



Department
of the
Treasury

Internal
Revenue
Service

Publication 463
Cat. No. 11081L

Travel, Entertainment, Gift, and Car Expenses

For use in preparing
1997 Returns



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Important Changes for 1997

Increase in standard meal allowance. The standard meal allowance for most areas in the United States has increased to \$30. Use of the standard meal allowance is explained in chapter 1.

Standard meal allowance for travel days you depart and return. When you travel away from home, you can claim $\frac{3}{4}$ of the standard meal allowance for the days you

depart and return. See *Travel for days you depart and return* under *Standard Meal Allowance* in chapter 1 for more information.

Increase in standard mileage rate. The standard mileage rate for the cost of operating your car in 1997 is 31½ cents a mile for all business miles. Use of the standard mileage rate is explained in chapter 4.

Depreciation limits on business cars. Generally, the total section 179 and depreciation deductions you can take on a car that you use in your business and first place in service in 1997 is \$3,160. Your depreciation cannot exceed \$5,000 for the second year of recovery, \$3,050 for the third year of recovery, and \$1,775 for each later tax year. Depreciation on cars and the section 179 deduction are covered in chapter 4.

Exceptions for clean-fuel cars. There are two exceptions to the depreciation limits. They are effective after August 5, 1997, for cars that run on clean fuel. See *Exceptions for clean-fuel cars* under *Depreciation Limits* in chapter 4.

Federal crime investigations. Certain federal employees who are participating in federal crime investigations are not subject to the 1-year rule for deducting temporary travel expenses. See *Exception for federal crime investigations* under *Temporary Assignment or Job* in chapter 1.

Officials paid on a fee basis. Certain fee-basis officials can claim their employee business expenses whether or not they itemize their other deductions on Schedule A (Form 1040). See *Special Rules* in chapter 6.

Important Reminder

Limits that apply to employee deductions. If you are an employee, deduct your work-related expenses discussed in this publication as a miscellaneous itemized deduction on Schedule A (Form 1040). Generally, the amount you can deduct is limited to the amount that exceeds 2% of your adjusted gross income. It may be further limited if your adjusted gross income is more than \$121,200 (\$60,600 if you are married filing separately). How to report your expenses is covered in chapter 6.

Introduction

You may be able to deduct business-related expenses you have for:

- ☞ Travel away from home,
- ☞ Entertainment,
- ☞ Gifts, or
- ☞ Local transportation.

Your expenses for travel away from home and for local transportation may include car expenses. This publication explains what expenses are deductible, how to report them on your return, what records you need to prove your expenses, and how to treat any expense reimbursements you may receive.

Who should use this publication. This publication deals with expenses of employees and sole proprietors. Other businesses (such as partnerships, corporations, and trusts) and employers who reimburse their employees for business expenses should refer to their tax form instructions and chapter 16 of Publication 535, *Business Expenses*, for information on deducting travel, entertainment, gift, and transportation expenses.


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

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

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

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

If you do not meet all of these conditions, you must complete Form 2106 or Form 2106-EZ and itemize your deductions to claim your expenses. See chapter 6.

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

Vehicle provided by employer. If an employer-provided vehicle was available for your use, you received a fringe benefit. Generally, your employer must include the value of the use or availability in your income as pay. However, there are exceptions if the use of the vehicle qualifies as a working condition fringe benefit (such as the use of a qualified nonpersonal use vehicle). Employers should see chapter 4 of Publication 535, *Business Expenses*, for information on fringe benefits.

A **working condition fringe** is any property or service provided to you by your employer that you could deduct as an employee business expense if you had paid for it. A **qualified nonpersonal use vehicle** is one that is not likely to be used more than minimally for personal purposes because of its design.

For information on how to report your car expenses that your employer did not provide or reimburse you for (such as when you pay for gas and maintenance for a car your employer provides), see *Vehicle Provided by Your Employer* in chapter 6.

Useful Items

You may want to see:

Publication

- 225** Farmer's Tax Guide
- 529** Miscellaneous Deductions

- 535** Business Expenses
- 1542** Per Diem Rates

Form (and Instructions)

- 1040** U.S. Individual Income Tax Return
- Schedule A (Form 1040)** Itemized Deductions
- Schedule C (Form 1040)** Profit or Loss From Business
- Schedule C-EZ (Form 1040)** Net Profit From Business
- Schedule F (Form 1040)** Profit or Loss From Farming
- 2106** Employee Business Expenses
- 2106-EZ** Unreimbursed Employee Business Expenses
- 4562** Depreciation and Amortization

See chapter 7, *How To Get More Information*, for information about getting these publications and forms.

1.

Travel Expenses

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

Travel expenses defined. For tax purposes, travel expenses are 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 field of business, trade, or profession. A necessary expense is one that is helpful and appropriate to your business. An expense does not have to be indispensable to be considered necessary. However, you cannot deduct expenses to the extent they are lavish or extravagant.

You will find examples of deductible travel expenses in *Table 1*.

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

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

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

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

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

Tax Home

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

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

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

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

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

Example. You live in Cincinnati where you have a seasonal job for 8 months and earn \$25,000. You work the remaining 4 months in Miami, also at a seasonal job, and earn \$9,000. 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 see if you have a tax home.

- 1) You have part of your business in the area of your main home and use that home for lodging while doing business there.

- 2) You have living expenses at your main home that you duplicate because your business requires you to be away from that home.
- 3) You have not left the area in which both your traditional place of lodging and your main home are located; you have a member or members of your family living at your main home; or you often use that home for lodging.

If you meet all three factors, your tax home is the home where you regularly live, and you may be able to deduct travel expenses. If you meet only two of the factors, you may have a tax home depending on all the facts and circumstances. If you meet only one factor, you are a transient; each place you work becomes your tax home 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 have not satisfied factor (1) because you did not work in Boston. You have satisfied factor (2) because you have duplicate living expenses. You also satisfy factor (3) because you do not abandon your apartment in Boston as your traditional home, you keep your community contacts, and you frequently return to live in your apartment. You have a tax home in Boston for travel expense deduction purposes.

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

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

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

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 of your travel costs in Phoenix 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 meals and lodging while you are living and working in Pittsburgh.

Temporary Assignment or Job

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

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

However, if your assignment or job is **indefinite**, that location becomes your new tax home and you cannot deduct your travel expenses while there. Your assignment or job in a single location is considered indefinite if it is realistically expected to last for more than one year, 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. You may be able to deduct the cost of relocating to your new tax home as a moving expense. See Publication 521, *Moving Expenses*, for more information.

Exception for federal crime investigations.

If you are a federal employee participating in a federal crime investigation, you may be able to deduct travel expenses even if you are away from your tax home for more than one year.

The Attorney General must certify that you are traveling:

- 1) For the federal government,

- 2) In a temporary duty status, and
- 3) To investigate or provide support services for the investigation of a federal crime.

If you qualify, the 1-year rule for deducting business travel expenses when away from your tax home does not apply.



As this publication was being prepared for print, Congress was considering legislation that would expand the definition in (3) to include prosecution of a federal crime. See Publication 553, Highlights of 1997 Tax Changes.

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

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

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

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

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

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

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

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

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

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

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

Members of the Armed Forces. If you are a member of the U.S. Armed Forces on a permanent duty assignment overseas, you are not traveling away from home. 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, which are explained in Publication 521.

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

What Are Travel Expenses?

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



When you travel away from home on business, you should keep records of all the expenses you incur and any advances you receive from your employer. You can use a log, diary, notebook, or any other written record to keep track of your expenses. The types of expenses you need to record, along with supporting documentation, are described in *Table 4*.

Deductible Travel Expenses

Deductible travel expenses include those ordinary and necessary expenses you incur while traveling away from home on business. The type of expense you can deduct depends on the facts and your circumstances.

Table 1 summarizes 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.

Additional rules on the cost of meals and on paying travel expenses for others are explained next.

Meals. You cannot deduct the cost of meals if it is not necessary for you to stop for sleep or rest to properly perform your duties unless you meet the rules for business entertainment. These rules are explained in chapter 2.

50% limit on meals. You can use either the actual cost of your meals or a standard amount to figure your meals expense. (See *Standard Meal Allowance* later in this chapter.) However, you can deduct only 50% of the cost of your unreimbursed business-related meals.

If you are reimbursed for these expenses, how you apply the 50% limit depends on whether your employer's reimbursement plan was accountable or nonaccountable. This limit applies whether the unreimbursed meal expense is for business travel or business entertainment. Chapter 2 discusses the 50% limit in more detail, and chapter 6 discusses accountable and nonaccountable plans.

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

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

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

Exception for business associate. If a business associate travels with you and meets the conditions in (2) and (3) above, you can claim the deductible travel expenses you pay for that person. A business associate is someone with whom you can reasonably expect to actively conduct business. It does not matter if you have already conducted business with the person as long as you reasonably expect to do so. A business associate can be a customer, client, supplier, employee, agent, partner, or professional advisor.

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

Example. Jerry drives to Chicago on business and takes his wife, Linda, with him. Linda is not Jerry's employee. Even if her presence serves a bona fide business purpose, her expenses are not deductible.

Jerry pays \$115 a day for a double room. A single room costs \$90 a day. He can deduct the total cost of driving his car to and from Chicago, but only \$90 a day for his hotel room. If he uses public transportation, he can deduct only his fare.

Table 1. Travel Expenses You Can Deduct

This chart summarizes expenses you can deduct when you travel away from home for business purposes. Additional rules on meals and paying travel expenses for others are explained under *Deductible Travel Expenses*.

IF you have expenses for:	THEN you can deduct the costs 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</i> and <i>Cruise ships</i> (under <i>Conventions</i>) for additional rules and limits.
Taxi, commuter bus, and airport limousine	Fares for these and other types of transportation that take you to or from: 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 may deduct actual expenses or the standard mileage rate (if you own the car), including business-related tolls and parking. If you lease a car while away from home on business, you can deduct only the business-related costs of the lease. This includes gas, oil, and repairs.
Lodging and meals	Your lodging and 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.

Standard Meal Allowance

You generally can deduct a standard amount for your daily meals and incidental expenses (**M&IE**) while you are traveling away from home on business. **Incidental expenses** include, but are not limited to, your costs for the following items:

- 1) Laundry, dry cleaning, and pressing of clothing, and
- 2) Fees and tips for persons who provide services, such as food servers and luggage handlers.

Incidental expenses do not include taxicab fares or the costs of telegrams or telephone calls. In this publication, "standard meal allowance" refers to the federal rate for M&IE (meals and incidental expenses).

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



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. You cannot use the standard meal allowance, however, if you are related to your employer as defined next.

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

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

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

Limit on standard meal allowance. If you are not reimbursed or if you are reimbursed under a nonaccountable plan for meal expenses, you can 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. Accountable and nonaccountable plans are discussed in chapter 6.

Other expenses that can qualify for the standard meal allowance. You can use the standard meal allowance to prove meal expenses you incur when traveling in connection with **investment** and other **income-producing property**. You can also use it to prove meal expenses you incur when traveling for qualifying **educational purposes**. You **cannot** use the standard meal allowance to prove the amount of your meals if you are traveling for medical or charitable purposes.

Amount of standard meal allowance. The standard meal allowance is the federal M&IE rate. For travel in 1997, the rate is **\$30 a day** for most areas in the United States. Other locations in the United States are designated as high-cost areas, qualifying for higher standard meal allowances. Locations qualifying for rates of \$34, \$38, or \$42 a day are listed in *Appendix A*.

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

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 federal per diem rates for these locations are published monthly in the *Maximum Travel Per Diem Allowances for Foreign Areas*.



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

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



You can also order it by calling the Government Printing Office at 1-202-512-1800 (not a toll-free number).



Internet access. Per diem rates are also available on the Internet.

If you have a computer and a modem, you can access domestic per diem rates at:

www.policyworks.gov/perdiem

You can access foreign per diem rates at:

www.state.gov/www/perdiems

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:

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

If this applies to you, you can claim a **\$36 a day** standard meal allowance (\$40 for travel outside the continental United States).

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

Travel for days you depart and return. For both the day your travel begins and the day your travel ends, you must prorate the standard meal allowance. You can do so by one of two methods.

- 1) You can claim $\frac{3}{4}$ of the standard meal allowance, or
- 2) You can use 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 three-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 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.

Trip Primarily for Business

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

Example. You work in Atlanta and take a business trip to New Orleans. On your way home, you stop in Mobile to visit your parents. You spend \$630 for the 9 days you are away from home for travel, meals, lodging, and other travel expenses. If you had not stopped in Mobile, you would have been gone only 6 days, and your total cost would have been \$580. You can deduct \$580 for your trip, including the cost of round-trip transportation to and from New Orleans. The cost of your meals is subject to the 50% limit on meals 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 in this section. Travel outside the United States does not include travel from one point in the United States to another point in the United States. The following discussion can help you determine whether your trip was entirely within the United States.

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

Example. You fly from New York to Puerto Rico with a scheduled stop in Miami. You return to New York nonstop. The flight from New York to Miami is in the United States, so only the flight from Miami to Puerto Rico is outside the United States. 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.

Private plane. If you travel by private plane, any trip, or part of a trip, for which both your takeoff and landing are in the United States is travel in the United States. This is true even if part of your flight is over a foreign country.

Example. You fly nonstop from Seattle to Juneau. Although the flight passes over Canada, the trip is considered to be travel in the United States. This is because both your takeoff and landing are in the United States.

Travel Outside the United States

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

How much of your travel expenses 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

Even if your trip is not entirely for business, it may be considered entirely for business if certain conditions are met.

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

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

Exception 1 – No substantial control.

Your trip is considered entirely for business if you did not have substantial control over arranging the trip. You are not considered to have substantial control merely because you have control over the timing of your trip.

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

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

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

another, to decide on the need for the business travel.

A self-employed person generally has substantial control over arranging business trips.

Exception 2 – Outside U.S. 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 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, but 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 $\frac{5}{21}$ (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 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 not entirely for business. If you do not meet any of the above exceptions, you may still be able to deduct some of your expenses. See *Travel Primarily for Business*, next.

Travel Primarily for Business

If you travel outside the United States primarily for business purposes but spend some of your time on nonbusiness 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 nonbusiness activities to determine your deductible amount. See *Travel allocation rules*, below.

Exception. 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 purposes, 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 travel days outside the United States.

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

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

Presence required. Count as a business day any day 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, personal visiting, or other nonbusiness activity.

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

Nonbusiness activity on the way to or from your business destination. If you had a vacation or other nonbusiness activity between the United States and your business destination, or between your business destination and the United States, you must allocate your travel expenses between business and nonbusiness days. You determine your total allowable travel expenses as follows.

- 1) Divide the number of business days by the total number of travel days.
- 2) Multiply the result in (1) by the cost of round-trip travel between the United States and your nonbusiness destination.
- 3) Add to the result in (2) the round-trip cost of travel between the United States and your business destination minus the round-trip cost of travel between the United States and your nonbusiness destination. This is the deductible part of your cost of getting to and from your business destination.
- 4) Add to the result in (3) your business travel expenses (such as meals, lodging, and taxi fares) while at your business destination. These are your total allowable travel expenses.

Example. You live in New York and flew to Paris on May 4 to attend a conference with a customer that began on May 5. The conference ended at noon on May 8. That evening you flew to Dublin where you visited with friends until the afternoon of May 21, when you flew home to New York. The primary purpose for the trip was to attend the conference.

If you had not stopped in Dublin, you would have arrived home the evening of May 8. You were outside the United States more than a week, and you are unable to show that you had no substantial control over arranging the trip or that a personal vacation was not a major consideration in making the trip. May 4 through May 8 (5 days) are business days and May 9 through May 21 (13 days) are nonbusiness days. You cannot deduct your expenses while in Dublin. You also cannot deduct $\frac{13}{18}$ of the cost of round-trip airfare and any other expenses from New York to Dublin.

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

- 1) $\frac{5}{18}$ of the round-trip airfare and other expenses between New York and Dublin, **plus**
- 2) The cost of the round-trip fare and any other expenses between New York and Paris minus the cost of the round-trip fare and any other expenses between New York and Dublin.

