. See *Main place of business or work*, later.

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 have a regular or main place of business or post of duty and there is no place where you regularly live, you are considered an itinerant (a transient) and your tax home is wherever you work. As an itinerant, you cannot claim a travel expense deduction because you are never considered to be traveling away from home.

Main place of business or work. If you have more than one place of work, consider the following when determining which one is your main place of business or work.

- The total time you ordinarily spend in each place.
- The level of your business activity in each place.
- Whether your income from each place is significant or insignificant.

Example

You live in Cincinnati where you have a seasonal job for 8 months each year and earn \$40,000. You work the other 4 months in Miami, also at a seasonal job, and earn \$15,000. 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.

Factors used to determine tax home. If you do not have a regular or main place of business or work, use the following three factors to determine where your tax home is.

1. You perform part of your business in the area of your main home and use that home for lodging while doing business in the area.
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 abandoned the area in which both your historical place of lodging and your claimed 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 satisfy all three factors, your tax home is the home where you regularly live. If you satisfy only two factors, you may have a tax home depending on all the facts and circumstances. If you satisfy only one factor, you are an itinerant. Your tax home is wherever you work and you cannot deduct travel expenses.

Example 1

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 do not satisfy factor (1) because you did not work in Boston. You satisfy factor (2) because you had duplicate living expenses. You also satisfy factor (3) because you did not abandon your apartment in Boston as your main home, you kept your community contacts, and you frequently returned to live in your apartment. Therefore, you have a tax home in Boston.

Example 2

You are an outside salesperson with a sales territory covering several states. Your employer's main office is in Newark, but you do not conduct any business there. 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 do not satisfy any of the three factors listed earlier. You are an itinerant and have no tax home.

TAX HOME DIFFERENT FROM FAMILY HOME

If you (and your family) do not live at your tax home (defined earlier), you cannot deduct the cost of traveling between your tax home and your family home. You also cannot deduct the cost of meals and lodging while at your tax home. See Example 1 that follows.

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 2, later.

Example 1

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 expenses you have for meals and lodging in Phoenix or the cost of traveling from Phoenix to Tucson. This is because Phoenix is your tax home.

Example 2

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. 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 non-entertainment-related meals and lodging while you are living and working in Pittsburgh.

II. Temporary Assignment Or Job

You may regularly work at your tax home and also work at another location. It may not be practical to return to your tax home from this other location at the end of each work day.

Temporary assignment vs. indefinite assignment. 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 you are away from your main place of work. You can deduct your travel expenses if they otherwise qualify for deduction. 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, the location of the assignment or job becomes your new tax home and you cannot deduct your travel expenses while there. An assignment or job in a single location is considered indefinite if it is realistically expected to last for more than one year, whether or not it actually lasts for more than 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.

Exception for federal crime investigations or prosecutions. If you are a federal employee participating in a federal crime investigation or prosecution, you are not subject to the one-year rule. This means you may be able to deduct travel expenses even if you are away from your tax home for more than one year provided you meet the other requirements for deductibility.

For you to qualify, the Attorney General (or his or her designee) must certify that you are traveling:

- For the federal government,
- In a temporary duty status, and
- To investigate or prosecute, or provide support services for the investigation or prosecution of a federal crime.

Determining temporary or indefinite. You must determine whether your assignment is temporary or indefinite when you start work. If you expect an assignment or job to last for one year or less, it is temporary unless there are facts and circumstances that indicate otherwise. An assignment or job 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 whether an assignment or job is temporary or indefinite.

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. Your tax home is Los Angeles. Because of a shortage of work, you took a job on a construction project in Fresno. Your job was scheduled to end in 8 months. The job actually lasted 10 months.

You realistically expected the job in Fresno to last 8 months. The job actually did last less than 1 year. The job is temporary and your tax home is still in Los Angeles.

Example 2

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

Your job in Fresno is indefinite because you realistically expected the work to last longer than 1 year, even though it actually lasted less than 1 year. You cannot deduct any travel expenses you had in Fresno because Fresno became your tax home.

Example 3

The facts are the same as in Example 1, except that you realistically expected the work in Fresno to last 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. You can only deduct your travel expenses for the first 8 months. You cannot deduct any travel expenses you had after that time because Fresno became your tax home when the job became indefinite.

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 between your temporary place of work and your tax home. You can claim these expenses up to the amount it would have cost you to stay 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 of your expenses for meals and lodging during the probationary period.

III. What Travel Expenses Are Deductible

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

You can deduct ordinary and necessary expenses you have when you travel away from home on business. The type of expense you can deduct depends on the facts and your circumstances.

Table 1-1 summarizes travel expenses you may be able to deduct. You may have other deductible travel expenses that are not covered there, depending on the facts and your circumstances.

TABLE 1-1. TRAVEL EXPENSES YOU CAN DEDUCT

This chart summarizes expenses you can deduct when you travel away from home for business purposes.

IF you have expenses for...	THEN you can deduct the cost of...
transportation	travel by airplane, train, bus, or car between your home and your business destination. If you were provided with a ticket or you are riding free as a result of a frequent traveler or similar program, your cost is zero. If you travel by ship, see <i>Luxury Water Travel and Cruise Ships (under Conventions)</i> for additional rules and limits.
taxi, commuter bus, and airport limousine	fares for these and other types of transportation that take you between: <ol style="list-style-type: none"> 1. The airport or station and your hotel, and 2. The hotel and the work location of your customers or clients, your business meeting place, or your temporary work location.
baggage and shipping	sending baggage and sample or display material between your regular and temporary work locations.
car	operating and maintaining your car when traveling away from home on business. You can deduct actual expenses or the standard mileage rate, as well as business-related tolls and parking. If you rent a car while away from home on business, you can deduct only the business-use portion of the expenses.
lodging and meals	your lodging and non-entertainment-related meals if your business trip is overnight or long enough that you need to stop for sleep or rest to properly perform your duties. Meals include amounts spent for food, beverages, taxes, and related tips. See <i>Meals</i> for additional rules and limits.
cleaning	dry cleaning and laundry.
telephone	business calls while on your business trip. This includes 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. These expenses might include transportation to or from a business meal, public stenographer’s fees, computer rental fees, and operating and maintaining a house trailer.

Records. When you travel away from home on business, you should keep records of all the expenses you have 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.

