

TAX ALERT: BUSINESS-TRAVEL PER DIEM RATES UPDATED FOR 2015

Effective Oct. 1, IRS Notice 2014-57, *2014–2015 Special Per Diem Rates*, updates the per diem rates that can be used for reimbursement of ordinary and normal business expenses incurred while employees travel away from home. It also revises the list of high-cost localities for use in the high-low substantiation method. The per diem rates, which are established by the General Services Administration (GSA), are updated before the end of the federal government’s fiscal year. Some employers elect to use these rates to simplify recordkeeping.

Background

As long as employees properly account for their business-travel expenses, reimbursements are generally tax-free to the employees and deductible by the employer. But keeping track of actual costs can be a logistical nightmare. With the government-approved per diem rates, employees don’t have to keep receipts for all of their travel expenses. So, employees and employers alike often prefer this recordkeeping shortcut.

Here’s how the per diem method works: Assuming that the travel qualifies as a business expense, the employer simply pays the employee the per diem allowance designated for the specific travel destination and deducts the per diem paid. The employee doesn’t have to report the payments on his or her personal tax return but still must substantiate the time, place and business purpose of the travel.

Although the rates are set by the GSA to cover travel by government employees, private employers may also use them for their employees. The rates are updated annually for the following areas:

- The 48 states in the continental United States and the District of Columbia (the “CONUS” rates),
- Certain areas outside the continental United States, including Alaska, Hawaii, Puerto Rico and U.S. possessions (the “OCONUS” rates), and
- Foreign countries outside the CONUS and OCONUS areas.

There are also optional rates for high-cost and low-cost areas. These designations simplify the expense reimbursement process even further by providing two per diem rates, one for high-cost localities and another for low-cost localities.

What do per diem rates cover?

Airfare and other transportation costs aren't covered by the per diem rates. What the rates do include are amounts for lodging and amounts for meals and incidental expenses (M&IE). For this purpose, M&IE includes:

- Meals and room service,
- Laundry, dry cleaning and ironing of clothing, and
- Fees and tips to service providers, such as food servers and luggage handlers.

Typically, if an employer chooses to use per diem rates, it uses them for all employees who regularly travel on business. An employer may choose to use the per diem rates for the specific travel destinations or for the high- and low-cost areas. However, per diem rates for lodging can't be used by an employee who owns, either directly or indirectly, more than 10% of the company. Instead, these owners must keep track of the actual amount of those business-travel expenses and retain their receipts. For M&IE, even those who own more than 10% of the company may use the per diem rates.

What's new in fiscal year 2015?

For fiscal year 2015 — which spans Oct. 1, 2014, through Sept. 30, 2015 —the per diem rate for high-cost areas has risen to \$259, an increase of \$8 over the prior year. This rate consists of \$194 for lodging and \$65 for M&IE.

The per diem rate for low-cost areas has increased by only \$2. The low-cost per diem rate is now \$172, including \$120 for lodging and \$52 for M&IE.

As usual, the list of cities (and their surrounding areas) included on the list of high-cost areas has been tweaked, and the time periods for which some of the seasonal areas will be included as high-cost areas have been revised. The changes are as follows:

- San Mateo/Foster City/Belmont, Calif.; Sunnyvale/Palo Alto/San Jose, Calif.; Glendive/Sidney, Mont.; and Williston, N.D. have been added to the list of high-cost areas.
- Time periods for Sedona, Ariz.; Napa, Calif.; Vail, Colo.; Fort Lauderdale, Fla.; Miami; and Philadelphia have been modified.
- Yosemite National Park, Calif.; San Diego; and Floral Park/Garden City/Great Neck, N.Y., have been removed from the list of high-cost areas.

The definition of “incidental travel expenses” has also been modified. To remain consistent with Federal Travel Regulations, incidental expenses now include only fees and tips given to porters, baggage carriers, hotel staff and staff on ships.

Transportation between places of lodging or business and places where meals are taken is no longer included in incidental expenses. In addition, the costs of mailing or filing travel vouchers and paying employer-sponsored charge card billings are specifically excluded. So, employers that use per diem rates may separately reimburse employees for transportation and mailing expenses.

Timing is everything

The travel expense updates go into effect on Oct. 1, 2014. During the last three months of calendar 2014, an employer that uses the per diem or high-low method may switch to the new rates or continue with the rates it’s been using for the first nine months of 2014.

But an employer must select one year’s set of rates for this quarter and stick with it; it can’t use 2014 rates for some employees and 2015 rates for others. Likewise, an employer can’t use the 2014 list of high-cost areas for some reimbursements and the 2015 list for others. In addition, if an employer used the high-low substantiation method for the first nine months of the year, it must continue using that method through Dec. 31, 2014.

Because business-travel expenses often attract IRS attention, they require detailed, accurate recordkeeping. The per diem and high-low methods can make recordkeeping less burdensome, but they’re not the best solution for all employers. If you have questions regarding the expense substantiation methods, please give us a call.

For more information

If you have questions about this alert, please contact [John Evans](#), Partner, by phone at 212.503.6380 or by email at jevans@markspaneth.com or any of our [Marks Paneth professionals](#).

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