Assume the round-trip plane fare and other expenses between New York and Paris are \$800 and the expenses between New York and Dublin are \$600. Your deductible plane fare and other expenses are \$366.67 [$(\frac{5}{18} \times \$600) + (\$800 - \$600)$].

Nonbusiness activity at or beyond business destination. If you had a vacation or other nonbusiness activity at or beyond your business destination, you must allocate your

travel expenses between your business and nonbusiness days. None of your travel expenses for nonbusiness activities at or beyond your business destination are deductible. You must also allocate your round-trip travel costs between the United States and your business destination as follows.

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

Add to this result your other business-related travel expenses (such as meals, lodging, and taxi fares) at your business destination. The sum is your total deductible travel expenses.

Example. Assume that the dates are the same as in the prior example but that instead of going to Dublin for your vacation you fly to Venice, Italy, for a vacation. You cannot deduct any part of the cost of your trip from Paris to Venice and return to Paris. In addition, you cannot deduct $\frac{13}{18}$ of the airfare and other expenses from New York to Paris and back to New York. You can deduct $\frac{5}{18}$ of the round-trip plane fare and other travel expenses from New York to Paris, plus your meals, lodging, and any other business expenses you had in Paris. If the round-trip plane fare and other travel expenses are \$800 from New York to Paris, you can deduct travel costs of \$222.22 ($\frac{5}{18} \times \800).

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

Travel Primarily for Vacation

If you travel outside the United States primarily for vacation or for investment purposes, the entire cost of the trip is a nondeductible personal expense. This is true even if you spend some time attending brief professional seminars or a continuing education program. You can, however, deduct your registration fees and any other expenses incurred that were 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 incurred by you for the five planned sessions you attended that are directly related and beneficial to your business are deductible business expenses. These expenses should be specifically stated to ensure proper allocation of your deductible business expenses.

Luxury Water Travel

If you travel by ocean liner, cruise ship, or other form of luxury water transportation for the purpose of carrying on your trade or business, there is a limit on the amount you can deduct. You cannot deduct more than **twice** the federal per diem rate allowable at the time of your travel. For purposes of this limit, the federal per diem is the highest amount allowed as a daily allowance for living expenses to employees of the executive branch of the federal government while they are away from home but in the United States.

Daily limit on luxury water travel. The highest per diem amount allowed and the daily limit for luxury water travel in 1997 is shown in the following table.

1997 Dates	Highest Federal Per Diem	Daily Limit on Luxury Water Travel
Jan. 1- Mar. 31	\$ 223	\$ 446
Apr. 1- Apr. 30	\$14	\$28
May 1- May 31	\$09	\$18
June 1- Oct. 31	\$21	\$42
Nov. 1- Dec. 31	\$23	\$46

Example. Caroline, a travel agent, took an ocean liner from New York to London, England, on business in May. Her expense for the 6-day cruise was \$2,600. Caroline's deduction for the cruise cannot exceed \$2,508 (6 days \times \$418 daily limit).

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

Example. In the previous example, Caroline's luxury water travel had a total cost of \$2,600. Of that amount, \$1,600 was separately stated as meals and entertainment. Caroline, who is self-employed, is not reimbursed for any of her travel expenses. Caroline computes her deductible travel expenses as follows.

Meals and entertainment	\$1,600
50% limit	$\times .50$
Allowable meals & entertainment .	\$ 800
Other luxury water travel expenses .	$+ 1,000$
Allowable cost before the daily limit	\$1,800
Daily limit for May 1997	\$418
Times number of days	$\times 6$
Maximum luxury water travel deduction	\$2,508
Amount of allowable deduction	<u>\$1,800</u>

Caroline's deduction for her cruise is limited to \$1,800, even though the per diem rate is higher.

Not separately stated. If your meal or entertainment charges are not separately stated or are not clearly identifiable, you do

not have to allocate any portion of the total charge to meals or entertainment.

Exceptions

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

Conventions

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

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

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

Conventions Held Outside the North American Area

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

North American area. The North American area includes:

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

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

- 1) The purpose of the meeting and the activities taking place at the meeting,
- 2) The purposes and activities of the sponsoring organizations or groups,
- 3) The 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, and

- 4) Other relevant factors you may present.

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

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

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

limited. Generally, you can deduct only 50% of your unreimbursed entertainment expenses. This limit is discussed later under *50% Limit*.

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

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

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

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

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

Deduction may depend on your type of business. Your kind of business may determine if a particular activity constitutes entertainment. For example, if you are a dress designer and have a fashion show to introduce your new designs to store buyers, the show generally is not considered entertainment. 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.

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

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

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

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

Entertainment tickets. The amount you can deduct for entertainment tickets is generally limited to the face value of the ticket even if you paid a higher price. For example, you cannot deduct service fees you pay to ticket agencies or brokers or any amount over the face value of the tickets you pay to scalpers.

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

2. Entertainment Expenses

You may be able to deduct business-related entertainment expenses you have for entertaining a client, customer, or employee. The rules and definitions are summarized in *Table 2*.

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

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

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

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

Even if you meet all the requirements for claiming a deduction for entertainment expenses, the amount you can deduct may be

What Entertainment Expenses Are Deductible?

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

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

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

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

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

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

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

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

Skyboxes and other private luxury boxes. If you rent a skybox or other private luxury box for more than one event at the same sports arena, your deduction is generally limited to the price of a nonluxury box seat ticket.

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

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

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

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

Table 2. **When Are Entertainment Expenses Deductible?**

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

Directly-Related Test

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

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

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

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

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

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

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

Expenses not considered directly related. Expenses generally are not considered directly related when entertainment occurs

where, because of substantial distractions, there is little or no possibility of engaging in the active conduct of business. Examples are:

- 1) A meeting or discussion at a nightclub, theater, or sporting event,
- 2) A meeting or discussion during what is essentially a social gathering, such as a cocktail party, or
- 3) A meeting with a group that includes persons who are not business associates at places such as cocktail lounges, country clubs, golf clubs, athletic clubs, or vacation resorts.

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

Associated Test

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

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

- 1) Is associated with your trade or business, and
- 2) Directly precedes or follows a substantial business discussion (defined later).

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

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

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

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

Directly before or after business discussion. Entertainment that is held on the same day as the business discussion is con-

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

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

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

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

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

50% Limit

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

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

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

Covered expenses. Taxes and tips relating to a business meal or entertainment activity are included in the amount that is subject to the 50% limit. Expenses such as cover charges for admission to a nightclub, rent paid for a room in which you hold a dinner or cocktail party, or the amount paid for parking at a sports arena are subject to the 50% limit. However, the cost of transportation to and from a business meal or a business-

related entertainment activity is not subject to the 50% limit.

Separating costs. If you pay or incur an expense for goods and services consisting of meals, entertainment, and other services (such as lodging or transportation), you must allocate that expense between the cost of meals and entertainment and the cost of the other services. You must have a reasonable basis for making this allocation. For example, you must allocate your expenses if a hotel includes one or more meals in its room charge, or if you are provided with one per diem amount to cover both your lodging and meal expenses.

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

The 50% limit also applies to activities that are not a trade or business. It applies to meal and entertainment expenses incurred for the production of income, including rental or royalty income. It also applies to 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 and entertainment expenses that would be deductible under the rules discussed in this publication.

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

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

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

Exceptions to the 50% Limit

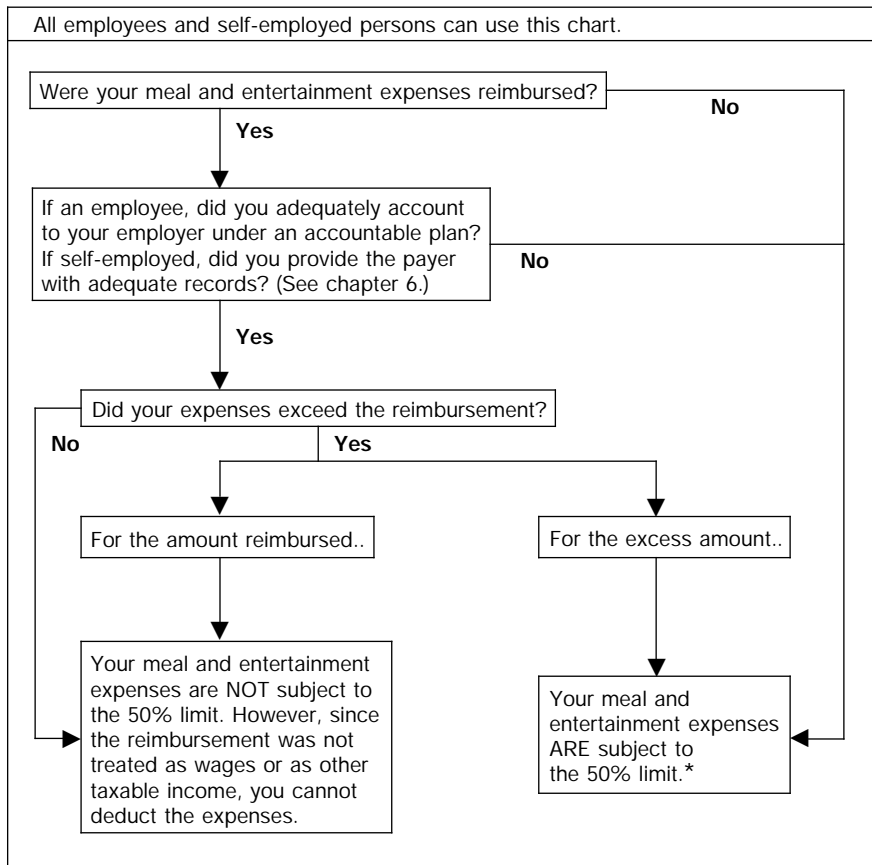
The 50% limit on meal and entertainment expenses applies if the expense is otherwise deductible based on the tests and rules explained in this chapter or in chapter 1.

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

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

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

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



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

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

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

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

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

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

Advertising expenses. You can deduct the cost of providing meals, entertainment, or recreational facilities to the general public as

a means of advertising or promoting goodwill in the community. For example, the expense of sponsoring a television or radio show is deductible, as is the expense of distributing free food and beverages to the general public. Expenses under this exception are **not** subject to the 50% limit.

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

3. Business Gift Expenses

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

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

A gift to the spouse of a business customer or client is generally an indirect gift to the customer or client. This rule does not apply if you have an independent bona fide business connection with the spouse and the gift is not intended for the other spouse's eventual use or benefit. These rules also apply to gifts you give to any other family member.

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

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

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

Exceptions. The following items are not included in the \$25 limit for business gifts.

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

Examples include pens, desk sets, and plastic bags and cases.
- 2) Signs, display racks, or other promotional material to be used on the business premises of the recipient.

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

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

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

You can change your treatment of the tickets at a later date, but not after the time allowed for the assessment of income tax. In most instances, this assessment period ends 3 years after the due date of your income tax return.

If you go with the customer to the event, you must treat the cost of the tickets as an entertainment expense. You cannot choose, in this case, to treat the tickets as a gift expense.

4.

Local Transportation Expenses

This chapter discusses expenses you can deduct for local business transportation. This includes the cost of transportation by air, rail, bus, taxi, etc., and the cost of driving and maintaining your car.

Local business transportation does *not* include expenses you have while traveling away from home overnight. Those expenses are deductible as travel expenses and are discussed in chapter 1. However, if you use your car while traveling away from home overnight, use the rules in this chapter to figure your deduction. See *Car Expenses*, later.

Local transportation expenses include the ordinary and necessary costs of:

- Getting from one workplace to another in the course of your business or profession when you are traveling within your tax home (Tax home is defined in chapter 1.),
- Visiting clients or customers,
- Going to a business meeting away from your regular workplace, and
- Getting from your home to a temporary workplace when you have one or more regular places of work. These temporary workplaces can be either within the area of your tax home or outside that area.

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

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

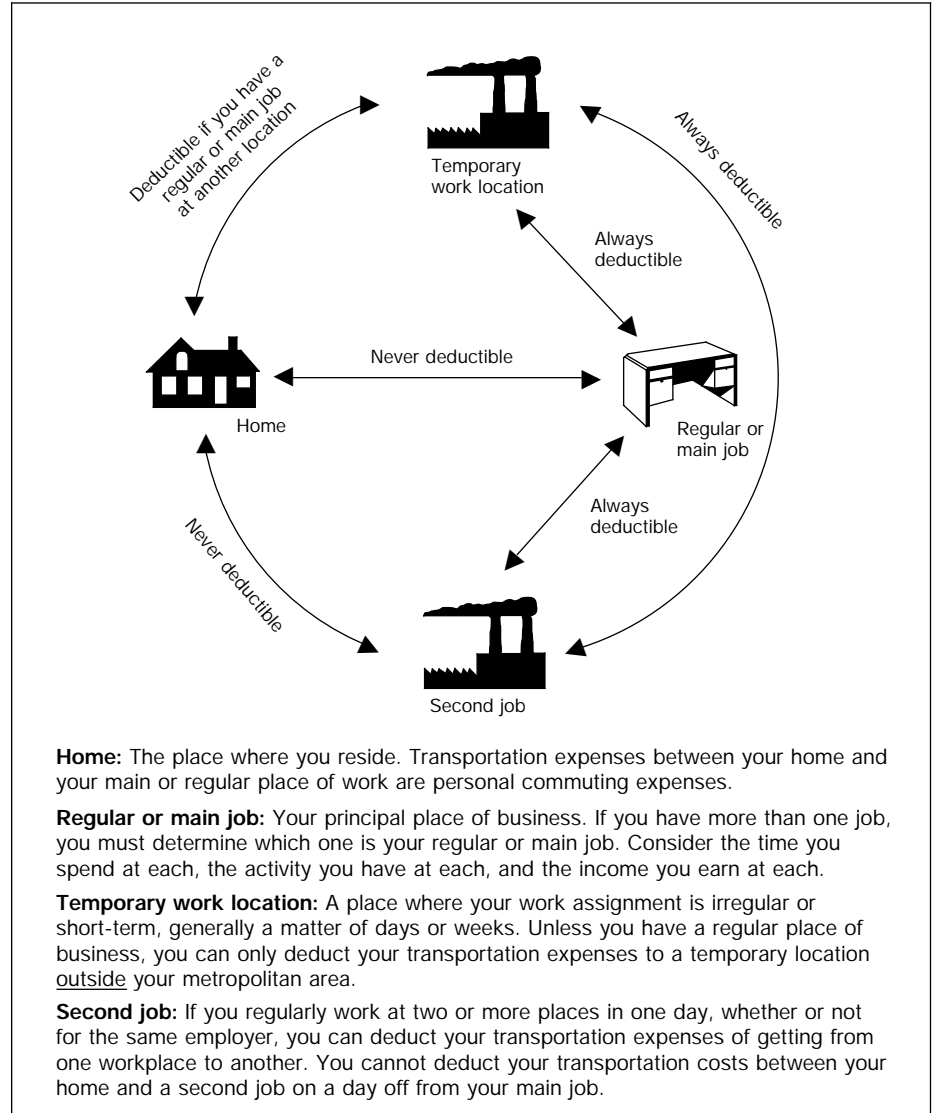
Illustration of local transportation. *Figure B* illustrates the rules for when you can deduct local transportation expenses when you have a regular or main job away from your home. You may want to refer to it when deciding whether you can deduct your local business transportation expenses.

Figure B. When Are Local Transportation Expenses Deductible?

All employees and self-employed persons can use this chart.

(Do not use this chart if your home is your principal place of business.

See *Office in the home*.)



Temporary work location. If you have one or more regular places of business and commute to a temporary work location, you can deduct the expenses of the daily round-trip transportation between your home and the temporary location. The temporary work must be irregular or short term (generally a matter of days or weeks).

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

If you have no regular place of work but ordinarily work in the metropolitan area where you live, you can deduct daily transportation costs between home and a temporary work site **outside** that metropolitan area. Generally, a metropolitan area includes the area within the city limits and the suburbs that are considered part of that metropolitan area. You cannot deduct daily transportation costs between your home and temporary work sites **within** your metropolitan area. These are nondeductible commuting costs.