Separating costs. If you have one expense that includes the costs of non-entertainment-related meals, entertainment, and other services (such as lodging or transportation), you must allocate that expense between the cost of non-entertainment-related meals and entertainment and the cost of 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.

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.

Employee. You can deduct the travel expenses of someone who goes with you if that person:

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.

Business associate. If a business associate travels with you and meets the conditions in (2) and (3) above, you can deduct the travel expenses you have for that person. A business associate is someone with whom you could reasonably expect to actively conduct business. A business associate can be a current or prospective (likely to become) customer, client, supplier, employee, agent, partner, or professional advisor.

Bona fide business purpose. A bona fide business purpose exists if you can 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 make the expenses deductible.

Example

Jerry drives to Chicago on business and takes his wife, Linda, with him. Linda is not Jerry's employee. Linda occasionally types notes, performs similar services, and accompanies Jerry to luncheons and dinners. The performance of these services does not establish that her presence on the trip is necessary to the conduct of Jerry's business. Her expenses are not deductible.

Jerry pays \$199 a day for a double room. A single room costs \$149 a day. He can deduct the total cost of driving his car to and from Chicago, but only \$149 a day for his hotel room. If he uses public transportation, he can deduct only his fare.

MEALS

You can deduct the cost of meals if it is necessary for you to stop for substantial sleep or rest to properly perform your duties while traveling away from home on business.

Meals and entertainment expenses are discussed in chapter 2.

Lavish or extravagant. You cannot deduct expenses for meals that 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, or resorts.

50% limit on meals. You can figure your meals expense using either of the following two methods.

- Actual cost.
- The standard meal allowance.

Both of these methods are explained below. But, regardless of the method you use, you generally can deduct only 50% of the unreimbursed cost of your meals.

If you are reimbursed for the cost of your meals, how you apply the 50% limit depends on whether your employer's reimbursement plan was accountable or nonaccountable. If you are not reimbursed, the 50% limit applies even if the unreimbursed meal expense is for business travel. Chapter 2 discusses the 50% limit in more detail.

Actual Cost

You can use the actual cost of your meals to figure the amount of your expense before reimbursement and application of the 50% deduction limit. If you use this method, you must keep records of your actual cost.

Standard Meal Allowance

Generally, you can use the "standard meal allowance" method as an alternative to the actual cost method. It allows you to use a set amount for your daily meals and incidental expenses (M&IE), instead

of keeping records of your actual costs. The set amount varies depending on where and when you travel. In this course, "standard meal allowance" refers to the federal rate for M&IE, discussed later under Amount of standard meal allowance. If you use the standard meal allowance, you still must keep records to prove the time, place, and business purpose of your travel.

Incidental expenses. The term "incidental expenses" means fees and tips given to porters, baggage carriers, hotel staff, and staff on ships.

Incidental expenses do not include expenses for laundry, cleaning and pressing of clothing, lodging taxes, or the costs of telegrams or telephone calls, transportation between places of lodging or business and places where meals are taken, or the mailing cost of filing travel vouchers and paying employer-sponsored charge card billings.

Incidental-expenses-only method. You can use an optional method (instead of actual cost) for deducting incidental expenses only. The amount of the deduction is \$5 a day. You can use this method only if you did not pay or incur any meal expenses. You cannot use this method on any day that you use the standard meal allowance. This method is subject to the proration rules for partial days. See Travel for days you depart and return, later in this chapter.

Note: The incidental-expenses-only-method is not subject to the 50% limit discussed next.

50% limit may apply. If you use the standard meal allowance method for non-entertainment-related meal expenses and you are not reimbursed or you are reimbursed under a nonaccountable plan, you can generally deduct only 50% of the standard meal allowance. If you are reimbursed under an accountable plan and you are deducting amounts that are more than your reimbursements, you can deduct only 50% of the excess amount. The 50% limit is discussed in more detail in chapter 2.

Caution! There is no optional standard lodging amount similar to the standard meal allowance. Your allowable lodging expense deduction is your actual cost.

Who can use the standard meal allowance. You can use the standard meal allowance whether you are an employee or self-employed, and whether or not you are reimbursed for your traveling expenses.

Use of the standard meal allowance for other travel. You can use the standard meal allowance to figure your meal expenses when you travel in connection with investment and other income-producing property. You can also use it to figure your meal expenses when you travel for qualifying educational purposes. You cannot use the standard meal allowance to figure the cost of your meals when you travel for medical or charitable purposes.

Amount of standard meal allowance. The standard meal allowance is the federal M&IE rate. For travel in 2019, the rate for most small localities in the United States is \$55 a day.

Most major cities and many other localities in the United States are designated as high-cost areas, qualifying for higher standard meal allowances.

Note: You can find this information (organized by state) at [Gsa.gov/Perdiem](https://www.gsa.gov/Perdiem). Enter a zip code or select a city and state for the per diem rates for the current fiscal year. Per diem rates for prior fiscal years are available by using the drop-down menu.

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.

Federal government's fiscal year. Per diem rates are listed by the Federal government's fiscal year which runs from October 1 to September 30. You can choose to use the rates from the 2019 fiscal year per diem tables or the rates from the 2020 fiscal year tables, but you must consistently use the same

tables for all travel you are reporting on your income tax return for the year. See Transition Rules, later.

Standard meal allowance for areas outside the continental United States. The standard meal allowance rates do not apply to travel in Alaska, Hawaii, or any other locations outside the continental United States. The Department of Defense establishes per diem rates for Alaska, Hawaii, Puerto Rico, American Samoa, Guam, Midway, the Northern Mariana Islands, the U.S. Virgin Islands, Wake Island and other non-foreign areas outside the continental United States. The Department of State establishes per diem rates for all other foreign areas.

Special rate for transportation workers. You can use a special standard meal allowance if you work in the transportation industry. You are in the transportation industry if your work:

- Directly involves moving people or goods by airplane, barge, bus, ship, train, or truck, and
- 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, you can claim a standard meal allowance of \$66 a day (\$71 for travel outside the continental United States) for travel in 2019.

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, you must use the special rate (and not use the regular standard meal allowance rates) for all trips you take that year.

Travel for days you depart and return. For both the day you depart for and the day you return from a business trip, you must prorate the standard meal allowance (figure a reduced amount for each day). You can do so by one of two methods.

