ALERTS AND UPDATES

Summer Business Trips Combined with Vacation May Provide Tax Benefits

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Summer is upon us, and you may be thinking of combining a business trip and vacation plans. Although business is business and pleasure is pleasure, the tax code does not always adhere to absolutes. With a little planning, valid tax deductions may be available for out-of-town business-travel expenses, both domestically and internationally. What follows are a few strategies to help you achieve the greatest tax benefit from properly combining and documenting business and personal travel.

Combine Business and Vacation Domestic Travel

When some vacation days are added onto a business trip within the United States, business-travel expenses are typically deductible. The actual transportation expenses (cabs, plane fare, etc.) are deductible for out-of-town business trips and include the costs of getting to and from the place of business activity, *i.e.*, travel to and from the departure airport; the airfare itself; baggage fees and tips; cabs to and from the destination airport; and so forth. Costs for rail travel or to drive a personal vehicle also fit into this category. The bottom line is domestic transportation costs are 100-percent deductible, as long as the primary reason for the trip is business rather than pleasure. On the other hand, if vacation is the primary reason for travel, no transportation expenses are deductible.

Although the Internal Revenue Service (IRS) does not specify how to determine if the primary reason for domestic travel is business, the number of days spent on business versus pleasure is a key factor. Travel days count as business days, as do weekends and holidays if they fall between days devoted to business and it would be impractical to return home. "Standby days," when physical presence is required, but work is not necessarily performed, also count as business days. Any other day principally devoted to business activities during normal business hours is also counted as a business day, as are days when work was expected but not possible, due to reasons such as local transportation difficulties, power failures, etc.

For domestic trips, business will likely be considered as the primary reason for a sojourn whenever the business days exceed the personal days. You may want to accumulate and maintain proof by logging everything in a daily planner. No deductions are allowed for a spouse, dependent or other individual who accompanies the taxpayer or employee on a business trip unless such person is an employee of the person who is paying or reimbursing the expenses, the travel of such person serves a bona-fide business purpose and the expenses of such person are otherwise deductible.

Once at the destination, out-of-pocket expenses for business days are fully deductible. Out-of-pocket expenses include lodging, hotel tips, meals (subject to the 50-percent disallowance rule), seminar and convention fees, and cab fare. Expenses for personal days are nondeductible, except in the "Saturday night stayover" situation explained below.

Maximizing the Tax Benefits of a Saturday Night Stayover

An effective strategy for maximizing deductions for the personal portions of a trip is with a Saturday night stayover that reduces the overall cost of the trip. If it can be shown that staying the extra day or two costs less (or no more) than returning home immediately after the business meeting is over, the IRS allows the deduction of additional meals and lodging expenses (subject to the 50-percent disallowance rule for meals) for the extra day(s). Naturally, a dominant business purpose for making the trip must exist. It may be prudent to document that airfare savings equaled or exceeded the out-of-pocket costs of staying the extra day(s), and maintain the documentation.

Deducting Foreign Travel Costs

When travel outside the United States occurs primarily for business reasons, the general rule is that travel expenses, including transportation, must be allocated between business and personal expenses. However, *transportation* expenses, as well as other out-of-pocket business expenses can be deducted in full if the trip is primarily for business and either of the following rules is satisfied:

- *The one-week rule.* The business trip is a week or less, not counting the day left, but counting the day of return.
- *The 25-percent rule.* Transportation and other out-of-pocket business expenses can also be deducted in full for trips lasting more than a week, as long as less than 25 percent of the trip is spent on vacation. For this purpose, count the day of departure and day of return as business days, as long as the travel is to or from the business destination. Also, count all the other types of business days mentioned under the one-week rule above. Expenses allocable to personal days are not deductible.

Travel on behalf of an employer qualifies for a full deduction, even if the above rules are not met, if the travel is subject to a reimbursement or travel-allowance arrangement and the individual is not a managing executive of the company or related to the employer. Finally, in a catchall provision, 100 percent of transportation costs to foreign destinations are deductible if it can be proven that personal vacation was not a consideration in choosing to make the trip.

If 100 percent of transportation expenses are not deductible under any of the above rules, the *business percentage* of transportation costs are still deductible—assuming the trip is primarily for business. To calculate the business percentage, divide the days spent principally on business activities by the total number of days outside the country, counting departure and return days. The travel days count as business days, just as the other types of days are considered business days for purposes of the one-week rule and the 25-percent rule.

Travel to Attend Foreign Conventions

If the reason for a trip outside North America is to attend a business convention directly related to a trade or business, the trip may qualify for deductions. However, all of the foreign travel rules discussed above must be followed, and it must be proven that it was just as reasonable for the meeting to be held on foreign soil as in North America and that the time spent in business meetings or activities was substantial when compared to that spent sight-seeing and doing other personal activities. Regardless of the location, travel costs to attend investment- or financial-planning conventions and seminars are not deductible.

Fortunately, the tight rules for foreign conventions are inapplicable in many cases because the definition of "North America" for this purpose is *very liberal*. It includes Canada, Mexico, Puerto Rico, the U.S. Virgin Islands, American Samoa, the Northern Mariana Islands, Guam, the Marshall Islands, Micronesia, Palau, Netherlands Antilles, Bahamas, Aruba, Antigua, Barbuda, Barbados, Bermuda, Costa Rica, Dominica, Dominican Republic, Grenada, Guyana, Honduras, Jamaica, Saint Lucia, Trinidad and Tobago, Midway Islands, Palmyra Atoll, Baker Island, Howland Island, Jarvis Island, Johnston Island, Kingman Reef, and Wake Island.

Conventions on Cruise Ships

Deductions related to conventions directly related to a trade or business that are held aboard cruise ships are limited to $2,000 per individual per calendar year. In addition, the ship must be a U.S.-registered vessel, and all of its ports-of-call must be in the United States or its possessions. Finally, the following information has to be attached to the taxpayers' return in the year the deduction is claimed:

- A signed statement showing the total days of the trip (excluding travel to and from the ship), the number of hours each day spent attending scheduled business activities, and the program of the convention's scheduled business activities.
- A statement signed by an officer of the sponsoring organization that includes a schedule of each day's business activities and the number of hours the taxpayer spent attending those activities.

Conclusion

Regardless if travel is strictly business-related or is a combination of business and vacation, it is prudent to be thorough and complete in maintaining adequate documentation that clearly establishes the business purpose of the travel, as the burden of proof is on the taxpayer. The tax implications and recordkeeping requirements of travel, particularly foreign travel, are rather complex.

For Further Information

The Tax Accounting Group has developed a business-travel log, available upon request, which facilitates recordkeeping. If you would like to receive that tool and discuss the complexities addressed in this *Alert* further, or if you would like us to review your planned domestic or foreign travel from a tax perspective, please contact Michael A. Gillen, Steven M. Packer or the Tax Accounting Group practitioner with whom you are regularly in contact. We wish you a safe and enjoyable summer.