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

Armed Forces reservists. A meeting of an Armed Forces reserve unit is considered a second place of business if the meeting is held on a day on which you work at your regular job. You can deduct the expense of getting to or from one workplace to the other as just discussed under *Two places of work*.

You usually cannot deduct the expense if the reserve meeting is held on a day on which you do not work at your regular job. In this case, your transportation is generally considered a nondeductible commuting cost. However, you can deduct your expenses if the

location of the meeting is temporary and you have one or more regular places of work.

If you ordinarily work in a particular metropolitan area but not at any specific location and the reserve meeting is held at a temporary location outside that metropolitan area, you can deduct your daily transportation expenses.

If you travel away from home overnight to attend a guard or reserve meeting, you can deduct your travel expenses. These are discussed in chapter 1.

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

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

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

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

Car pools. You cannot deduct the cost of using your car in a nonprofit car pool. Do not include payments you receive from the passengers in your income. These payments are considered reimbursements of your expenses. However, if you operate a car pool for a profit, you must include these payments from passengers in your income. You can then deduct your car expenses (using the rules in this publication).

Hauling tools or instruments. If you haul tools or instruments in your car while commuting to and from work, this does not make your car expenses deductible. However, if you have additional costs for hauling tools or instruments (such as for renting a trailer you tow with your car), you can deduct those additional costs.

Union members' trips from a union hall. If you get your work assignments at a union hall and then go to your place of work, the costs of getting from the union hall to your place of work are nondeductible commuting expenses.

Example. You are a banquet waitress who works at several locations in your hometown area. You must appear at the union hall to get your work assignment for the day. Although you need the union to get the job, you are employed where you work, not where the union hall is located. You cannot deduct the cost of the trips from your union hall to your place of work.

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

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

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


Example 1. You regularly work in an office in the city where you live. Your employer sends you to a one-week training session at a different office in the same city. You travel directly from your home to the training location and return each day. You can deduct the cost of your daily round-trip transportation between your home and the training location.

Example 2. Your principal place of business is in your home. You can deduct the cost of round-trip transportation between your qualifying home office and your client's or customer's place of business.

Example 3. You have no regular office, and you do not have an office in your home. In this case, the location of your first business contact is considered your office. Transportation expenses between your home and this first contact are nondeductible commuting expenses. Transportation expenses between your last business contact and your home are also nondeductible commuting expenses. Although you cannot deduct the costs of these trips, you can deduct the costs of going from one client or customer to another.

Car Expenses

If you use your car for business purposes, you may be able to deduct car expenses. You generally can use one of two methods to figure your expenses: actual expenses or the standard mileage rate. In this publication, "car" includes a van, pickup, or panel truck.

 **TIP** You may be entitled to a tax credit for an electric vehicle or a deduction from gross income for a part of the cost of a clean-fuel vehicle that you place in service during the year. The vehicle must meet certain requirements, and you do not have to use it in your business to qualify for the credit or the deduction. However, you must reduce your basis for depreciation of the clean-fuel vehicle property by the amount of the credit or deduction you claim. See Depreciation Deduction, later. For more information on clean-fuel vehicles, see chapter 15 of Publication 535.

Standard Mileage Rate

You may be able to use the standard mileage rate to figure the deductible costs of operating your car for business purposes. You can use the standard mileage rate only for a car that you own.

For 1997, the standard mileage rate is

31½ cents a mile for all business miles (47¼ cents a mile for U.S. Postal Service employees with rural routes). These rates are adjusted periodically for inflation.



If you choose to use the standard mileage rate, you **cannot** deduct your actual car expenses. These include depreciation, maintenance and repairs, gasoline (including gasoline taxes), oil, insurance, and vehicle registration fees.

You generally can use the standard mileage rate whether or not you are reimbursed and whether or not any reimbursement is more or less than the amount figured using the standard mileage rate. See chapter 6 for more information on reimbursements.

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

If you choose to use the standard mileage rate, you are considered to have chosen not to use the depreciation methods discussed later. This is because the standard mileage rate includes an allowance for depreciation. You also cannot claim the section 179 deduction (discussed later) if you use the standard mileage rate. If you change to the actual expenses method in a later year, but before your car is considered fully depreciated, you have to estimate the remaining useful life of the car and use straight line depreciation. See the exception in *Methods of Depreciation* under *Depreciation Deduction*, later.

Standard mileage rate not allowed. You cannot use the standard mileage rate if you:

- 1) Do not own the car,
- 2) Use the car for hire (such as a taxi),
- 3) Operate two or more cars at the same time (as in fleet operations),
- 4) Claimed a deduction for the car in an earlier year using ACRS or MACRS depreciation (discussed later), or
- 5) Claimed a section 179 deduction (discussed later) on the car.

Two or more cars. If you own two or more cars that are used for business at the same time, you cannot use the standard mileage rate for the business use of any car. However, you may be able to deduct a part of the actual expenses for operating each of the cars. See *Actual Car Expenses* for information on how to figure your deduction.

You are **not** using two or more cars for business at the same time if you alternate using (use at different times) the cars for business.

The following examples illustrate the rules for when you can and cannot use the standard mileage rate for two or more cars.

Example 1. Marcia, a salesperson, owns a car and a van that she alternates using for calling on her customers. She can use the standard mileage rate for the business mileage of the car and the van.

Example 2. Tony uses his own pickup truck in his landscaping business. During the year, he traded in his old truck for a newer one. Tony can use the standard mileage rate

for the business mileage of both the old and the new trucks.

Example 3. Chris owns a repair shop and an insurance business. He uses his pickup truck for the repair shop and his car for the insurance business. No one else uses either the pickup truck or the car for business purposes. Chris can use the standard mileage rate for the business use of the truck and the car.

Example 4. Maureen owns a car and a van that are both used in her housecleaning business. Her employees use the car and she uses the van to travel to the various customers. Maureen cannot use the standard mileage rate for the car or the van. This is because both vehicles are used in Maureen's business at the same time. She must use actual expenses for both vehicles.

Interest. If you are an employee, you cannot deduct any interest paid on a car loan. This applies even if you use the car 100% for business as an employee.

However, if you are self-employed and use your car in your business, you can deduct that part of the interest expense that represents your business use of the car. For example, if you use your car 50% for business, you can deduct 50% of the interest on Schedule C (Form 1040). You cannot deduct the rest of the interest expense.

Personal property taxes. If you itemize your deductions on Schedule A (Form 1040), you can deduct on line 7 state and local personal property taxes on motor vehicles. You can take this deduction even if you use the standard mileage rate or if you do not use the car for business.

If you are self-employed and use your car in your business, you can deduct the business part of state and local personal property taxes on motor vehicles on Schedule C, Schedule C–EZ, or Schedule F (Form 1040).

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

Sale, trade-in, or other disposition. If you sell, trade in, or otherwise dispose of your car, you may have a gain or loss on the transaction or an adjustment to the basis of your new car. See *Disposition of a Car*, later.

Actual Car Expenses

If you do not choose to use the standard mileage rate, you may be able to deduct your actual car expenses.

TIP If you qualify to use both methods, figure your deduction both ways to see which gives you a larger deduction.

Actual car expenses include the costs of:

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

If you have fully depreciated a car that you are still using in your business, you can continue to claim your other actual expenses for the business use of your car. Continue to

keep records, as explained later in chapter 5.

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

Example. You are a sales representative for a clothing firm and drive your car 20,000 miles during the year: 12,000 miles for business and 8,000 miles for personal use. You can claim only 60% (12,000 ÷ 20,000) of the cost of operating your car as a business expense.

Employer-provided vehicle. If you use a vehicle provided by your employer for business purposes, you can deduct your actual unreimbursed car expenses. You cannot use the standard mileage rate if you do not own the car. See *Vehicle Provided by Your Employer* in chapter 6.

Interest on car loans. If you are an employee, you cannot deduct any interest paid on a car loan. This interest is treated as personal interest and is not deductible. If you are self-employed and use your car in that business, see *Interest*, earlier, under *Standard Mileage Rate*.

Taxes paid on your car. If you are an employee, you can deduct personal property taxes paid on your car if you itemize deductions. Enter the amount paid on line 7 of Schedule A (Form 1040).

You cannot deduct luxury or sales taxes, even if you use your car 100% for business. Luxury and sales taxes are part of your car's basis and may be recovered through depreciation. See *Depreciation Deduction*, later.

Fines and collateral. Fines and collateral for traffic violations are not deductible.

Casualty and theft losses. If your car is damaged, destroyed, or stolen, you may be able to deduct part of the loss that is not covered by insurance, whether or not you used your car entirely for business. See Publication 547, *Casualties, Disasters, and Thefts (Business and Nonbusiness)*, for information on deducting a loss on your car.

Depreciation. Generally, the cost of a car, plus sales tax, luxury tax, and improvements, is a capital expense. Because the benefits last longer than one year, you generally cannot deduct a capital expense. However, you can recover this cost by claiming a section 179 deduction (the deduction allowed by section 179 of the Internal Revenue Code) and/or a depreciation deduction. In other words, you recover the cost over more than one year by deducting part of it each year. The section 179 deduction and the depreciation deduction are discussed later.

Generally, there are limits on both of these deductions, and special rules apply if you use your car 50% or less in your work or business.

You can claim a section 179 deduction and a depreciation method other than straight line only if you do not use the standard mileage rate to figure your business-related car expenses in the year you first place a car in service. If you claim either a depreciation deduction or a section 179 deduction in the year you first place a car in service, you cannot

use the standard mileage rate on that car in any future year.

Car defined. For depreciation purposes, a car is any four-wheeled vehicle that is made primarily for use on public streets, roads, and highways. It must have an unloaded gross vehicle weight of 6,000 pounds or less. A truck or van is included in the definition only if it has a gross vehicle weight of 6,000 pounds or less. A car includes any part, component, or other item that is physically attached to it or is traditionally included in the purchase price.

A car does not include:

- 1) An ambulance, hearse, or combination ambulance-hearse used directly in a business, and
- 2) A vehicle used directly in the business of transporting persons or property for pay or hire.

See Publication 946, *How To Depreciate Property*, for more information on how to depreciate your vehicle.

Section 179 Deduction

The section 179 deduction allows you to choose to treat part or all of the business cost of a car as an expense rather than taking depreciation deductions over a specified recovery period. As an expense, the section 179 amount is deductible only in the year the car is placed in service. For this purpose, "placed in service" means the year you first use the car for any purpose. A car first used for personal purposes cannot qualify for the deduction in a later year when its use changes to business.

Example. In 1995 you bought a new car and placed it in service for personal purposes. In 1997 you began to use it for business. The fact that you changed its use to business use does not qualify the cost of your car for a section 179 deduction in 1997. However, you can claim a depreciation deduction for the business use of the car in 1997. See *Depreciation Deduction*, later.

Limits. There are limits on:

- 1) The total cost of property qualifying for a section 179 deduction, and
- 2) The total amount of the section 179 deduction **plus** the depreciation deduction (discussed later).

Limit on cost of qualifying property. Generally, you can choose to treat up to \$18,000 of the cost of qualifying property as a section 179 deduction in 1997. The yearly limit, however, depends on the percentage of business use, and you must use the property **more than 50%** for business to claim any section 179 deduction.

TIP The limit on the cost of property qualifying for the section 179 deduction increases each year up to 2003. However, the maximum limits for the business cost of a car, discussed later, continue to apply.

Example. Peter purchased a car this year for \$4,500 and he used it 60% for business. The total cost of Peter's car that qualifies for the section 179 deduction is \$2,700 (\$4,500 cost × 60% business use). But see *Limit on total section 179 and depreciation deductions*, discussed next.

Limit on total section 179 and depreciation deductions. The total amount of section 179 and depreciation deductions that you can claim for a car that you place in service in 1997 cannot be more than \$3,160. The limit is reduced if your business use of the car is less than 100%. See *Depreciation Limits*, later, for more information.

Example. Peter, in the previous example, had a car with a qualifying cost of \$2,700 for his section 179 deduction. However, Peter is limited to a total section 179 deduction plus depreciation deduction of \$1,896 (\$3,160 limit × 60% business use).

Cost of car. The business cost of the car for purposes of the section 179 deduction does not include any amount figured by reference to any other property held by you at any time. For example, if you trade in a used car on a new car to use in your business, your cost for purposes of the section 179 deduction does not include the adjusted basis of the car you trade in for the new car.

Basis of car. The amount of the section 179 deduction reduces the basis of your car. If you choose the section 179 deduction, you must reduce the basis of your car before you figure your depreciation deduction.

Generally, choosing a section 179 deduction gives you a larger total deduction (depreciation plus section 179 deduction) in the first year. Not choosing it gives you a larger depreciation deduction in the later years.

Example. On January 3, 1997, Stella bought a car for \$12,000, including sales tax, to use exclusively in her delivery business. She paid \$9,000 cash and received \$3,000 in trade for her old car (also used in her business). The adjusted basis of her old car was \$3,000.

Stella's cost of the new car is \$9,000 for purposes of section 179. Her basis for depreciation would be \$12,000 if she does not choose section 179. The total of her section 179 and depreciation deductions is limited to \$3,160, the first year maximum. If she does not choose section 179, her depreciation deduction, using the MACRS method (discussed later), would be \$2,400 [\$12,000 basis × 20% (double declining balance rate)] from Table 3, explained later.

When to choose. If you want to take the section 179 deduction, you must make the choice in the tax year you both purchase the car **and** place it in service for business or work. Employees use Form 2106 to make this choice and report the section 179 deduction. All others use Form 4562. Make your choice by taking the deduction on the appropriate form and file it with your original tax return. You cannot make the choice on an amended tax return filed after the due date (including extensions). Once made, the choice can be changed only with the consent of the Internal Revenue Service (IRS).

Reduction in business use. To be eligible to claim the section 179 deduction, you must use your car more than 50% for business or work in the year you acquired it. If your business use of the car is 50% or less in a later tax year during the recovery period, you have to include in income in that later year any excess depreciation. Any section 179 deduction claimed on the car is included in calculating the excess depreciation. For infor-

mation on this calculation, see *Excess depreciation* later in this chapter under *Car Used 50% or Less for Business*.

Dispositions. If you dispose of a car on which you had claimed the section 179 deduction, the amount of that deduction is treated as a depreciation deduction for recapture purposes. Any gain on the disposition of the property is treated as ordinary income up to the amount of the section 179 deduction and any depreciation you claimed. For information on the disposition of depreciable property, see chapter 4 of Publication 544, *Sales and Other Dispositions of Assets*.

Depreciation Deduction

If you use a car in your business, you can claim a depreciation deduction: that is, you can deduct a certain amount each year as a recovery of your cost or other basis in the car. You cannot use the standard mileage rate if you decide to take a depreciation deduction in the year you first place the car in service.

You generally need to know three things about the car you intend to depreciate. You must know:

- 1) The car's basis,
- 2) The date the car was placed in service, and
- 3) The method of depreciation you will use.

Basis. The car's basis for figuring depreciation is your original basis reduced by:

- 1) Any section 179 deduction (discussed earlier in this chapter),
- 2) Any clean-fuel vehicle deduction (discussed in Publication 535), and
- 3) Any qualified electric vehicle credit (discussed in Publication 535).

The original basis of property you buy is usually its cost. Additional rules concerning basis are discussed later in this chapter under *Unadjusted basis*.

Placed in service. A car generally is placed in service when it is available for use in your work or business, in the production of income, or in a personal activity. Depreciation begins when the car is ready for use in your work or business or for the production of income.

For purposes of computing depreciation, if you first start using the car entirely for personal use and later convert it to business use, the car is treated as placed in service on the date of conversion. Your basis is the lesser of the fair market value or the car's adjusted basis on the date of conversion.

Car placed in service and disposed of in the same year. If you place a car in service and dispose of it in the same tax year, you cannot claim any depreciation deduction for that car.

Methods of depreciation. Generally, one depreciation system is available for cars: modified accelerated cost recovery system (MACRS). MACRS rules for cars are discussed later in this chapter.