- **Method 1:** You can claim $\frac{3}{4}$ of the standard meal allowance.
- **Method 2:** You can prorate using any method that you consistently apply and that is in accordance with reasonable business practice.

Example

Jen is employed in New Orleans as a convention planner. In March, her employer sent her on a 3-day trip to Washington, DC, to attend a planning seminar. She left her home in New Orleans at 10 a.m. on Wednesday and arrived in Washington, DC, at 5:30 p.m. After spending two nights there, she flew back to New Orleans on Friday and arrived back home at 8:00 p.m. Jen's employer gave her a flat amount to cover her expenses and included it with her wages.

Under Method 1, Jen can claim $2\frac{1}{2}$ days of the standard meal allowance for Washington, DC: $\frac{3}{4}$ of the daily rate for Wednesday and Friday (the days she departed and returned), and the full daily rate for Thursday.

Under Method 2, Jen could also use any method that she applies consistently and that is in accordance with reasonable business practice. For example, she could claim 3 days of the standard meal allowance even though a federal employee would have to use Method 1 and be limited to only $2\frac{1}{2}$ days.

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. See Part of Trip Outside the United States, later.

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 personal side trip, or had other personal 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 in May. Your business travel totals 900 miles round trip. On your way home, you stop in Mobile to visit your parents. You spend \$2,165 for the 9 days you are away from home for travel, non-entertainment-related 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 \$1,633.50. You can deduct \$1,633.50 for your trip, including the cost of round-trip transportation to and from New Orleans. The deduction for your non-entertainment-related meals is subject to the 50% limit on meals mentioned 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 for travel in the United States. 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

You fly from New York to Puerto Rico with a scheduled stop in Miami. Puerto Rico is not considered part of the United States for purposes of travel. 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. Because there are no scheduled stops between Puerto Rico and New York, all of the return trip is outside 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.

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 you can deduct depends in part upon how much of your trip outside the United States was business related.

Travel Entirely for Business or Considered Entirely for Business

You can deduct all your travel expenses of getting to and from your business destination if your trip is entirely for business or considered entirely for business.

Travel entirely for business. If you travel outside the United States and you spend the entire time on business activities, you can deduct all of your travel expenses.

Travel considered entirely for business. Even if you did not spend your entire time on business activities, your trip is considered entirely for business if you meet at least one of the following four exceptions.

Exception 1 - No substantial control. Your trip is considered entirely for business if you did not have substantial control over arranging the trip. The fact that you control the timing of your trip does not, by itself, mean that you have substantial control over arranging your trip.

You do not have substantial control over your trip if you:

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

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 generally has substantial control over arranging business trips.

Exception 2 - Outside United States no more than a week. Your trip is considered entirely for business if 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 do count the day you return to the United States.

Example

You traveled to Brussels primarily for business. You left Denver on Tuesday and flew to New York. On Wednesday, you flew from New York to Brussels, 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 you depart does not count as a day outside the United States.

You can deduct your cost of the round-trip flight between Denver and Brussels. You can also deduct the cost of your stay in Brussels for Thursday and Friday while you conducted business. However, you cannot deduct the cost of your stay in Brussels from Saturday through Tuesday because those days were spent on nonbusiness activities.

Exception 3 - Less than 25% of time on personal activities. Your trip is considered entirely for business if:

- You were outside the United States for more than a week, and
- You spent less than 25% of the total time you were outside the United States on nonbusiness activities.

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 5/21 (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 non-entertainment-related meals (subject to the 50% limit), lodging, and other related expenses.

Exception 4 - Vacation not a major consideration. Your trip is considered entirely for business if you can establish that a personal vacation was not a major consideration, even if you have substantial control over arranging the trip.

Travel Primarily for Business

If you travel outside the United States primarily for business but spend some of your time on other activities, you generally cannot deduct all of your travel expenses. You can only deduct the business portion of your cost of getting to and from your destination. You must allocate the costs between your business and other activities to determine your deductible amount. See Travel allocation rules, below.

Tip: You do not have to allocate your travel expenses if you meet one of the four exceptions listed earlier under Travel considered entirely for business. In those cases, you can deduct the total cost of getting to and from your destination.

Travel allocation rules. If your trip outside the United States was primarily for business, you must allocate your travel time on a day-to-day basis between business days and nonbusiness days. The days you depart from and return to the United States are both counted as days outside the United States. To figure the deductible amount of your round-trip travel expenses, use 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 business and nonbusiness days of travel.

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

Day spent on business. If your principal activity during working hours is pursuit of your trade or business, count the day 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. Count weekends, holidays, and other necessary standby days 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, do not count them as 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 your presence was required on both Friday and Monday, they are business days. Because the weekend is between business days, Saturday and Sunday are counted as business days. This is true even though you use the weekend for sightseeing, visiting friends, or other nonbusiness activity.

Example 2

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

Nonbusiness activity on the way to or from your business destination. If you stopped for a vacation or other nonbusiness activity either on the way from the United States to your business destination, or on the way back to the United States from your business destination, you must allocate part of your travel expenses to the nonbusiness activity.

The part you must allocate is the amount it would have cost you to travel between the point where travel outside the United States begins and your nonbusiness destination and a return to the point where travel outside the United States ends.

You determine the nonbusiness portion of that expense by multiplying it by a fraction. The numerator of the fraction is the number of nonbusiness days during your travel outside the United States and the denominator is the total number of days you spend outside the United States.

Example

You live in New York. On May 4 you flew to Paris to attend a business conference that began on May 5. The conference ended at noon on May 14. That evening you flew to Dublin where you visited with friends until the afternoon of May 21, when you flew directly 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 14. You did not meet any of the exceptions that would allow you to consider your travel entirely for business. May 4 through May 14 (11 days) are business days and May 15 through May 21 (7 days) are nonbusiness days.

You can deduct the cost of your non-entertainment-related meals (subject to the 50% limit), lodging, and other business-related travel expenses while in Paris.

You cannot deduct your expenses while in Dublin. You also cannot deduct 7/18 of what it would have cost you to travel round-trip between New York and Dublin.

You paid \$750 to fly from New York to Paris, \$400 to fly from Paris to Dublin, and \$700 to fly from Dublin back to New York. Round trip airfare from New York to Dublin would have been \$1,250.