Exception. If you used the standard mileage rate in the first year of business use and change to the actual expenses method in a later year, you cannot depreciate your car under the MACRS rules. You must use straight line depreciation over the estimated remaining useful life of the car.

To figure depreciation under the straight line method, you must reduce your basis in the car (but not below zero) by a set rate per mile for all miles for which you used the standard mileage rate. The rate per mile varies depending on the year(s) you used the standard mileage rate. For the rate(s) to use, see *Depreciation adjustment when you used the standard mileage rate under Disposition of a Car*, later.

This reduction to basis is in addition to those basis adjustments described later under *Unadjusted basis*. You must use the adjusted basis of your car to figure your depreciation deduction. For additional information on how to figure your depreciation under this exception, use the information in Publication 534, *Depreciating Property Placed in Service Before 1987*.

Cars placed in service before 1987. If you are still depreciating a car you placed in service before 1987, continue to follow the rules appropriate for that method. See Publication 534 for more information.

Percentage of business use. Generally, you must use a car more than 50% for a qualified business use (defined next) to qualify for the section 179 deduction and MACRS deduction. If your business use is 50% or less, you must use the straight line method to depreciate your car. This is explained later under *Car Used 50% or Less for Business*.

Qualified business use. A qualified business use is any use in your trade or business. It does not include use for the production of income (investment use). However, after you have satisfied the 50%-business-use requirement, you may combine your business and investment use to compute any allowable deduction for a tax year.

Use of your car by another person. Do not treat any use of your car by another person as use in your trade or business unless that use meets one of the following three conditions.

- 1) It is directly connected with your business,
- 2) It is properly reported by you as income to the other person (and, if you have to, you withhold tax on the income), or
- 3) It results in a payment of fair market rent. This includes any payment to you for the use of your car.

Business use changes. If you used your car more than 50% in a qualified business use in the year you placed it in service, but 50% or less in a later year (including the year of disposition), you have to change to the straight line method of depreciation. See *Business use drops to 50% or less in a later year*.

More-than-50%-use test. You meet this test for any tax year if you use your car more than 50% in a qualified business use. You must meet this test each year of the recovery period (6 years under MACRS) for your car.

If you use your car for more than one purpose during the tax year, you must allocate the use to the various purposes. You do this on the basis of mileage. Figure the percentage of qualified business use by dividing the number of miles you drive your car for business purposes during the year by the total number of miles you drive the car during the year for any purpose.



Property does not cease to be used more than 50% in a qualified business use by reason of a transfer at death.

Change from personal to business use. If you change the use of a car from 100% personal use to business use during the tax year, you may not have mileage records for the time before the change to business use. In this case, you figure the percentage of business use for the year as follows.

- 1) Determine the percentage of business use for the period following the change. Do this by dividing business miles by total miles driven during that period.
- 2) Multiply the percentage in (1) by a fraction. The numerator (top number) is the number of months the car is used for business and the denominator (bottom number) is 12.

Example. You use a car only for personal purposes during the first 6 months of the year. During the last 6 months of the year, you drive the car a total of 15,000 miles of which 12,000 miles are for business. This gives you a business use percentage of 80% (12,000 ÷ 15,000) for that period. Your business use for the year is 40% (80% × 6/12).

Limits. The amount you can claim for section 179 and depreciation deductions may be limited. Maximum limits apply depending on the year in which you placed your car in service. You have to adjust the limits if you did not use the car exclusively for business. See *Depreciation Limits*, later.

Unadjusted basis. You use your unadjusted basis to figure your depreciation using the depreciation chart explained later under *Modified accelerated cost recovery system (MACRS)*. Your unadjusted basis for figuring depreciation is your original basis increased or decreased by certain amounts.

To figure your unadjusted basis, begin with the original basis of your car, generally its cost. Cost includes sales and luxury taxes, destination charges, and dealer preparation. Increase your basis by any substantial improvements you make to your car, such as adding air conditioning or a new engine. Decrease your basis by any deductible casualty loss, diesel fuel tax credit, gas guzzler tax, clean-fuel vehicle deduction, and qualified electric vehicle credit.

If you use your car exclusively for business, subtract the section 179 deduction from the result to arrive at your unadjusted basis. If you use your car only partly for business, multiply the result by the business use percentage and then subtract the section 179 deduction to arrive at your unadjusted basis.



If your business use later falls to 50% or less, you may have to include in your income any excess depreciation. See *Car Used 50% or Less for Business*, later, for more information.

If you acquired the car by gift or inheritance, see Publication 551, *Basis of Assets*, for information on your basis in the car.

Improvements. A major improvement to a car is treated as a new item of 5-year recovery property that is placed in service in the year the improvement is made. It does not matter how old the car is when the improvement is added. Follow the same steps for depreciating the improvement as you would for depreciating the original cost of the car.

However, you must treat the improvement and the car as a whole when applying the limits on the depreciation deductions. Your car's depreciation deduction for the year (plus the depreciation on any improvements) cannot be more than the depreciation limit that applies for that year. See *Depreciation Limits*, later.

Effect of trade-in on basis. When you trade an old car for a new one, the original basis of the new car is generally the adjusted basis of the old car plus any additional payment you make.

Traded car used entirely for business. If you trade in a car that you used entirely in your business for another car that will be used entirely in your business, the original basis of the new car is the adjusted basis of the old car, plus any additional amount you pay for the new car.

Example 1. Paul trades in a car that has an adjusted basis of \$3,000 for a new car. In addition, he pays cash of \$7,000 for the new car. His original basis of the new car is \$10,000 (the \$3,000 adjusted basis of the old car plus the \$7,000 cash paid). Paul's unadjusted basis would be the same unless he claims the section 179 deduction or has other increases or decreases to his original basis.

Example 2. In July 1994, Marcia purchased a car for \$26,000 and placed it in service for 100% use in her business. She did not claim a section 179 deduction. Marcia's unadjusted basis for the car was \$26,000. For 1994 through 1996, Marcia figured her depreciation deduction using the MACRS chart for those years.

In September 1997, Marcia traded that car in and paid \$14,200 cash for a new car to be used 100% in her business. Marcia is allowed one-half of the regular depreciation amount for 1997 for her old car. (See *Disposition of a Car*, later.)

Marcia figures her original basis in the new car, \$28,192, as follows.

Cost of old car	\$26,000
Less: Total depreciation allowed from 1994 through 1997	<u>- 12,008</u>
Adjusted basis of old car	\$13,992
Plus: Additional cost for new car	<u>+ 14,200</u>
Basis of new car	<u>\$28,192</u>

Traded car used partly in business. If you trade in a car (that you acquired after June 18, 1984) that you used partly in your business for a new car that you will use in your business, you must make a "trade-in" adjustment for the personal use of the old car. This adjustment has the effect of reducing the basis of your old car, but not below zero, for purposes of figuring your depreciation deduction for the new car. (This adjustment is not used, however, when you determine the gain or loss on the later disposition of the new car.)

To figure the unadjusted basis of your new car for depreciation, first add to the adjusted basis of the old car any additional amount you pay for the new car. Then subtract from that total the excess, if any, of:

- 1) The total of the amounts that would have been allowable as depreciation during the tax years before the trade if 100% of the use of the car had been business and investment use, over
- 2) The total of the amounts actually allowable as depreciation during those years.

Example 1. In March, Mark traded his 1993 van (placed in service in 1993) for a new 1997 model. He used the old van 75% for business use and he used the new van 75% for business use in 1997. Mark claimed actual expenses for the business use of the old van since 1993. He did not claim a section 179 deduction for the old or the new van.

Mark paid \$12,800 for the 1993 van in June 1993. He paid an additional \$9,800 when he acquired the 1997 van. Mark was allowed 1/2 of the depreciation deduction amount for his old van for 1997, the year of disposition, as explained later under *Disposition of a Car*.

Mark figures the unadjusted basis for depreciating his new van as shown next:

Cost of old van	\$12,800
Less: Total depreciation allowed on the business cost of old van, \$9,600 (\$12,800 × 75%) from 1993–1997	<u>- 8,494</u>
Adjusted basis of old van	\$ 4,306
Plus: Add'l cost for new van	<u>+ 9,800</u>
Basis of new van before trade-in adjustment	\$14,106
Trade-in adjustment:	
Depreciation at 100% business use:	
1997—(\$12,800 × .1152) × 1/2 yr (Limit: \$1,675)	\$ 737
1996—12,800 × .1152 (Limit: \$1,675)	1,475
1995—12,800 × .192 (Limit: \$2,750)	2,458
1994—12,800 × .32 (Limit: \$4,600)	4,096
1993—12,800 × .20 (Limit: \$2,860)	2,560
Total	<u>\$11,326</u>
Less: Actual depreciation allowed	<u>- 8,494</u>
Excess of 100% over actual amount	\$2,832
Less: Lesser of Excess amount (\$2,832) or Adjusted basis of old van (\$4,306)	<u>- 2,832</u>
Unadjusted basis of new van for depreciation	<u>\$11,274</u>

Example 2. Rob paid \$15,000 for a new car that he placed in service in 1994. He used it partly for business in 1994 (9,000 business miles of 15,000 total miles), 1995 (12,000 business miles of 16,000 total miles), and 1996 (14,400 miles of 18,000 total miles). He used the standard mileage rate in those years to claim the business use of his car. See *Depreciation adjustment when you used the standard mileage rate under Disposition of a Car*, later.

On January 3, 1997, Rob traded in this car and paid an additional \$6,000 for his new car. Rob figures the unadjusted basis for his new car as shown next:

Cost of old car	\$15,000
Less: Total depreciation allowed:	
1996—14,400 mi. × .12	\$1,728
1995—12,000 mi. × .12	1,440
1994—9,000 mi. × .12	<u>1,080</u>
Adjusted basis of old car	\$10,752
Plus: Additional cost for new car	<u>+ 6,000</u>
Basis of new car before trade-in adjustment	\$16,752
Trade-in adjustment:	
Depreciation at 100% business use:	
1996—18,000 mi. × .12	\$2,160
1995—16,000 mi. × .12	1,920
1994—15,000 mi. × .12	<u>1,800</u>
Total	\$5,880
Less: Actual depreciation allowed	<u>4,248</u>
Excess of 100% over actual amount	\$1,632
Less: Lesser of Excess amount (\$1,632) or Adjusted basis of old car (\$10,752)	<u>- 1,632</u>
Unadjusted basis of new car for depreciation	<u>\$15,120</u>

Modified accelerated cost recovery system (MACRS). The modified accelerated cost recovery system (MACRS) is the name given to the tax rules for getting back (recovering) through depreciation deductions the cost of property used in a trade or business or to produce income.

The maximum amount you can deduct is limited, depending on the year you placed your car in service. See *Depreciation Limits*, later.

Recovery period. Under MACRS, cars are classified as 5-year property. You actually depreciate the cost of a business car, truck, or van over a period of 6 calendar years. This is because your car is generally treated as placed in service or disposed of in the middle of the year.

Depreciation deduction for certain Indian reservation property. Shorter recovery periods are provided under MACRS for qualified Indian reservation property placed in service on Indian reservations after 1993 and before 2004. The recovery period that applies for a business-use car is 3 years instead of 5 years. However, the depreciation limits, discussed later, will still apply.

For more information on the qualifications for this shorter recovery period and the percentages to use in figuring the depreciation deduction, see chapter 3 of Publication 946.

Depreciation methods. There are three methods that you can use to depreciate your car:

- 1) The 200% declining balance method (200% DB) over a 5-year recovery period that switches to the straight line method when that method provides a greater deduction,
- 2) The 150% declining balance method (150% DB) over a 5-year recovery period that switches to the straight line method when that method provides a greater deduction, and
- 3) The straight line method (SL) over a 5-year recovery period.

TIP If you use Table 3 (discussed later) to determine your depreciation rate for 1997, you do not need to determine in what year your deduction is greater using the straight line method. This is because the chart has the switch to the straight line method built into its rates.

Before choosing a method, you may wish to consider the following:

- 1) Using the straight line method provides equal yearly deductions throughout the recovery period, and
- 2) Using the declining balance methods provides greater deductions during the earlier recovery years with the deductions generally getting smaller each year.

MACRS depreciation chart. A 1997 MACRS Depreciation Chart and instructions are included in this section as Table 3. Using this table will make it easy for you to figure the 1997 depreciation deduction for your car. A similar chart appears in the *Instructions for Form 2106*.



You may have to use the tables in Publication 946 instead of using this MACRS Depreciation Chart.

You must use the Depreciation Tables in Publication 946, and not use the MACRS depreciation chart in this publication, if any of the following conditions apply to you.

- 1) You file your return on a fiscal year basis.
- 2) You file your return for a short tax year (less than 12 months).
- 3) During the year, all of the following conditions apply to you.
 - a) You placed some property in service from January through September,
 - b) You placed some property in service from October through December, and
 - c) The basis of the property you placed in service from October through December was more than 40% of the total bases of all property placed in service for the year.

If you use the percentages from the chart, you must continue to use them for the entire recovery period of your car. However, you cannot continue to use the chart if the basis of your car is adjusted because of a casualty. In that case, for the year of adjustment and the remaining recovery period, figure the depreciation without the chart using the car's adjusted basis at the end of the year of adjustment and over the remaining recovery period.



In future years, do not use the chart from this publication. Instead, use the chart in the publication or in the instructions for those future years.

If you dispose of the car before the end of the recovery period, you are generally allowed a half year of depreciation in the year of disposition unless you purchased the car during the last quarter of a year. See *Depreciation deduction for the year of disposition under Disposition of a Car*, later, for information on how to figure the depreciation allowed in the year of disposition.

How to use the 1997 chart. To figure your depreciation deduction for 1997, find the percentage in the column of the chart based on the date that you first placed the car in service and the depreciation method that you are using. Multiply the unadjusted basis of your car (defined earlier) by that percentage to determine the amount of your depreciation deduction. If you prefer to figure your depreciation deduction without the help of the chart, see Publication 946.



Your deduction cannot be more than the maximum depreciation limit for cars. See *Depreciation Limits*, later.

Example. Phil bought a used truck in February 1996 to use exclusively in his landscape business. He paid \$6,200 for the truck with no trade-in. Phil did not claim any section 179 deduction and he chose to use the 200% DB method to get the largest depreciation deduction in the early years.

Phil used the MACRS depreciation chart in 1996 to find his percentage. The unadjusted basis of his truck equals its cost be-

cause Phil used it exclusively for business. He multiplied the unadjusted basis of his truck, \$6,200, by the percentage that applied, 20%, to figure his 1996 depreciation deduction of \$1,240.

In 1997, Phil used the truck for personal purposes when he repaired his father's cabin. His records show that the business use of his truck was 90% in 1997. Phil used Table 3 to find his percentage. Reading down the first column for the date placed in service and across to the 200% DB column, he locates his percentage, 32%. He multiplies the unadjusted basis of his truck, \$5,580 (\$6,200 cost \times 90% business use), by 32% to figure his 1997 depreciation deduction of \$1,786.

Depreciation Limits

There are limits on the amount you can deduct for depreciation of your car. (The section 179 deduction is treated as depreciation for purposes of the limits.) The maximum amount you can deduct each year depends on the year you place the car in service. These limits are shown in the following table.

**Maximum Depreciation Limits
Cars Placed in Service After 1986**

Year Placed In Service	1st ^y Year ^y	2nd ^y Year ^y	3rd ^y Year ^y	4th & Later ^y Years ^y
1997	\$3,160	\$5,000	\$3,050	\$1,775 ^y
1995-1996	3,060	4,900	2,950	1,775 ^y
1994	2,960	4,700	2,850	1,675 ^y
1993	2,860	4,600	2,750	1,675 ^y
1992	2,760	4,400	2,650	1,575 ^y
1991	2,660	4,300	2,550	1,575 ^y
Pre-1991				1,475 ^y

Exceptions for clean-fuel cars. There are two exceptions to the depreciation limits. They are effective after August 5, 1997, for cars that run on clean fuel. Clean-fuel cars are discussed in chapter 15 of Publication 535. The exceptions follow.