You figure the deductible part of your air travel expenses by subtracting 7/18 of the round-trip fare and other expenses you would have had in traveling directly between New York and Dublin ($\$1,250 \times 7/18 = \486) from your total expenses in traveling from New York to Paris to Dublin and back to New York ($\$750 + \$400 + \$700 = \$1,850$).

Your deductible air travel expense is \$1,364 ($\$1,850 - \486).

Nonbusiness activity at, near, or beyond business destination. If you had a vacation or other nonbusiness activity at, near, or beyond your business destination, you must allocate part of your travel expenses to the nonbusiness activity.

The part you must allocate is the amount it would have cost you to travel between the point where travel outside the United States begins and your business destination and a return to the point where travel outside the United States ends.

You determine the nonbusiness portion of that expense by multiplying it by a fraction. The numerator of the fraction is the number of nonbusiness days during your travel outside the United States and the denominator is the total number of days you spend outside the United States.

None of your travel expenses for nonbusiness activities at, near, or beyond your business destination are deductible.

Example

Assume that the dates are the same as in the previous 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 Paris to Venice and return to Paris. In addition, you cannot deduct 7/18 of the airfare and other expenses from New York to Paris and back to New York.

You can deduct 11/18 of the round-trip plane fare and other travel expenses from New York to Paris, plus your non-entertainment-related meals (subject to the 50% limit), lodging, and any other business expenses you had in Paris. (Assume these expenses total \$4,939.) If the round-trip plane fare and other travel-related expenses (such as food during the trip) are \$1,750 from New York to Paris, you can deduct travel costs of \$1,069 (11/18 x \$1,750), plus the full \$4,939 for the expenses you had in Paris.

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

Travel Primarily for Personal Reasons

If you travel outside the United States primarily for vacation or for investment purposes, the entire cost of the trip is a nondeductible personal expense. However, if you spend some time attending brief professional seminars or a continuing education program, you can deduct your registration fees and other expenses you have that are directly related to your business.

Example

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 you have 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 in your records to ensure proper allocation of your deductible business expenses.

LUXURY WATER TRAVEL

If you travel by ocean liner, cruise ship, or other form of luxury water transportation for business purposes, there is a daily limit on the amount you can deduct. The limit is twice the highest federal per diem rate allowable at the time of your travel. (Generally, the federal per diem is the amount paid to federal government employees for daily living expenses when they travel away from home, but in the United States, for business purposes.)

Daily limit on luxury water travel. The highest federal per diem rate allowed and the daily limit for luxury water travel in 2019 is shown in the following table.

2019 Dates	Highest Federal Per Diem	Daily Limit on Luxury Water Travel
January 1 - March 31	\$470	\$940
April 1 - April 30	348	698

May 1 - May 31	346	692
June 1 - September 30	399	798
October 1 - October 31	410	820
November 1 - November 30	376	752
December 1 - December 31	465	930

Example

Caroline, a travel agent, traveled by ocean liner from New York to London, England on business in May. Her expense for the 6-day cruise was \$6,200. Caroline’s deduction for the cruise cannot exceed \$4,152 (6 days x \$692 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 non-entertainment-related 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 \$6,200. Of that amount, \$3,700 was separately stated as non-entertainment-related meals and \$1,000 was separately stated as entertainment. Caroline, who is self-employed, is not reimbursed for any of her travel expenses. Caroline figures her deductible travel expenses as follows.

Entertainment	\$1,000	
0% limit	<u>x 0.00</u>	
Allowable entertainment		\$0.00
Non-entertainment-related meals	\$3,700	
50% limit	<u>x .50</u>	
Allowable non-entertainment-related meals & entertainment	\$1,850	
Other travel expenses	<u>+1,500</u>	
Allowable cost before the daily limit		\$3,350
Daily limit for May 2019	\$692	
Times number of days	<u>x 6</u>	
Maximum luxury water travel deduction		\$4,152
Amount of allowable deduction		<u>\$3,350</u>

Caroline’s deduction for her cruise is limited to \$3,350, even though the limit on luxury water travel is higher.

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

Exceptions

The daily limit on luxury water travel (discussed earlier) does not apply to expenses you have to attend a convention, seminar, or meeting on board a cruise ship. See Cruise Ships under Conventions.

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.

Caution! Your appointment or election as a delegate does not, in itself, determine whether you can deduct travel expenses. You can deduct your travel expenses only if your attendance is connected to your own trade or business.

Convention agenda. The convention agenda or program generally shows the purpose of the convention. You can show your attendance at the convention benefits your trade or business by comparing the agenda with the official duties and responsibilities of your position. The agenda does not have to deal specifically with your official duties and responsibilities; it will be enough if the agenda is so related to your position that it shows your attendance was for business purposes.

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, and
- It is reasonable to hold the meeting outside the North American area.

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 the following locations.

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

The North American area also includes U.S. islands, cays, and reefs that are possessions of the United States and not part of the fifty states or the District of Columbia.

Reasonableness test. The following factors are taken into account to determine if it was as reasonable to hold the meeting outside the North American area as within the North American area.

- The purpose of the meeting and the activities taking place at the meeting.
- The purposes and activities of the sponsoring organizations or groups.
- The homes of the active members of the sponsoring organizations and the places at which other meetings of the sponsoring organizations or groups have been or will be held.
- Other relevant factors you may present.

Cruise Ships

You can deduct up to \$2,000 per year of your expenses of attending conventions, seminars, or similar meetings held on cruise ships. All ships that sail are considered cruise ships.

You can deduct these expenses only if all of the following requirements are met.

1. The convention, seminar, or meeting is directly related to your trade or business.
2. The cruise ship is a vessel registered in the United States.
3. All of the cruise ship's ports of call are in the United States or in possessions of the United States.
4. You attach to your return a written statement signed by you that includes information about:
 - a) The total days of the trip (not including 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.
5. 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.

CHAPTER 1: TEST YOUR KNOWLEDGE

The following questions are designed to ensure that you have a complete understanding of the information presented in the chapter (assignment). They are included as an additional tool to enhance your learning experience and do not need to be submitted in order to receive CPE credit.

We recommend that you answer each question and then compare your response to the suggested solutions on the following page(s) before answering the final exam questions related to this chapter (assignment).