- 1) Amounts you pay (such as for retrofit parts and components) to modify a car to run on clean fuel are not subject to the depreciation limit on cars. Only the cost of the car before modification is subject to the limit. This means you can claim an additional depreciation deduction for the amount you pay to modify a car to permit it to run on clean fuel. This rule applies to modifications placed in service after August 5, 1997.
- 2) If you place a car in service after August 5, 1997, that was produced to run on electricity, your depreciation limit for 1997 is increased to a maximum of \$9,480.

Car used less than full year. The depreciation limits are not reduced if you use a car for less than a full year. This means that you do not reduce the limit when you either place a car in service or dispose of a car during the year. However, the depreciation limits are reduced if you do not use the car exclusively for business and investment purposes. See *Reduction for personal use*, later.

Example. Marie purchased a car in June 1997 for \$16,000 to use exclusively in her business. She does not claim the section 179 deduction and she chooses the 200% DB method of depreciation.

Marie's depreciation (using the rate from Table 3) is \$3,200 (\$16,000 \times 20%). However, the maximum amount she can deduct for depreciation (from the *Maximum Depreci-*

**Table 3. 1997 MACRS Depreciation Chart
(Use to Figure Depreciation for 1997)**

If you claim actual expenses for your car, use the chart below to find the depreciation method and percentage to use for your 1997 return. If your car was placed in service before 1987, see the depreciation chart in the Form 2106 instructions.

First, using the left column, find the date you first placed the car in service. Then select the depreciation method and percentage from column (a), (b), or (c) following the rules explained in this chapter.

For cars placed in service before 1997, you must use the same method you used on last year's return unless a decline in your business use requires you to change to the straight line method. (See *Car Used 50% or Less for Business*.)

Multiply the unadjusted basis of your car by your business use percentage. Multiply the result by the percentage you found in the chart to find the amount of your depreciation deduction for 1997. (Also see *Depreciation Limits*.)



If you placed your car in service after September of any year and you placed other business property in service during the same year, you may have to use the Jan. 1—Sept. 30 percentage instead of the Oct. 1—Dec. 31 percentage for your car.

To find out if this applies to you, determine: 1) the basis of all business property you placed in service after September of that year and 2) the basis of all business property you placed in service during that entire year. If the basis of the property placed in service after September is not more than 40% of the basis of all property placed in service for the entire year, use the percentage for Jan. 1—Sept. 30 for figuring depreciation for your car. See *Conventions* in chapter 3 of Publication 946 for more details.

Example. You buy machinery (basis of \$22,000) in May 1997 and a new van (basis of \$14,000) in October 1997, both used 100% in your business. You use the percentage for Jan. 1—Sept. 30, 1997, to figure the depreciation for your van. This is because the \$14,000 basis of the property (van) placed in service after September is not more than 40% of the basis of all property placed in service during the year [40% × (\$22,000 + 14,000) = \$14,400].

Date Placed In Service	(a)		(b)		(c)	
	200% Declining Balance (200% DB) ¹		150% Declining Balancing (150% DB) ¹		Straight Line (SL)	
Oct. 1 — Dec. 31, 1997	200 DB	5.0%	150 DB	3.75%	SL	2.5%
Jan. 1 — Sept. 30, 1997	200 DB	20.0	150 DB	15.1	SL	10.0
Oct. 1 — Dec. 31, 1996	200 DB	38.0	150 DB	28.88	SL	20.0
Jan. 1 — Sept. 30, 1996	200 DB	32.0	150 DB	25.5	SL	20.0
Oct. 1 — Dec. 31, 1995	200 DB	22.8	150 DB	20.21	SL	20.0
Jan. 1 — Sept. 30, 1995	200 DB	19.2	150 DB	17.85	SL	20.0
Oct. 1 — Dec. 31, 1994	200 DB	13.68	150 DB	16.4	SL	20.0
Jan. 1 — Sept. 30, 1994	200 DB	11.52	150 DB	16.66	SL	20.0
Oct. 1 — Dec. 31, 1993	200 DB	10.95	150 DB	16.41	SL	20.0
Jan. 1 — Sept. 30, 1993	200 DB	11.52	150 DB	16.66	SL	20.0
Oct. 1 — Dec. 31, 1992	200 DB	9.58	150 DB	14.35	SL	17.5
Jan. 1 — Sept. 30, 1992	200 DB	5.76	150 DB	8.33	SL	10.0
Prior to 1992 ²						

¹You can use this column only if the business use of your car is more than 50%.

²If your car was subject to the maximum limits for depreciation and you have unrecovered basis in the car, you can continue to claim depreciation. See *Deductions in years after the recovery period* under *Depreciation Limits*.

ation Limits table) is \$3,160. (See *Deductions in years after the recovery period*, later.)

Reduction for personal use. The depreciation limits are further reduced based on your percentage of personal use. If you use a car less than 100% in your business or work, you must determine the depreciation deduction limit by multiplying the limit amount by the percentage of business and investment use during the tax year.

Example. In June 1997, Karl, an outside dental supply salesman, purchased a car for \$25,400 to make sales calls in a territory that extends 200 miles around his home base. He uses his car 85% for his business. Karl does not claim the section 179 deduction and he

chooses the 200% DB method to figure his depreciation deduction.

In 1997, Karl computes his MACRS deduction to be \$4,318 [(\$25,400 × 85%) × 20%]. However, Karl's deduction is limited to \$2,686. This is the depreciation limit (\$3,160) multiplied by the business use percentage (85%).

Karl continues to use his car 85% for business. Depreciation in the next four years continues to be subject to deduction limits. Karl computes his depreciation limits for those years as follows:

\$4,250 (\$5,000 × 85%) in 1998,

\$2,593 (\$3,050 × 85%) in 1999, and

\$1,509 (\$1,775 × 85%) in 2000 and 2001.

In 2002, Karl's MACRS deduction is \$1,244 [(\$25,400 × 85%) × 5.76%]. Since that amount is less than the depreciation limit of \$1,509 (\$1,775 × 85%), Karl's depreciation deduction for 2002 is \$1,244.

If Karl continues to use his car for business after 2002, he can continue to claim a depreciation deduction for his unrecovered basis. However, he cannot deduct more than \$1,775 multiplied by his business use percentage. See *Deductions in years after the recovery period*, later.

Section 179 deduction. The section 179 deduction is treated as a depreciation deduction. If you place a car in service in 1997, use it only for business, and choose the section 179 deduction, the combined section 179

and depreciation deduction for that car for 1997 is limited to \$3,160.

Example. On September 5, 1997, Jack bought a used car for \$6,000 and placed it in service. He used it 80% for his business and he chooses to take a section 179 deduction for the car.

Before applying the limit, Jack figures his maximum section 179 deduction to be \$4,800. This is the amount of his qualifying property (up to the maximum \$18,000 amount) multiplied by his business use ($\$6,000 \times 80\%$).

Jack then figures that his section 179 deduction for 1997 is limited to \$2,528 (80% of \$3,160). He then has an unadjusted basis of \$2,272 [$(\$6,000 \times 80\%) - \$2,528$] for determining his depreciation deduction. Since he has already reached the maximum limit for 1997, Jack will use the unadjusted basis to figure his depreciation deduction for 1998.

Deductions in years after the recovery period. If the depreciation limits apply to your car, you may have **unrecovered basis** in your car at the end of the recovery period. You can deduct that unrecovered basis after the recovery period ends.

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

How to treat unrecovered basis. If you continue to use your car for business after the recovery period, you can claim a depreciation deduction for each succeeding tax year until you recover your full basis in the car. The maximum amount you can deduct is determined by the date you placed the car in service.

The recovery period. For cars placed in service after 1986, your recovery period is 6 calendar years. For a 5-year recovery period, a part year's depreciation is allowed in the first calendar year, a full year's depreciation is allowed in each of the next 4 calendar years, and the rest of the first year's depreciation is allowed in the 6th calendar year.

Your recovery period is the same whether you use MACRS declining balance or straight line depreciation. Under MACRS, you determine your unrecovered basis in the 7th year after the car was placed in service.

Deduction amount after the recovery period. In years after the recovery period, a deduction for the unrecovered basis is allowed only for the business use of the car. If you use your car less than 100% for business, the depreciation deduction will be less than the maximum amount. For example, no deduction is allowed for a year you use your car 100% for personal purposes.

Example. In May 1991, Bob bought and placed in service a car that he used exclusively in his business. The car cost \$28,600. Bob did not claim a section 179 deduction for the car. He continued to use the car 100% in his business throughout the recovery period (1991 through 1996). For those years, Bob used the MACRS Depreciation Chart and Maximum Limits Table (as explained earlier) to compute his depreciation deductions as shown in the following table.

Year ^y	MACRS %	MACRS Amount	Maximum Limit ^y	Deprec. Allowed ^y
'91	20.0 ^y	\$5,720 ^y	\$2,660 ^y	\$ 2,660 ^y
'92	32.0 ^y	9,152 ^y	4,300 ^y	4,300 ^y
'93	19.2 ^y	5,491 ^y	2,550 ^y	2,550 ^y
'94	11.52 ^y	3,295 ^y	1,575 ^y	1,575 ^y
'95	11.52 ^y	3,295 ^y	1,575 ^y	1,575 ^y
'96	5.76 ^y	1,647 ^y	1,575 ^y	1,575 ^y
Total				\$14,235^y

At the end of 1996, Bob had an unrecovered basis in the car of \$14,365. This was the \$28,600 original basis of his car less the \$14,235 depreciation deductions allowed during the recovery period.

Bob continued to use the car 100% for business in 1997. He can claim a depreciation deduction of \$1,575 for the year. If he continues to use the car 100% for business in 1998 and later years, Bob can deduct the lesser of \$1,575 or his remaining unrecovered basis in those years until his deductions total the \$12,790 unrecovered basis ($\$14,365 - 1,575$ claimed in 1997).

If Bob's business use of the car was less than 100% during any year, his depreciation deduction would be less than the maximum amount allowable for that year. However, in determining his unrecovered basis in the car, he would still reduce his original basis by the maximum amount allowable. Bob's unrecovered basis at the beginning of 1997 would still be \$14,365 in this example. This is true even if his actual depreciation deduction for any year was less than the maximum amount shown.

Car Used 50% or Less for Business

If you use your car 50% or less in a qualified business use (defined earlier under *Depreciation Deduction*), special rules apply. For this purpose, "car" was defined earlier under *Actual Car Expenses*. When figuring your depreciation deduction:

- 1) You cannot take the section 179 deduction, and
- 2) You must figure depreciation using the straight line method over a 5-year period. You must continue to use the straight line method even if your percentage of business use increases to more than 50% in a later year.

Instead of making the computation yourself, you can use column (c) of *Table 3* to find the percentage to use.

Example. On May 21, 1997, Dan bought a car for \$15,000. He used it 40% for his consulting business. Because he did not use the car more than 50% for business, Dan cannot take any section 179 deduction, and he must use the straight line method over a 5-year period to recover the cost of his car.

Dan deducts \$600 in 1997. This is the lesser of:

- 1) $\$600 [(\$15,000 \text{ cost} \times 40\% \text{ business use}) \times 10\% \text{ recovery percentage (from column (c), Table 3)}]$, or
- 2) $\$1,264 (\$3,160 \text{ maximum limit} \times 40\% \text{ business use})$.

Business use drops to 50% or less in a later year. If you use your car more than 50% in a qualified business use in the tax year it is placed in service but not in a later

tax year, special rules apply to the years during the recovery period (6 years). For the year your business use drops to 50% or less and all later years, you must do the following:

- 1) Determine your depreciation for that car using the straight line method over a 5-year recovery period. You determine your depreciation for this tax year and any later tax years as if you had not met the more-than-50%-use test in the year in which it was placed in service.
- 2) Determine and include in your gross income any excess depreciation, discussed later.

Example. In June 1994, you purchased a car for exclusive use in your business. You met the more-than-50%-use test for the first 3 years of the recovery period (1994 through 1996) but failed to meet it in the fourth year (1997). You determine your depreciation for 1997 using 20% (from column (c) of *Table 3*). You also will have to determine and include in your gross income any excess depreciation, discussed next.

Excess depreciation. You must include any excess depreciation in your gross income and add it to your car's adjusted basis for the first tax year in which the car is not used more than 50% in a qualified business use. Use **Form 4797, Sales of Business Property**, to report the excess depreciation in your gross income.

Excess depreciation is:

- 1) The amount of the depreciation deductions allowable for the car (including any section 179 deduction claimed) for tax years in which the car was used more than 50% in a qualified business use, minus
- 2) The amount of the depreciation deductions that would have been allowable for those years if the car **had not** been used more than 50% in a qualified business use for the year it was placed in service.

Example. On June 25, 1994, you bought a car for \$11,000 and placed it in service. You did not claim the section 179 deduction. You used the car exclusively in a qualified business use for 1994, 1995, and 1996. For those years, you used the MACRS chart to figure depreciation deductions totaling \$7,832 (\$2,200 for 1994, \$3,520 for 1995, and \$2,112 for 1996).

During 1997, you used the car 50% for business and 50% for personal purposes. Since you did not meet the more-than-50%-use test, you must include in gross income for 1997 your excess depreciation determined as follows:

Total depreciation claimed:	\$7,832
(MACRS 200% DB method)	
Total depreciation allowable:	
(Straight line method)	
1994—10% of \$11,000	\$1,100
1995—20% of \$11,000	2,200
1996—20% of \$11,000	2,200
Excess depreciation	\$2,332

In 1997, you must include \$2,332 in your gross income using Form 4797. Your adjusted basis for the car is also increased by \$2,332. Your 1997 depreciation deduction is \$1,100 [$\$11,000$ (unadjusted basis) \times 50% (business use percentage) \times 20% (from column (c) of *Table 3*)].

Disposition of a Car

If you dispose of your car, you may have a taxable gain or a deductible loss. The portion of any gain that is due to depreciation (including any section 179 or clean-fuel vehicle deduction) that you claimed on the car will be treated as ordinary income. However, you may not have to recognize a gain or loss if you dispose of the car because of a casualty, theft, or trade-in. For information on how to report the disposition of your car, see Publication 544.

Casualty or theft. For a casualty or theft, a gain results when you receive insurance or other reimbursement that is more than the adjusted basis of your car. If you then spend all of the proceeds to acquire replacement property (a new car or repairs to the old car) within a specified period of time, you do not recognize any gain. The basis of the replacement property is its cost minus any gain that is not recognized. See Publication 547 for more information.

Trade-in. When you trade in an old car for a new one, the transaction is considered a like-kind exchange. Generally, no gain or loss is recognized. (For exceptions, see chapter 1 of Publication 544.) In a trade-in situation, the basis of the new property is generally the adjusted basis of the old property plus any additional amount you pay. (See *Unadjusted basis*, earlier.)

Depreciation adjustment when you used the standard mileage rate. If you used the standard mileage rate for the business use of your car, depreciation was included in that rate. The rate of depreciation that was allowed in the standard mileage rate is shown in the chart that follows. This depreciation reduces the basis of your car (but not below zero) in figuring its adjusted basis when you dispose of it.

TIP *These rates do not apply for any year in which the actual expenses method was used.*

Year(s)	Depreciation Rate per Mile
1994 – 1997	\$.12
1992 – 1993	.11½
1989 – 1991	.11
1988	.10½
1987	.10
1986	.09
1983 – 1985	.08
1982	.07½
1980 – 1981	.07

For tax years before 1990, the depreciation rates apply to the first 15,000 miles. For tax years after 1989, the depreciation rates apply to all business miles.

Example. In 1993, you bought a car for exclusive use in your business. The car cost \$14,000. From 1993 through 1997, you used the standard mileage rate to figure your car expense deduction. You drove your car 18,100 miles in 1993, 16,300 miles in 1994, 17,600 miles in 1995, 18,700 miles in 1996, and 16,900 miles in 1997. The depreciation allowed is figured as follows:

Year	Miles x Rate	Depreciation
1993	18,100 × .11½	\$2,082
1994	16,300 × .12	1,956
1995	17,600 × .12	2,112
1996	18,700 × .12	2,244
1997	16,900 × .12	2,028
Total depreciation		\$10,422

At the end of 1997, your adjusted basis in the car is \$3,578 (\$14,000 – \$10,422).

Depreciation deduction for the year of disposition. If you deduct actual car expenses and you dispose of your car before the end of its recovery period, you are allowed a reduced depreciation deduction for the year of disposition.

To figure the reduced depreciation deduction for a car disposed of in 1997, first determine the depreciation deduction for the full year using Table 3.

If you used a *Date Placed in Service* line for Jan. 1–Sept. 30, you can deduct one-half of the regular depreciation amount for the year of disposition. Figure your depreciation deduction for the full year using the rules explained in this chapter and deduct 50% of that amount with your other actual car expenses.

If you used a *Date Placed in Service* line for Oct. 1–Dec. 31, you can deduct a percentage of the regular depreciation amount that is based on the month you disposed of the car. Figure your depreciation deduction for the full year using the rules explained in this chapter and multiply the result by the percentage from the following table for the month that you disposed of the car.

Month	Percentage
Jan., Feb., March	12.5%
April, May, June	37.5%
July, Aug., Sept.	62.5%
Oct., Nov., Dec.	87.5%



Do not use this table if you are a fiscal year filer. See Dispositions in chapter 3 of Publication 946.

Leasing a Car

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

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

If you lease a car that you use in your business for 30 days or more, you may have to include an "inclusion amount" in your income for each tax year you lease the car. The inclusion amount has the effect of reducing your deduction for your lease payment. For information on reporting inclusion amounts, see *Car rentals* under *Completing Forms 2106 and 2106-EZ* in chapter 6 if you are an employee. See the instructions for Schedule C (Form 1040) if you are a sole proprietor and Schedule F (Form 1040) if you are a farmer.

The **inclusion amount** is a percentage of part of the fair market value of the leased car multiplied by the percentage of business and investment use of the car for the tax year. The inclusion amount is prorated for the number of days of the lease term included in the tax year. The effect of adding this amount to income is to limit your deduction for lease payments so that it equals the depreciation

deduction you would have on the car if you owned it.

Inclusion Amounts

If you lease a car for a lease term of 30 days or more, you may have to include an inclusion amount in your gross income. This applies to each tax year that you lease the car if the fair market value (defined next) of the car when the lease began was more than:

\$12,800 for leases beginning in 1987 through 1990,

\$13,400 for leases beginning in 1991,

\$13,700 for leases beginning in 1992,

\$14,300 for leases beginning in 1993,

\$14,600 for leases beginning in 1994,

\$15,500 for leases beginning in 1995 and 1996, and

\$15,800 for leases beginning in 1997.

Fair market value is the price at which the property would change hands between a buyer and a seller, neither having to buy or sell, and both having reasonable knowledge of all the necessary facts. Sales of similar property around the same date may be helpful in figuring the fair market value of the property.

The fair market value is the value on the first day of the lease term. If the capitalized cost of a car is specified in the lease agreement, that amount is treated as the fair market value.

Figuring the inclusion amount. Use the table in the appropriate Appendix B (depending on the year you first placed the car in service), included at the end of this publication, to determine the inclusion amount if the fair market value of the car is \$100,000 or less. (See the Revenue Procedure(s) identified in the second footnote of the Appendices for the inclusion amount if the fair market value is more than \$100,000. They are available at most IRS offices and many local libraries.) For each tax year during which you lease the car, the inclusion amount is determined as follows:

- 1) Determine the dollar amount from the table as described below,
- 2) Prorate the dollar amount from the table for the number of days of the lease term included in the tax year, and
- 3) Multiply the prorated amount by the percentage of business and investment use for the tax year.

To determine the dollar amount from the table in the appropriate Appendix B, use the fair market value of the car on the first day of the lease term to find the correct line of the table. Use the tax year in which the car is used under the lease to find the correct column of the table. However, for the **last** tax year of the lease, use the dollar amount for the **preceding** year.

Example. On January 17, 1995, you leased a car for 3 years and placed it in service for use in your business. The car had a fair market value of \$29,250 on the first day of the lease term. You use the car 75% for your business and 25% for personal purposes during each year of the lease. Assuming you continue to use the car 75% for business, you use Appendix B-3 to arrive at the following

amounts to include in your gross income for each year of the lease:

Tax year	Dollar amount	Proration	Business use	Inclusion amount
1995	\$ 148	349/365	75%	\$ 106
1996	24	366/366	75%	243
1997	81	365/365	75%	361
1998	81	16/365	75%	16

Leased car changed from business to personal use. If you first lease a car for business use and, in a later year, change it to personal use, follow the rules explained earlier under *Figuring the inclusion amount*. Since this is the last year of the business use of the leased car, use the amount for the preceding year of the lease, and prorate the amount for the number of days in the lease term included in the tax year.

Example. On April 16, 1996, Will leased a car with a fair market value of \$28,600 for 3 years. He used the car exclusively in his own data processing business. On October 7, 1997, Will closed his own business and went to work for a company where he is not required to use a car for business. Will computed his inclusion amount for 1996 and 1997 as shown in the following table.

Tax year	Dollar amount	Proration	Business use	Inclusion amount
1996	\$ 103	260/366	100%	\$ 73
1997	81	279/365	100%	99

Leased car changed from personal to business use. If you first lease a car for personal use and, in a later year, change it to business use, you must determine the car's fair market value on the date of conversion. Then follow the rules explained earlier under *Figuring the inclusion amount*. Use the fair market value on the date of conversion, and the appropriate Appendix B for the year of conversion.

Example. In March 1994, Janice leased a car for 4 years for personal use. On June 1, 1997, she started working as a self-employed advertising consultant. She started using the leased car for business purposes, and her records show that her business use for June 1 through December 31 was 60%. To figure her inclusion amount for 1997, Janice obtained an appraisal from an independent car leasing company that showed the fair market value of her 1994 car on June 1, 1997, was \$18,650. Using *Appendix B-1*, Janice computed her inclusion amount for 1997 as shown in the following table.

Tax year	Dollar amount	Proration	Business use	Inclusion amount
1997	\$ 24	214/365	60%	\$9



By keeping timely and accurate records, you will have support to show the IRS if your tax return is ever examined. Or, you will have proof of expenses that your employer may require if you are reimbursed under an accountable plan. These plans are discussed in chapter 6 under *Reimbursements*.

How To Prove Expenses

This section explains the items you need to prove depending on which expense you are deducting. It also discusses rules for the records you must keep. These rules may apply to more than one type of expense. The topics include:

- A chart showing what is needed to prove expenses,
- A discussion of adequate records,
- How to treat confidential information,
- When you need documentary evidence,
- Duplicate information,
- When to record information,
- When expenses must be kept separate,
- When expenses can be combined,
- What if your records are incomplete, and
- What if your return is examined.

Chart that shows proof needed. You must be able to prove (substantiate) certain elements of expense to deduct travel, entertainment, business gift, and local transportation expenses. *Table 4* summarizes the elements for each expense discussed in this publication. You must be able to prove the elements listed across the top of the chart. You prove them by having the information and receipts (where needed) for the expenses listed in the first column. You cannot deduct amounts that you approximate or estimate.

Adequate records. You should keep adequate records that prove your expenses or have sufficient evidence that will support your own statement. Written evidence has considerably more value than oral evidence alone, and you must generally prepare a written record for it to be considered adequate. However, if you prepare a record in a computer memory device with the aid of a logging program, it is considered an adequate record.

You should keep the proof you need in an account book, diary, statement of expense, or similar record, and keep documentary evidence (such as receipts, canceled checks, or bills) that together will support each element of an expense. A receipt is ordinarily the best evidence to prove the amount of an expense. You cannot deduct amounts that are considered lavish or extravagant.

Confidential information. You do not need to put confidential information relating to an element of a deductible expense (such as the place, business purpose, or business relationship) in your account book, diary, or other record. However, you do have to record the information elsewhere at or near the time of the expense and have it available to fully prove that element of the expense.

Documentary evidence. You generally must have documentary evidence, such as receipts, canceled checks, or bills, to support your expenses. However, this evidence is not needed if any of the following apply:

- 1) You have meals or lodging expenses while traveling away from home for which you account to your employer under an accountable plan and you use a per diem allowance method that includes meals and/or lodging,
- 2) Your expense, other than lodging, is less than \$75, or
- 3) You have a transportation expense for which a receipt is not readily available.

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

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

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

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

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

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

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

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

Proving business purpose. You must generally provide a written statement of the business purpose of an expense. However, the degree of proof varies according to the circumstances in each case. If the business purpose of an expense is clear from the surrounding circumstances, then you do not need to give a written explanation.

Example. If you are a sales representative who calls on customers on an established sales route, you do not have to give a written explanation of the business purpose for traveling that route. You can satisfy the requirements by recording the length of the delivery route once, the date of each trip at or near the time of the trips, and the total miles you drove the car during the tax year. You could also establish the date of each trip with a receipt, record of delivery, or other documentary evidence.

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

5. Recordkeeping

This chapter discusses the records you need to keep if you plan to deduct an expense discussed in this publication.

Table 4. How To Prove Certain Business Expenses

IF you have expenses for:	THEN you must keep records that show details of the following elements.			
	Amount	Time	Place or Description	Business Purpose and Business Relationship
Travel	Cost of each separate expense for travel, lodging, and meals. Incidental expenses may be totaled in reasonable categories such as taxis, daily meals for traveler, etc.	Dates you left and returned for each trip and number of days spent on business.	Destination or area of your travel (name of city, town, or other designation).	<u>Purpose:</u> Business purpose for the expense or the business benefit gained or expected to be gained. <u>Relationship:</u> N/A
Entertainment	Cost of each separate expense. Incidental expenses such as taxis, telephones, etc., may be totaled on a daily basis.	Date of entertainment. (Also see <i>Business Purpose</i> .)	Name and address or location of place of entertainment. Type of entertainment if not otherwise apparent. (Also see <i>Business Purpose</i> .)	<u>Purpose:</u> Business purpose for the expense or the business benefit gained or expected to be gained. For entertainment, the nature of the business discussion or activity. If the entertainment was directly before or after a business discussion: the date, place, nature, and duration of the business discussion, and the identities of the persons who took part in both the business discussion and the entertainment activity. <u>Relationship:</u> Occupations or other information (such as names, titles, or other designations) about the recipients that shows their business relationship to you. For entertainment, you must also prove that you or your employee was present if the entertainment was a business meal.
Gifts	Cost of the gift.	Date of the gift.	Description of the gift.	<u>Purpose:</u> Business purpose for the expense. <u>Relationship:</u> N/A
Transportation (Car)	Cost of each separate expense. For car expenses, the cost of the car and any improvements, the date you started using it for business, the mileage for each business use, and the total miles for the year.	Date of the expense. For car expenses, the date of the use of the car.	Your business destination (name of city, town, or other designation).	<u>Purpose:</u> Business purpose for the expense. <u>Relationship:</u> N/A

Timely recordkeeping. You do not need to write down the elements of every expense at the time of the expense. However, a record of the elements of an expense or of a business use made at or near the time of the expense or use, and supported by sufficient documentary evidence, has more value than a statement prepared later when generally there is a lack of accurate recall.

A log maintained on a weekly basis, which accounts for use during the week, is considered a timely record. An expense account statement you give your employer, client, or customer can also be considered a timely record. This is true if it is copied from your account book, diary, statement of expense, or similar record.

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

Season or series tickets. If you purchase season or series tickets for business use, you must treat each ticket in the series as a separate item. To determine the cost of individual tickets, divide the total cost (but not more than face value) by the number of

games or performances in the series. You must keep records to show whether you use each ticket as a gift or entertainment. Also, you must be able to prove the cost of non-luxury box seat tickets if you rent a skybox or other private luxury box for more than one event. See *Entertainment tickets* in chapter 2.

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

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

Expenses of a similar nature occurring during the course of a single event are considered a single expense. For example, if during entertainment at a cocktail lounge, you pay separately for each serving of

refreshments, the total expense for the refreshments is treated as a single expense.

Car expenses. You can account for several uses of your car that can be considered part of a single use, such as a round trip or uninterrupted business use, by a single record. For example, you may make deliveries at several different locations on a route that begins and ends at your employer's business premises and that may include a stop at the business premises between two deliveries. You can account for these using a single record of miles driven. Minimal personal use, such as a stop for lunch on the way between two business stops, is not an interruption of business use.

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

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

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

If the element is the description of a gift, or the cost, time, place, or date of an expense, there must be direct evidence. This evidence can be a written statement or the oral testimony of your guests or a witness, which gives detailed information about the element or documentary evidence. If the element is either the business relationship of your guests or the business purpose of the amount spent, the evidence can be circumstantial. For example, the nature of your work, such as deliveries, provides circumstantial evidence of your use of your car for business purposes. Invoices of deliveries establish when you used the car for business.

Sampling. You can maintain an adequate record for parts of a tax year and use that record to substantiate the amount of business or investment use for the entire year. You must demonstrate by other evidence that the periods for which an adequate record is kept are representative of the use throughout the tax year.

Example. You use your car for local business transportation to visit the offices of clients, meet with suppliers and other subcontractors, and pick up and deliver items to clients. There is no other business use of the car, but you and other members of your family use the car for personal purposes. You maintain adequate records during the first week of each month that show that 75% of the use of the car is for business. Invoices and bills show that your business use continues at the same rate during the later weeks of each month. Your weekly records are representative of the use of the car each month and are sufficient evidence to support the percentage of business use for the year.

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

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

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

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

If your return is examined. If your return is examined, you may have to provide additional information to the IRS. This information could be needed to clarify or to establish the accuracy or reliability of information contained in your records, statements, testimony, or documentary evidence before a deduction is allowed.

How Long To Keep Records and Receipts

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

You must keep records of the business use of your car for each year of the recovery period. See *More-than-50%-use test* in chapter 4 under *Depreciation Deduction*.

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

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

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

Examples of Records

Examples of records that show the information you need to keep for different types of expenses are included in this publication as *Table 6* and *Table 7*. They are part of the illustrated examples shown at the end of chapter 6.

6.

How To Report

This chapter explains how and where to report the expenses discussed in this publication. It discusses reimbursements, including treatment of accountable and nonaccountable plans, adequate accounting, per diem allowances, and car or mileage allowances. The chapter ends by showing you how to complete Forms 2106 and 2106-EZ.

Where To Report

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

Self-employed. You must report your income and expenses on Schedule C or C-EZ (Form 1040) if you are a sole proprietor, or on Schedule F (Form 1040) if you are a farmer. If you claim car or truck expenses, you must provide certain information on the use of your vehicle. You provide this infor-

mation on Schedule C, Schedule C-EZ, or **Form 4562**. You do not use Form 2106 or Form 2106-EZ.

If you file Schedule C:

- 1) Report your travel expenses, except meals, on line 24a,
- 2) Report your meals (actual cost or standard meal allowance) and entertainment on line 24b (The 50% limit is figured on line 24c.),
- 3) Report your business gift expenses and local business transportation expenses, other than car expenses, on line 27, and
- 4) Report your business car expenses on line 10. Complete Part IV of the form unless you have to file Form 4562 for depreciation or amortization.

If you file Schedule C-EZ, report the total of all business expenses on line 2. You can only include 50% of your business meals and entertainment in that total. If you include business car expenses, you must also complete Part III of the form.

If you file Schedule F:

- 1) Report your business car expenses on line 12. Attach Form 4562 and provide information on the use of your car in Part V, and
- 2) Report all other business expenses discussed in this publication on line 34. You can only include 50% of your business meals and entertainment on that line.

See your forms instructions for more information on how to complete your tax return.

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

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

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

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

Gifts. If you did not receive any reimbursements (or the reimbursements were all included in box 1 of your Form W-2) and the only business expense you are claiming is for business gifts, do not complete Form 2106 or 2106-EZ. Instead, claim the amount of your deductible business gifts directly on line 20 of Schedule A (Form 1040). Otherwise, you must complete Form 2106 or 2106-EZ.