1. For tax purposes, travel expenses are the expenses of traveling away from home for your business, profession, or job that are which of the following:

- A. ordinary and necessary
- B. regular and required
- C. lavish and extravagant
- D. direct and indirect

2. Which of the following is true if you are an itinerant worker:

- A. your tax home is the home where you regularly live
- B. your tax home is wherever you work
- C. you can deduct all of your travel expenses
- D. both B and C above

3. An assignment in a single location is considered to be temporary when it is realistically expected to last (and does in fact last) for a maximum of what length of time:

- A. one month or less
- B. six months or less
- C. one year or less
- D. eighteen months or less

4. Which of the following is true regarding using the "standard meal allowance":

- A. you must keep records of your actual costs
- B. the standard amount is the same regardless of where you live
- C. you are not required to keep records to prove the time, place, and business purpose of your travel

- D. incidental expenses do not include expenses for laundry, lodging taxes, or telephone calls

5. For travel in the United States, if your trip was primarily for business, and while at your business destination you extended your stay for a vacation, which of the following is correct:

- A. you can deduct any expenses related to getting to and from your business destination
- B. you can deduct business related expenses at your business destination
- C. both A and B above
- D. the entire cost of the trip is a nondeductible personal expense

6. Which of the following travel expenses are deductible:

- A. travel expenses when you attend a convention if you can show your attendance benefits your trade or business
- B. travel expenses for your family
- C. travel expenses for attending an investment convention
- D. all of the above

CHAPTER 1: SOLUTIONS AND SUGGESTED RESPONSES

Below are the solutions and suggested responses for the questions on the previous page(s). If you choose an incorrect answer, you should review the pages as indicated for each question to ensure comprehension of the material.

1.

- A. **CORRECT**. An ordinary expense is one that is common and accepted in your trade or business. A necessary expense is one that is helpful and appropriate for your business.
- B. Incorrect. An expense does not have to be required to be considered necessary.
- C. Incorrect. Lavish and extravagant expenses are not considered to be ordinary or necessary.
- D. Incorrect. This is not the correct distinction of travel expenses.

2.

- A. Incorrect. There are three factors that are used to determine your main home. If you satisfy all three of the factors, your tax home is considered to be the home where you regularly live and you are not considered to be an itinerant.
- B. **CORRECT**. There are three factors that are used to determine your main home. If you only satisfy one of the three factors, you are considered to be an itinerant, and your tax home is wherever you work.
- C. Incorrect. If you are an itinerant, you cannot deduct travel expenses.
- D. Incorrect. Since only one of the responses is correct, this cannot be the correct answer.

3.

- A. Incorrect. The actual period of time is longer.
- B. Incorrect. The actual period of time is longer.
- C. **CORRECT**. If your assignment is temporary, you can deduct your travel expenses if they otherwise qualify for deduction.
- D. Incorrect. This period of time would be considered indefinite.

4.

- A. Incorrect. The standard meal allowance allows you to use a set amount for your daily meals and incidental expenses (M&IE), instead of keeping records of your actual costs.
- B. Incorrect. The set amount of the standard meal allowance varies depending on where and when you travel.

- C. Incorrect. Even when using the standard meal allowance, you must still keep records to prove the time, place, and business purpose of your travel.
 - D. **CORRECT**. Incidental expenses include fees and tips given to porters, baggage carriers, hotel maids, etc.
- 5.
- A. Incorrect. You can deduct the business-related travel costs of getting to and from the business destination, but this is not the best answer.
 - B. Incorrect. You can deduct the business-related expenses at your business destination, but this is not the best answer.
 - C. **CORRECT**. If you extend your stay for a vacation, make a personal side trip, or have other personal activities while you are at the business destination, you can still deduct your business-related travel expenses.
 - D. Incorrect. The business-related expenses are still deductible as long as the primary purpose of the trip was for business-related reasons.
- 6.
- A. **CORRECT**. You can deduct your travel expenses only if your attendance is connected to your own trade or business.
 - B. Incorrect. Regardless of the purpose for the convention, you cannot deduct the travel expenses for your family.
 - C. Incorrect. If the convention is for investment, political, social, or other purposes unrelated to your trade or business, you cannot deduct the expenses.
 - D. Incorrect. Only one of the responses is correct.

Chapter 2: Meals And Entertainment

Chapter Objective

After completing this chapter, you should be able to:

- Identify the deductibility of non-entertainment-related meals and entertainment expenses.

You can no longer take a deduction for any expense related to activities generally considered entertainment, amusement, or recreation. You can continue to deduct 50% of the cost of business meals if you (or your employee) are present and the food or beverages are not considered lavish or extravagant.

Tip: If food or beverages are provided during or at an entertainment event, and the food and beverages were purchased separately from the entertainment or the cost of the food and beverages was stated separately from the cost of the entertainment on one or more bills, invoices, or receipts, you may be able to deduct the separately stated costs as a meal expense.

I. Entertainment

ENTERTAINMENT-DEFINED

Entertainment includes any activity generally considered to provide entertainment, amusement, or recreation. Examples include entertaining guests at nightclubs; 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 customers or their families.

Deduction may depend on your type of business. Your kind of business may determine if a particular activity is considered 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. This is 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.

Separating costs. If you have one expense that includes the costs of entertainment and other services (such as lodging or transportation), you must allocate that expense between the cost of entertainment and the cost of other services. You must have a reasonable basis for making this allocation. For example, you must allocate your expenses if a hotel includes entertainment in its lounge on the same bill with your room charge.

Exceptions to the Rules

In general, entertainment expenses are nondeductible. However, there are a few exceptions to the general rule including:

- Entertainment treated as compensation on your originally filed tax returns (and treated as wages to your employees);
- Recreational expenses for employees such as a holiday party or a summer picnic;
- Expenses related to attending business meetings or conventions of certain exempt organizations such as business leagues, chambers of commerce, professional associations, etc.; and
- Entertainment sold to customers. For example, if you run a nightclub, your expenses for the entertainment you furnish to your customers, such as a floor show, are not subject to the nondeductible rules.

Examples of Nondeductible Entertainment

Entertainment events. Generally, you cannot deduct any expense for an entertainment event. This includes expenses for entertaining guests at nightclubs; at social, athletic, and sporting clubs; at theaters; at sporting events; on yachts; or on hunting, fishing, vacation, and similar trips.