Statutory employees. If you received a Form W-2 and the "Statutory employee" box in box 15 was checked, report your income and expenses related to that income on Schedule C or C-EZ (Form 1040). Do not complete Form 2106 or Form 2106-EZ.

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



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 reimbursement applies.

Reimbursement for personal expenses. If your employer reimburses you for non-deductible personal expenses, such as for vacation trips, your employer must report the reimbursement as wage income (in box 1 of your Form W-2). You cannot deduct personal expenses.

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

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

Vehicle Provided by Your Employer

If your employer provides you with a car, you may be able to deduct the actual expenses of operating that car for business purposes. The amount you can deduct depends on the amount that your employer included in your income and the business and personal miles you drove during the year. You **cannot** use the standard mileage rate for a car that you do not own.

Value reported on Form W-2. Your employer can figure and report either the actual value of your personal use of the car or the value of the car as if you used it entirely for personal purposes (100% income inclusion). Your employer must separately state the amount if 100% of the annual lease value was included in your income. If you are unsure what amount was included in your Form W-2, ask your employer.

Full value included in your income. You can deduct the value of the business use of an employer-provided car if your employer reported 100% of the value of the car in your income. On your 1997 Form W-2, *Wage and Tax Statement*, the amount of the value will be included in box 1, *Wages, tips, other compensation*, and box 12, *Benefits included in box 1*.

To claim your expenses, complete Part II, Sections A and C, of Form 2106. Enter your actual expenses on line 23 of Section C and include the entire value of the employer-provided car on line 25. Complete the rest of the form.

Less than full value included in your income. If less than the full annual lease value of the car was included on your Form W-2, this means that your Form W-2 only includes the value of your personal use of the car. Do not enter this value on your Form 2106; it is not deductible.

If you paid any actual costs (that your employer did not provide or reimburse you for) to operate the car, you can deduct the business portion of those costs. Examples of costs that you may have are gas, oil, and repairs. Complete Part II, Sections A and C, of Form 2106. Enter your actual costs on line 23 of Section C and leave line 25 blank. Complete the rest of the form.

Reimbursements

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

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

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

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

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

- 1) Reimbursing you for your actual expenses, as discussed throughout this publication,
- 2) Reimbursing you for travel expenses:
 - a) Using the meals only allowance (discussed later) to reimburse your meals and incidental expenses and reimbursing you for your actual lodging expenses,
 - b) Using the regular federal per diem rate (discussed later), or
 - c) Using the high-low rate (discussed later),
- 3) Reimbursing you for business use of your car:
 - a) At the standard mileage rate, or
 - b) At a flat rate or stated schedule (This can be paid periodically at a fixed rate, at a cents-per-mile rate, at a variable rate based on a stated schedule, or any combination of these rates.), or

- 4) Reimbursing you under any other method that is acceptable to the IRS.

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

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

Employers. If you are an employer and you reimburse employee business expenses, how you treat this reimbursement on your employee's Form W-2 depends in part on whether you have an accountable plan. Reimbursements treated as paid under an accountable plan, as explained next, are not reported as pay. Reimbursements treated as paid under nonaccountable plans, as explained later, are reported as pay. See Publication 15, *Circular E, Employer's Tax Guide*, for information on employee pay.

Accountable Plans

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

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

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

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

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

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

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

adequately accounted for or returned within a reasonable period of time.

Employee meets accountable plan rules.

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

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

Employee does not meet accountable plan rules. Even though you are reimbursed under an accountable plan, some of your expenses may not meet all three rules.

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

If you receive an allowance or advance that is higher than the federal rate, see *Returning Excess Reimbursements*, later. In this publication, "federal rate" means any of the three per diem allowances or the standard mileage rate.

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

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

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

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

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

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

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

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

However, if your actual expenses (or your expenses using the standard meal allowance) are more than your per diem allowance, you can complete Form 2106 and deduct the excess amount on Schedule A (Form 1040). If you are using actual expenses, you must be able to prove to the IRS the total amount of your expenses and reimbursements for the entire year. If you are using the standard meal allowance, you do not have to prove that amount.

Example 1. In April, Jeremy takes a 2-day business trip to Denver. The federal rate in Denver is \$126 per day. As required by his employer's accountable plan, he accounts for the time (dates), place, and business purpose of the trip. His employer reimburses him \$126 a day (\$252 total) for living expenses. Jeremy's living expenses in Denver are not more than \$126 a day.

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

Example 2. In June, Matt takes a two-day business trip to Boston. Matt's employer uses the high-low method (discussed later) to reimburse employees. Since Boston is a high-cost area, Matt is given an advance of \$166 a day (\$332 total) for his lodging, meals, and incidental expenses. Matt's actual expenses totaled \$390.

Matt is reimbursed under an accountable plan. However, since his \$390 of expenses exceed his \$332 advance, Matt includes the excess expenses when he itemizes his deductions. Matt completes Form 2106 (showing **all** of his expenses and reimbursements). He must also allocate his reimbursement between his meals and other expenses as discussed later under *Completing Forms 2106 and 2106-EZ*.

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

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

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

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

Her employer included the \$12 that was more than the federal rate $[(\$40 - \$34) \times 2]$ in box 1 of Laura's Form W-2. Her employer shows \$68 ($\34×2) in box 13 of her Form W-2. This amount is not included in Laura's income. Laura does not have to complete Form 2106; however, she must include the \$12 in her gross income as wages (by reporting the total amount shown in box 1 of her Form W-2).

Example 2. Joe also lives in Austin and works for the same employer as Laura. In May the employer sent Joe to San Diego for 4 days and paid the hotel directly for Joe's hotel bill. The employer reimbursed Joe \$45 a day for his meals and incidental expenses. The federal rate for San Diego is \$38 a day.

Joe can prove that his actual meal expenses totaled \$290. His employer's accountable plan will not pay more than \$45 a day for travel to San Diego, so Joe does not give his employer the records that prove that he actually spent \$290. However, he does account for the time, place, and business purpose of the trip. This is Joe's only business trip in 1997.

Joe was reimbursed \$180 ($\45×4 days), which is \$28 more than the federal rate of \$152 ($\38×4 days). The employer includes the \$28 as income on Joe's Form W-2 in box 1. The employer also enters \$152 in box 13 of Joe's Form W-2, along with a code L.

Joe completes Form 2106 to figure his deductible expenses. He enters the total of his actual expenses for the year (\$290) on Form 2106. He also enters the reimbursements that were not included in his income (\$152). His total deductible expense, before the 50% limit, is \$138. After he figures the 50% limit on his unreimbursed meals and entertainment, he will include the balance, \$69, as an itemized deduction.

Car or mileage allowances. How you report a car or mileage allowance that you received under an accountable plan depends on whether the reimbursement or your actual expenses were more than the standard mileage rate of 31½ cents a mile for 1997. The standard mileage rate is considered to be the federal rate. If your allowance was equal to or less than 31½ cents a mile, see *Per diem allowance LESS than or EQUAL to the federal rate*, earlier. If your allowance was more than 31½ cents a mile, see *Per diem allowance MORE than the federal rate*, earlier.

Example 1. Nicole drives 10,000 miles a year for business. Under her employer's accountable plan, she accounts for the time (dates), place, and business purpose of each trip. Her employer pays her a mileage allowance of 31½ cents a mile. Nicole's expenses of operating her car are not more than 31½ cents a mile.

Nicole's employer does not include any of the reimbursement on her Form W-2 because the mileage allowance is not more than the standard mileage rate. Nicole does not deduct the expenses on her return because her expenses are not more than the allowance she received.

Example 2. The facts in Matt's case are the same as those in *Example 1*. However, Matt's employer pays him a mileage allowance of only 20 cents a mile.

Matt is reimbursed under an accountable plan. However, since his \$3,150 expenses computed under the standard mileage rate (10,000 miles \times 31½ cents) exceed his \$2,000 reimbursement (10,000 miles \times 20 cents), Matt itemizes his deductions to claim the excess expenses. Matt completes Form 2106 (showing **all** of his expenses and reimbursements) and enters \$1,150 (\$3,150 – \$2,000) as an itemized deduction.

Example 3. The facts in Debbie's case are the same as in *Example 1*, except Debbie gets reimbursed 35 cents a mile, which is 3½ cents a mile more than the standard mileage rate. Her employer must include the reimbursement amount up to the standard mileage rate, \$3,150 (10,000 miles \times 31½ cents), in box 13 (code L) of her Form W-2. That amount is not taxable.

Debbie's employer must also include \$350 (10,000 miles \times 3½ cents) in box 1 of her Form W-2. This is the reimbursement that is more than the standard mileage rate. Because her reimbursement is equal to or more than her expenses, Debbie does not complete Form 2106.

Example 4. Joe's employer advanced him 36 cents a mile for the 10,000 business miles Joe was expected to drive during the year. His total advance was \$300 per month (\$3,600 annually for the 10,000 miles \times 36 cents). However, Joe has records to show that his actual car expenses for the year were \$4,000. His employer's accountable plan will not pay more than 36 cents a mile so Joe only gives his employer enough records each month to prove that he spent \$3,600 (\$300 per month).

On Joe's Form W-2, his employer includes \$450 in box 1 as if it were wages. The \$450 is the amount of the total advance of \$3,600 (10,000 miles \times 36 cents) that is more than \$3,150 (10,000 miles \times 31½ cents), the standard mileage rate. The \$3,150 is shown with a code L in box 13 of Joe's Form W-2.

To claim his excess expenses, Joe completes Form 2106 and reports his total expenses of \$4,000 and his reimbursement of \$3,150 shown in box 13 of his Form W-2. Joe will claim \$850 (\$4,000 – \$3,150) as an itemized deduction.

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

Adequate Accounting

One of the three rules (listed earlier) for a reimbursement or other expense allowance arrangement to qualify as an accountable plan is that you adequately account to your employer for your expenses. You adequately account by giving your employer documentary evidence of your travel, mileage, and other employee business expenses, along with a statement of expense, an account book, a diary, or a similar record in which you entered each expense at or near the time you

had it. Documentary evidence includes receipts, canceled checks, and bills. (See chapter 5.)

You must account for **all** amounts received from your employer during the year as advances, reimbursements, or allowances for travel, entertainment, gifts, business use of your car, or any other expenses. This includes amounts that were charged to your employer by credit card or other method. You must give your employer the same type of records and supporting information that you would have to give to the IRS if the IRS questioned a deduction on your return. You must pay back the amount of any reimbursement or other expense allowance for which you do not adequately account or that exceeds the amount for which you accounted.

Per diem allowance or reimbursement.

You may be able to prove the amount of your expense by using a per diem allowance amount. This is a fixed amount of daily reimbursement that your employer gives you for your lodging, meal, and incidental expenses when you are away from home on business. The term "incidental expenses" is defined in chapter 1 under *Standard Meal Allowance*.

A per diem allowance satisfies the adequate accounting requirements for the amount in question if all four of the following conditions apply.

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

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

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

Proving your expenses with a per diem allowance. If your employer pays for your expenses using a per diem allowance, including a meals only allowance, you can generally use the allowance as proof for the

amount of your expenses. However, the amount of expense that you can prove this way cannot be more than:

- 1) The federal M&IE rate (if you receive only a meal allowance), or
- 2) The regular federal per diem rate or the high-low rate (if you receive a per diem allowance for lodging and meals).

You can only use a per diem allowance for which you make an adequate accounting to your employer to prove the cost of meals and/or lodging reimbursed by your employer's accountable plan. You must still provide other proof of the time, place, and business purpose for each expense.

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

The federal rates for M&IE are the same as those rates discussed under *Standard Meal Allowance* in chapter 1.

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

Under the high-low method, the per diem amount for travel during 1997 is \$166 for certain locations. All other areas have a per diem amount of \$109. Employers can get Publication 1542 that gives the areas eligible for the \$166 per diem amount under the high-low method for all or part of the year.

Prorating the standard meal allowance on partial days of travel. The standard meal allowance is for a full 24-hour day of travel. If you travel for part of a day, such as on the days you depart and return, you must prorate the full-day M&IE rate. You can use either of the following methods to figure the federal M&IE for that day.

- 1) **Method 1:**
 - a) For the day you depart, add ¾ of the standard meal allowance amount for that day.
 - b) For the day you return, add ¾ of the standard meal allowance amount for the preceding day.
- 2) **Method 2:** Prorate the standard meal allowance using any method that you consistently apply and that is in accordance with reasonable business practice. For example, an employer can treat 2 full days of per diem (that includes M&IE) paid for travel away from home from 9 a.m. of one day to 5 p.m. of the next day as being no more than the federal rate. This is true even though a federal employee would be limited to a reimbursement of M&IE for only 1½ days of the federal M&IE rate.

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

Car or mileage allowance amount. You may be able to prove the amount of your expense by using a car or mileage allowance amount. A car or mileage allowance satisfies the adequate accounting requirements for the amount if all three of the following conditions apply.

- 1) Your employer reasonably limits payments of the car expenses to those that are ordinary and necessary in the conduct of the trade or business.
- 2) The allowance is paid at the standard mileage rate, at another rate per mile, or based on a fixed and variable rate (FAVR) allowance (as described later).
- 3) You prove the time (dates), place, and business purpose of using your car to your employer within a reasonable period of time.

However, you have additional recordkeeping requirements if you are related to your employer, as discussed next.

Related to your employer. If you are related to your employer (as defined under *Standard Meal Allowance* in chapter 1), you must be able to prove your expenses to the IRS. This is true even if you have already adequately accounted to your employer and returned any excess reimbursement. (You can still use the standard mileage rate, discussed in chapter 4, or a FAVR allowance, discussed later, to adequately account to your employer and the IRS.)

Proving your expenses with a car or mileage allowance. If your employer pays for your expenses using a car or mileage allowance, you can generally use the allowance as proof for the amount of your expenses. However, the amount of expense that you can prove this way cannot be more than the standard mileage rate or the amount of the FAVR allowance that your employer does **not** include in box 1 of your Form W-2.

You can only use a car or mileage allowance to prove the amount of business car expense. You must still prove the time (dates), place, and business purpose for each expense. The most frequently used methods of figuring a car or mileage allowance are discussed here.

Fixed or variable mileage allowance. You can prove the amount of your expenses if your employer reimburses your car expenses at a fixed rate, at a cents-per-mile rate, or at a variable rate based on a stated schedule. However, the amount you can prove by this method cannot be more than the standard mileage rate.

Fixed and variable rate (FAVR). Your employer may choose to reimburse your car expenses by paying you an allowance that includes a combination of payments covering fixed and variable costs, such as a cents-per-mile rate to cover your variable operating costs (such as gas, oil, etc.) plus a flat amount to cover your fixed costs (such as depreciation, insurance, etc.). This is called a **FAVR allowance**. If your employer chooses to use this method, your employer will request the necessary records from you and will not include any part considered to be paid from an accountable plan in box 1 of your Form W-2. The IRS will consider you to have

proved the amount reimbursed by your employer (up to the amount not included in box 1 of your Form W-2).

Returning Excess Reimbursements

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

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

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

Unproved amounts. If you do not prove that you actually traveled on each day for which you received a per diem or car allowance (proving the elements described in *Table 4*), you must return this unproved amount of the travel advance within a reasonable period of time. If you fail to do this, your employer will include as income in box 1 of your Form W-2 the unproved amount of per diem or car allowance as excess reimbursement. This unproved amount is considered paid under a nonaccountable plan (discussed later).

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

Example. Your employer sends you on a 5-day business trip to Phoenix and gives you a \$225 ($\45×5 days) advance to cover your meals and incidental expenses. The federal per diem for meals and incidental expenses in Phoenix is \$38. Your trip lasts only 3 days. Under your employer's accountable plan, you must return the \$90 ($\45×2 days) advance for the 2 days you did not travel. You do not have to return the \$21 difference between the allowance you received and the federal rate for Phoenix [$(\$45 - \$38) \times 3$ days]. However, the \$21 will be reported on your Form W-2 as wages.

Nonaccountable Plans

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

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

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

An arrangement that repays you for business expenses by reducing the amount reported as your wages, salary, or other pay will be treated as a nonaccountable plan. This is because you are entitled to receive the full amount of your pay whether or not you incurred any business expenses.