Entertainment facilities. Generally, you cannot deduct any expense for the use of 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.

Club dues and membership fees. You cannot deduct dues (including initiation fees) for membership in any club organized for business, pleasure, recreation, or other social purposes. This rule applies to any membership organization if one of its principal purposes is either:

- To conduct entertainment activities for members or their guests; or
- To provide members or their guests with access to entertainment facilities, discussed later.

The purposes and activities of a club, not its name, will determine whether or not you can deduct the dues. You cannot deduct dues paid to:

- Country clubs,
- Golf and athletic clubs,
- Airline clubs,
- Hotel clubs, and
- Clubs operated to provide meals under circumstances generally considered to be conducive to business discussions.

Gift or entertainment. Any item that might be considered either a gift or entertainment generally will be considered entertainment. 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.

II. Meals

As discussed above, entertainment expenses are generally nondeductible. However, you may continue to deduct 50% of the cost of business meals if you (or an employee) is present and the food or beverages are not considered lavish or extravagant. The meals may be provided to a current or potential business customer, client, consultant, or similar business contact.

Food and beverages that are provided during entertainment events are not considered entertainment if purchased separately from the entertainment, or if the cost of the food and beverages is stated separately from the cost of the entertainment on one or more bills, invoices, or receipts. However, the entertainment disallowance rule may not be circumvented through inflating the amount charged for food and beverages.

Other rules for meals and entertainment expenses. Any allowed expense must be ordinary and necessary. An ordinary expense is one that is common and accepted in your trade or business. A necessary expense is one that is helpful and appropriate for your business. An expense does not have to be required to be considered necessary. Expenses must not be lavish or extravagant. An expense is not considered lavish or extravagant if it is reasonable based on the facts and circumstances.

III. 50% Limit

In general, you can deduct only 50% of your business-related meal expenses, unless an exception applies. (If you are subject to the Department of Transportation's "hours of service" limits, you can deduct 80% of your business-related meal and entertainment expenses. See Individuals subject to "hours of service" limits, later.)

The 50% 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.

Examples of meals might include:

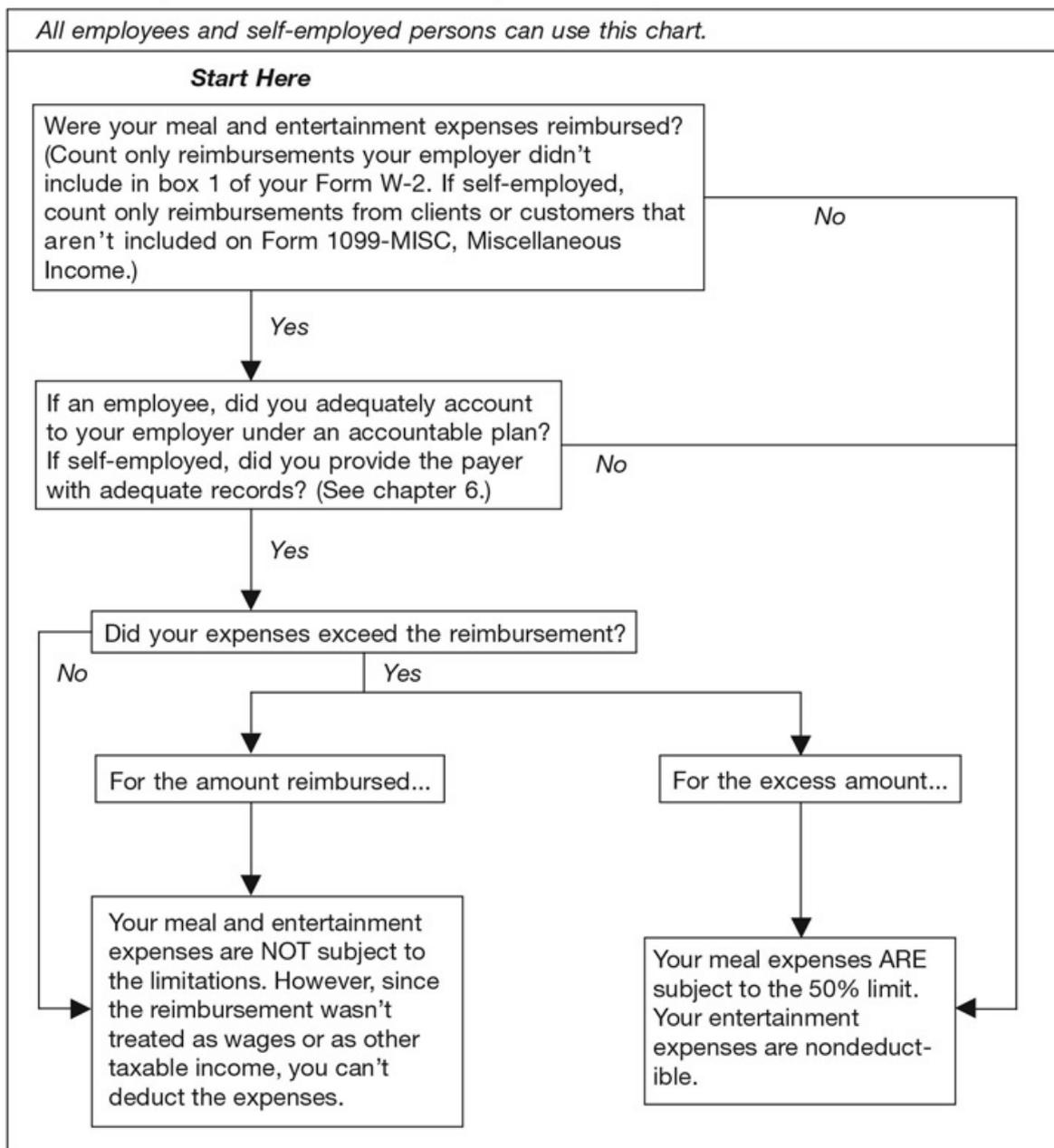
- Meals while traveling away from home (whether eating alone or with others) on business, or
- Meal at a business convention or business league meeting.

Costs to include or exclude. Taxes and tips relating to a business meal are included as a cost of the meal and are subject to the 50% limit. However, the cost of transportation to and from the meal is not treated as part of the cost and would not be subject to the limit.

Application of 50% limit. The 50% limit on meal expenses applies if the expense is otherwise deductible and is not covered by one of the exceptions discussed later. Figure 2-1 can help you determine if the 50% limit applies to you.

FIGURE 2-1. DOES THE 50% LIMIT APPLY TO YOUR EXPENSES?

There are exceptions to these rules. See Exceptions to the 50% Limit for Meals, later.



The 50% limit also applies to certain meal expenses that are not business related. It applies to meal expenses you have for the production of income, including rental or royalty income. It also applies to the cost of meals included in 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 expenses that would be deductible under the other rules discussed in this course.

Taking turns paying for meals. If a group of business acquaintances takes turns picking up each others' meal checks primarily for personal reasons, without regard to whether any business purposes are served, no member of the group can deduct any part of the expense.

Example 1: You spend \$200 (including tax and tip) for a business-related meal. If \$110 of that amount is not allowable because it is lavish and extravagant, the remaining \$90 is subject to the 50% limit. Your deduction cannot be more than \$45 (50% x \$90).

Example 2: You purchase two tickets to a concert for \$200 for you and your client. Your deduction is zero because no deduction is allowed for entertainment expenses.

EXCEPTIONS TO THE 50% LIMIT FOR MEALS

Your meal expense is not subject to the 50% limit if the expense meets one of the following exceptions.

1. **Expenses treated as compensation.** In general, expenses for goods, services, and facilities, to the extent the expenses are treated by the taxpayer, with respect to entertainment, amusement, or recreation, as compensation to an employee and as wages to the employee for tax purposes.
2. **Employee's reimbursed expenses.** If you are an employee, you are not subject to the 50% limit on expenses for which your employer reimburses you under an accountable plan.
3. **Self-employed reimbursed expenses.** If you are self-employed, your deductible meal expenses are not subject to the 50% limit if all three of the following requirements are met.
 - You have these expenses as an independent contractor.
 - Your customer or client reimburses you or gives you an allowance for these expenses in connection with services you perform.
 - You provide adequate records of these expenses to your customer or client.

In this case, your client or customer is subject to the 50% limit on the expenses.

Example

You are a self-employed attorney who adequately accounts for meal expenses to a client who reimburses you for these expenses. You are not subject to the limitation on meal expenses. If the client can deduct the expenses, the client is subject to the 50% limitation.

If you (as an independent contractor) have expenses for meals related to providing services for a client but do not adequately account for and seek reimbursement from the client for those expenses, you are subject to the 50% limit on non-entertainment-related meals, and entertainment-related meal expenses are nondeductible to you.

4. **Recreational expenses for employees.** You are not subject to the 50% limit for expenses for recreational, social, or similar activities (including facilities) such as a holiday party or a summer picnic.
5. **Advertising expenses.** You are not subject to the 50% limit if you provide meals to the general public as a means of advertising or promoting goodwill in the community. For example, neither the expense of sponsoring a television or radio show nor the expense of distributing free food and beverages to the general public is subject to the 50% limit.

6. **Sale of meals.** You are not subject to the 50% limit if you actually sell meals to the public. For example, if you run a restaurant, your expense for the food you furnish to your customers is not subject to the 50% limit.

Individuals subject to "hours of service" limits. You can deduct a higher percentage of your meal expenses while traveling away from your tax home if the meals take place during or incident to any period subject to the Department of Transportation's "hours of service" limits. The percentage is 80%. Individuals subject to the Department of Transportation's "hours of service" limits include the following persons.

- Certain air transportation workers (such as pilots, crew, dispatchers, mechanics, and control tower operators) who are under Federal Aviation Administration regulations.
- Interstate truck operators and bus drivers who are under Department of Transportation regulations.
- Certain railroad employees (such as engineers, conductors, train crews, dispatchers, and control operations personnel) who are under Federal Railroad Administration regulations.
- Certain merchant mariners who are under Coast Guard regulations.

CHAPTER 2: TEST YOUR KNOWLEDGE

The following questions are designed to ensure that you have a complete understanding of the information presented in the chapter (assignment). They are included as an additional tool to enhance your learning experience and do not need to be submitted in order to receive CPE credit.

We recommend that you answer each question and then compare your response to the suggested solutions on the following page(s) before answering the final exam questions related to this chapter (assignment).

1. Generally, you can deduct what percentage of business-related meal expenses in 2019:

- A. none
- B. 25%
- C. 50%
- D. 100%

CHAPTER 2: SOLUTIONS AND SUGGESTED RESPONSES

Below are the solutions and suggested responses for the questions on the previous page(s). If you choose an incorrect answer, you should review the pages as indicated for each question to ensure comprehension of the material.

- 1.
- A. Incorrect. Although the rules changed for entertainment expenses beginning in 2019, a portion of meal expenses are still deductible.
 - B. Incorrect. Greater than 25% of meal expenses are deductible for 2019.
 - C. **CORRECT**. You may continue to deduct 50% of the cost of business meals if the business owner (or an employee) is present and the food or beverages are not considered lavish or extravagant.
 - D. Incorrect. Meal expenses are not deductible in full.

Chapter 3: Gifts

Chapter Objective

After completing this chapter, you should be able to:

- Identify the restrictions on the deduction for business gifts.

If you give gifts in the course of your trade or business, you can deduct all or part of the cost. This chapter explains the limits and rules for deducting the costs of gifts.

\$25 limit. 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.

If you give a gift to a member of a customer's family, the gift is generally considered to be an indirect gift to the customer. This rule does not apply if you have a bona fide, independent business connection with that family member and the gift is not intended for the customer's eventual use.

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.

Example

Bob Jones sells products to Local Company. He and his wife, Jan, gave Local Company three gift baskets to thank them for their business. They paid \$80 for each gift basket, or \$240 total. Three of Local Company's executives took the gift baskets home for their families' use. Bob and Jan have no independent business relationship with any of the executives' other family members. They can deduct a total of \$75 (\$25 limit x 3) for the gift baskets.

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

Exceptions. The following items are not considered gifts for purposes of the \$25 limit.

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.

Gift or entertainment. Any item that might be considered either a gift or entertainment generally will be considered entertainment. 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.

Caution! 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 unclaimed unreimbursement applies. This type of deduction is considered a miscellaneous deduction which is no longer allowable due to the suspension of miscellaneous itemized deductions subject to the 2% floor under section 67(a).

CHAPTER 3: TEST YOUR KNOWLEDGE

The following questions are designed to ensure that you have a complete understanding of the information presented in the chapter (assignment). They are included as an additional tool to enhance your learning experience and do not need to be submitted in order to receive CPE credit.

We recommend that you answer each question and then compare your response to the suggested solutions on the following page(s) before answering the final exam questions related to this chapter (assignment).

1. Which of the following would generally not be considered an incidental cost when determining the value of a gift:

- A. engraving on jewelry
- B. packaging the gift
- C. mailing the gift
- D. sales tax

CHAPTER 3: SOLUTIONS AND SUGGESTED RESPONSES

Below are the solutions and suggested responses for the questions on the previous page(s). If you choose an incorrect answer, you should review the pages as indicated for each question to ensure comprehension of the material.

1.

- A. Incorrect. A cost is incidental if it does not add substantial value to the gift.
- B. Incorrect. The cost of packaging a gift would generally be considered incidental unless the cost of the packaging provides substantial value in comparison to the cost of the gift (i.e., an ornamental gift basket for the packaging of fruit).
- C. Incorrect. The cost of mailing a gift is generally considered to be incidental to the gift.
- D. **CORRECT**. The sales tax paid for the item would be included in its cost.

GLOSSARY

Accountable Plan - A reimbursement arrangement for deductible business expenses that are adequately accounted for to the employer within a reasonable period of time, and that any excess reimbursement or allowance is returned to the employer within a reasonable period of time.

Adjusted Basis - Generally the cost of the property plus any permanent improvements made to it, less any casualty losses or depreciation deducted in earlier tax years.

Associated Test - The entertainment was associated with the active conduct of the trade or business, and was held directly before or after a substantial business discussion.

Depreciation - Recover the cost of income producing property through yearly tax deductions.

Directly-Related Test - The main purpose of the combined business and entertainment was the active conduct of business, business was engaged with the person during the entertainment period, and there was more than a general expectation of getting income or some other specific business benefit at some future time.

Excess Reimbursement - Any amount which was not adequately accounted for within a reasonable period of time.

Fair Market Value - The price at which the property would change hands between a buyer and a seller, neither having to buy or sell, or both, having reasonable knowledge of all the relevant facts.

Hours of Service Limits - Apply to certain workers who are under certain federal regulations under the Department of Transportation.

Incidental Expenses - Includes items such as fees and tips given to porters, baggage carriers, etc; transportation between places of lodging or business and places where meals are taken; and mailing costs associated with filing travel vouchers and payment of employer sponsored charge card billings. Not included are expenses for laundry, cleaning, and pressing of clothing, lodging taxes, or the costs of telegrams or telephone calls.

Modified Accelerated Cost Recovery System (MACRS) - Name given to the tax rules for getting back through depreciation deductions the cost of property used in a trade or business or to produce income.

Necessary Expense - One that is helpful and appropriate for your business. Does not have to be required to be considered necessary.

Ordinary Expense - One that is common and accepted in your field of trade, business, or profession.

Placed in Service - When the property is ready and available for a specific use, regardless of whether or not it is actually being used.

Substantial Control - Generally considered to having substantial control for purposes of travel if you are self-employed, an employer, or are a managing executive. The fact that you control the timing of your trip does not, by itself, mean that you have substantial control over arranging your trip.

Tax Home - Generally your regular place of business or post of duty, regardless of where you maintain your family home, and includes the entire city or general area in which your business or work is located.

Unrecovered Basis - Cost or other basis in a car reduced by any clean-fuel vehicle deduction, electric vehicle credit, and depreciation and section 179 deductions that would have been allowable if the car had been used 100% for business or investment use.

FINAL EXAM

Maximizing Deductions Part 1

The following exam is attached only for your convenience. To access the official exam for this self-study course, please log into your account online and take the Final Exam from the course details page. A passing score of 70 percent or better will receive course credit and a Certificate of Completion.

1. What was the standard mileage rate for a car used for business in 2019:

- A. 14 cents
- B. 24 cents
- C. 53.5 cents
- D. 58 cents

2. An expense that is helpful and appropriate for your business is considered to be which of the following:

- A. an ordinary expense
- B. a necessary expense
- C. necessary if it is required
- D. an extravagant expense

3. In order to satisfy the rest requirement, which of the following is correct:

- A. you must be away from your tax home for a whole day
- B. you must at least take a nap in your car
- C. your relief from duty must be long enough to get necessary sleep or rest
- D. you must take a lunch break of one hour or longer

4. Generally, where is your tax home:

- A. your regular place of business
- B. the metropolitan area that you live in
- C. your personal residence
- D. the location where you spend the most time

5. Which of the following is true when you travel back to your tax home while on a temporary assignment:

- A. you are considered away from home even when you are back in your home town on your days off
- B. you can deduct your travel expenses while traveling between your temporary place of work and your tax home
- C. you cannot deduct the cost of your hotel room if kept while at home
- D. you cannot go back home on your days off

6. Generally, you cannot deduct the travel expenses of someone who goes with you on a business trip if which of the following is true:

- A. that person is your employee
- B. that person has a bona fide business purpose for the travel
- C. that person would otherwise be allowed to deduct the travel expenses
- D. that person is your dependent

7. Which of the following is correct regarding the amount of the standard meal allowance:

- A. it is the federal rate for your meals and incidental expenses (M&IE)

- B. it is the value assigned by the corporation
- C. it is any reasonable rate
- D. it is assigned by each state

8. Incidental expenses do not include which of the following:

- A. tips for hotel staff
- B. telephone costs
- C. tips for a porter
- D. tips for stewards on ships

9. For travel outside the United States, even if you did not spend your entire time on business activities, your trip is considered entirely for business if you meet the following exception:

- A. you did not have substantial control over arranging the trip
- B. non-business activities were less than 50%
- C. you were outside of the U.S. for more than seven consecutive days
- D. there are no exceptions to this rule

10. For business gifts you give directly or indirectly to any one person during your tax year, you can deduct no more than what amount:

- A. \$10
- B. \$20
- C. \$25
- D. \$50