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

Your employer will combine the amount of any reimbursement or other expense allowance paid to you under a nonaccountable plan with your wages, salary, or other pay. Your employer will report the total in box 1 of your Form W-2.

You must complete Form 2106 or 2106-EZ and itemize your deductions to deduct your expenses for travel, transportation, meals, or entertainment. Your meal and entertainment expenses will be subject to the 50% limit discussed in chapter 2. Also, your total expenses will be subject to the 2%-of-adjusted-gross-income limit that applies to most miscellaneous itemized deductions.

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

Kim is being reimbursed under a nonaccountable plan. Her employer will include the \$6,000 on Kim's Form W-2 as if it were wages. If Kim wants to deduct her business expenses, she must complete Form 2106 or 2106-EZ and itemize her deductions.

Example 2. Kevin is paid \$2,000 a month by his employer. On days that he travels away from home on business, his employer designates \$50 a day of his salary as paid to reimburse his travel expenses. Because his employer would pay Kevin his monthly salary whether or not he was traveling away from home, the arrangement is a nonaccountable plan. No part of the \$50 a day designated by his employer is treated as paid under an accountable plan.

Rules for Independent Contractors

This section provides rules for independent contractors who incur expenses on behalf of a client or customer. The rules cover the reporting and substantiation of certain expenses discussed in this publication, and they affect both independent contractors and their clients or customers.

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

IF the type of reimbursement (or other expense allowance) arrangement is under:	THEN the employer reports on Form W-2:	AND the employee reports on Form 2106: *
An accountable plan with:		
<i>Actual expense reimbursement:</i> Adequate accounting made <u>and</u> excess returned	No amount.	No amount.
<i>Actual expense reimbursement:</i> Adequate accounting and return of excess both required <u>but</u> excess not returned	The excess amount as wages in box 1.	No amount.
<i>Per diem or mileage allowance up to the federal rate:</i> Adequate accounting made <u>and</u> excess returned	No amount.	All expenses and reimbursements only if excess expenses are claimed. Otherwise, form is not filed.
<i>Per diem or mileage allowance up to the federal rate:</i> Adequate accounting and return of excess both required <u>but</u> excess not returned	The excess amount as wages in box 1. The amount up to the federal rate is reported only in box 13—it is not reported in box 1.	No amount.
<i>Per diem or mileage allowance exceeds the federal rate:</i> Adequate accounting up to the federal rate only <u>and</u> excess not returned.	The excess amount as wages in box 1. The amount up to the federal rate is reported only in box 13—it is not reported in box 1.	All expenses (and reimbursements reported on Form W-2, box 13) only if expenses in excess of the federal rate are claimed. Otherwise, form is not filed.
A nonaccountable plan with:		
Either adequate accounting or return of excess, or both, not required by plan	The entire amount as wages in box 1.	All expenses.
No reimbursement plan:	The entire amount as wages in box 1.	All expenses.

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

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

Accounting to Your Client

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

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

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

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

Required Records for Clients or Customers

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

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

Contractor adequately accounts. If the contractor does adequately account to you for entertainment expenses, you (the client or customer) must keep records documenting each element of the expense, as explained in chapter 5. Use your records as proof for a

deduction on your tax return. If entertainment expenses are accounted for separately, you are subject to the 50% limit on entertainment. You do not, however, have to file an information return to report amounts for which you reimbursed the contractor, as long as he or she adequately accounted to you for these expenses.

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

Completing Forms 2106 and 2106-EZ

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



CAUTION If you are self-employed, do not file Form 2106 or 2106-EZ. Report your expenses on Schedule C, Schedule C-EZ, or on Schedule F (Form 1040). See the instructions for the form that you must file.

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

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

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

Information on use of cars. If you claim any deduction for the business use of a car, you must answer certain questions and provide information about the use of the car. The information relates to the following items:

- 1) Mileage (total, business, commuting, and other personal mileage),
- 2) Percentage of business use,
- 3) Date placed in service,
- 4) Use of other vehicles,
- 5) After-work use,

- 6) Whether you have evidence to support the deduction, and
- 7) Whether or not the evidence is written.

Employees must complete Section A, Part II, Form 2106, or Part III, Form 2106-EZ, to provide this information.

Standard mileage rate. If you claim a deduction based on the standard mileage rate instead of your actual expenses, you must complete Section B, Part II, Form 2106. The amount on line 22 (Section B) is carried to line 1, Part I, Form 2106. In addition, on line 2, Part I, Form 2106, you can deduct parking fees and tolls that apply to the business use of the car. If you file Form 2106-EZ, complete line 1 for the standard mileage rate and line 2 for parking fees and tolls. See *Standard Mileage Rate* in chapter 4 for information on using this rate.

Actual expenses. If you claim a deduction based on actual expenses, you cannot use Form 2106-EZ. You must complete Section C, Part II, Form 2106. In addition, you must complete Section D to show your depreciation deduction and any section 179 deduction you can claim.

If you are still using a car that is fully depreciated, continue to complete Section C. Since you have no depreciation deduction, enter zero on line 28. In this case, you do not complete Section D.

Car rentals. If you claim car rental expenses on line 24a of Form 2106, you may have to include an inclusion amount in your gross income as described in chapter 4. If so, you can show your car expenses and any inclusion amount as follows:

- 1) Compute the inclusion amount **without** taking into account your business use percentage for the tax year,
- 2) Report the inclusion amount from (1) above on line 24b, Part II, Form 2106, and
- 3) Report on line 24c the **net** amount of car rental expenses (total car rental expenses minus the inclusion amount computed in (1) above).

The net amount of car rental expenses will be adjusted on line 27, Part II, of Form 2106, to reflect the percentage of business use for the tax year.

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

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

TIP *If line 4 expenses are the only ones you are claiming and you received no reimbursements (or the reimbursements were all included in box 1 of your Form*

W-2), do not complete Form 2106 or 2106-EZ. Instead, claim these amounts directly on line 20 of Schedule A (Form 1040). List the type and amount of each expense on the dotted lines next to line 20 and include the total on line 20.

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

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

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

Allocating your reimbursement. If you were reimbursed under an accountable plan and want to deduct excess expenses that were not reimbursed, you may have to allocate your reimbursement. This is necessary when your employer does both of the following:

- 1) Pays you a single amount that covers meals and/or entertainment, as well as other business expenses, and
- 2) Does not clearly identify how much is for deductible meals and/or entertainment.

You must allocate that single payment so that you know how much to enter in Column A and Column B of line 7 of Form 2106.

Example. Rob's employer paid him an expense allowance of \$5,000 this year under an accountable plan. The \$5,000 payment consisted of \$2,000 for airfare and \$3,000 for entertainment and car expenses. The employer did not clearly show how much of the \$3,000 was for the cost of deductible entertainment. Rob actually spent \$6,500 during the year (\$2,000 for airfare, \$2,000 for entertainment, and \$2,500 for car expenses).

Since the airfare allowance was clearly identified, Rob knows that \$2,000 of the payment goes in Column A of line 7 of Form 2106. To allocate the remaining \$3,000, Rob uses the worksheet from the instructions for Form 2106. His completed worksheet is shown next.

- | | |
|--|-----------|
| 1. Enter the total amount of reimbursements your employer gave you that were not reported to you in box 1 of Form W-2 ... | \$ 0.000y |
| 2. Enter the total amount of your expenses for the periods covered by this reimbursement | y 5.000y |
| 3. Of the amount on line 2, enter your total expense for meals and entertainment | y 0.000y |
| 4. Divide line 3 by line 2. Enter the result as a decimal (to at least two places) | y.44 y |

- | | |
|---|--------|
| 5. Multiply line 1 by line 4. Enter the result here and in Column B, line 7 | y.320y |
| 6. Subtract line 5 from line 1. Enter the result here and in Column A, line 7 | y.680y |

On line 7 of Form 2106, Rob enters \$3,680 (\$2,000 airfare and \$1,680 of the \$3,000) in Column A and \$1,320 (of the \$3,000) in Column B.

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

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

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

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

3. Limit on total itemized deductions. If your adjusted gross income (line 32 of Form 1040) is more than \$121,200 (\$60,600 if you are married filing separately), the total of certain itemized deductions, including employee business expenses, may be limited. See your form instructions for information on how to figure this limit.

Special Rules

This section discusses special rules that apply only to government officials who are paid on a fee basis, performing artists, and disabled employees with impairment-related work expenses.

Officials Paid on a Fee Basis

Certain fee-basis officials can claim their employee business expenses whether or not they itemize their other deductions on Schedule A (Form 1040).

Fee-basis officials are persons who are employed by a state or local government and who are paid in whole or in part on a fee basis. They can deduct their business expenses in performing services in that job as an adjustment to gross income rather than as a miscellaneous itemized deduction.

After you complete Form 2106 or 2106-EZ, include your employee business expenses from line 10 of Form 2106 or line 6 of Form 2106-EZ in the total on line 31 of Form 1040. Write "FBO" and the amount of your employee business expenses on the dotted line next to line 31 of Form 1040.



This special rule is retroactive to 1987, and you can file an amended return on Form 1040X, Amended U.S. Individual Income Tax Return, for any year that is affected by this change. However, you generally must file the amendment within three years from the time you filed the return or within two years from the time you paid the tax, whichever is later.

Expenses of Certain Performing Artists

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

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

Special rules for married persons. If you are married, you must file a joint return unless you lived apart from your spouse at all times during the tax year. If you file a joint return, you must figure requirements (1), (2), and (3) separately for both you and your spouse. However, requirement (4) applies to your and your spouse's combined adjusted gross income.

Where to report. If you meet all of the above requirements, you should first complete Form 2106 or 2106-EZ. Then you include your performing-arts-related expenses from line 10 of Form 2106 or line 6 of Form 2106-EZ in the total on line 31 of Form 1040. Write "QPA" and the amount of your performing-arts-related expenses on the dotted line next to line 31 of Form 1040.

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

Impairment-Related Work Expenses of Disabled Employees

If you are an employee with a physical or mental disability, your impairment-related work expenses are not subject to the 2%-of-adjusted-gross-income limit that applies to most other employee business expenses. After you complete Form 2106 or 2106-EZ, enter your impairment-related work expenses from line 10 of Form 2106 or line 6 of Form 2106-EZ on line 27 of Schedule A (Form 1040), and identify the type and amount of this expense on the dotted line next

to line 27. Enter your employee business expenses that are **unrelated** to your disability from line 10 of Form 2106 or line 6 of Form 2106-EZ on line 20 of Schedule A (Form 1040).

Impairment-related work expenses are your allowable expenses for attendant care at your workplace and other expenses in connection with your workplace that are necessary for you to be able to work.

You are disabled if you have:

- A physical or mental disability (for example, blindness or deafness) that functionally limits your being employed, or
 - A physical or mental impairment (for example, a sight or hearing impairment) that substantially limits one or more of your major life activities, such as performing manual tasks, walking, speaking, breathing, learning, or working.
- You can deduct impairment-related expenses as business expenses if they are:
- Necessary for you to do your work satisfactorily,
 - For goods and services not required or used, other than incidentally, in your personal activities, and
 - Not specifically covered under other income tax laws.

Example. You are blind. You must use a reader to do your work. You use the reader both during your regular working hours at your place of work and outside your regular working hours away from your place of work. The reader's services are only for your work. You can deduct your expenses for the reader as business expenses.

Illustrated Examples

The following examples illustrate the reporting of travel, entertainment, gift, and transportation expenses on Forms 2106 and 2106-EZ. Business use of a car is shown using actual car expenses in *Example 1* and the standard mileage rate in *Example 2*. Sample records that prove some of the claimed expenses are also shown.

Example 1. David Pine purchased a car for \$18,500 (including sales tax) on January 6, 1997. In 1997, he used the car 70% for business purposes. A sample page from David's logbook is illustrated in *Table 6*. He records his business mileage (but not his personal miles) and expenses daily.

David uses **Form 2106** to claim actual car expenses. He completes Section A, Part II, as shown later on his illustrated form. He does not claim the section 179 deduction. He uses the MACRS double declining balance method (200% DB) to determine his depreciation deduction.

His depreciation deduction normally would be \$2,590 [\$18,500 (unadjusted basis) × 70% (business use) × 20% (from *Table 3*)]. However, it is limited in the first year to \$2,212 [\$3,160 (from the *Maximum Depreciation Limits* table shown in chapter 4) × 70%]. He enters these amounts in Section D, Part II.

His other car expenses included \$3,080 for gas, oil, repairs, and insurance. He enters this amount in Section C, Part II, and multiplies it by the 70% business use. He adds this amount (\$2,156) to the depreciation deduction (\$2,212) and reports the total (\$4,368) on line 1, Part I.

His other transportation expenses for parking fees, tolls, and taxis were \$1,190. He enters this amount on line 2, Part I. David's employer reimbursed him a total of \$2,940 for his car and transportation expenses. This amount was paid from an accountable plan and was not shown on David's Form W-2. However, since he is claiming expenses that are more than his reimbursements, he must show the entire reimbursement amount on line 7, Part I. Since David had no meal or entertainment expenses, he enters his excess deductible expenses (\$2,618) on line 10, Part I. He can deduct these expenses (subject to the 2%-of-adjusted-gross-income limit) on line 20 of Schedule A (Form 1040) if he itemizes his deductions.

Example 2. Bill Wilson is an employee of Fashion Clothing Co. in Manhattan, NY. In a typical week, Bill leaves his home on Long Island on Monday morning and drives to Albany to exhibit the Fashion line for 3 days to prospective customers. Then he drives to Troy to show Fashion's new line of merchandise to Town Department Store, an old customer. While in Troy, he talks with Tom Brown, purchasing agent for Town Department Store, to discuss the new line. He later takes John Smith of Attire Co. out to dinner to discuss Attire Co.'s buying Fashion's new line of clothing.

Bill purchased his car on January 3, 1995. He uses the standard mileage rate for car expense purposes. He records his total mileage, business mileage, parking fees, and tolls for the year. Bill records his expenses and other pertinent information in his *Weekly Traveling Expense and Entertainment Record*, shown in *Table 7*. He obtains receipts for his expenses for lodging and for any other expenses of \$75 or more.

During the year, Bill drove a total of 25,000 miles of which 20,000 miles were for business. Following the instructions for Part II of Form 2106, he answers all the questions and figures his car expense to be \$6,300 (20,000 business miles × 31½ cents standard mileage rate).

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

Type of Expense	Amount
Parking fees and tolls	\$ 325
Car expenses	6,300
Meals	2,632
Lodging, laundry, dry cleaning	8,975
Entertainment	1,870
Gifts, education, etc.	430
Total	\$20,532

Bill received an allowance of \$3,600 (\$300 per month) to help offset his expenses. Bill did not have to account to his employer for the reimbursement and the \$3,600 was included as income in box 1 of his Form W-2.

Because Bill's reimbursement was included in his income and he is using the standard mileage rate for his car expenses, he files Form 2106-EZ with his tax return.

Table 6. Daily Business Mileage and Expense Log

Name: *David Pine*

Date	Destination (City, Town, or Area)	Business Purpose	Odometer Readings			Expenses	
			Start	Stop	Miles this trip	Type (Gas, oil, tolls, etc.)	Amount
6/1/97							
6/2/97	Local (St. Louis)	Sales calls	8,097	8,188	91	Gas	\$ 18.25
6/3/97	Indianapolis	Sales calls	8,211	8,486	275	Parking	2.00
6/4/97	Louisville	See Bob Smith (Pot. Client)	8,486	8,599	113	Gas/Repair flat tire	16.50 8.00
6/5/97	Return to St. Louis		8,599	8,875	276	Gas	17.25
6/6/97	Local (St. Louis)	Sales calls	8,914	9,005	91		
6/7/97							
	Weekly Total		8,097	9,005	846		\$ 62.00
	Total Year-to-Date				6,236		\$993.00

▶ See separate instructions.

▶ Attach to Form 1040.

Your name David Pine	Social security number 559 : 00 : 9559	Occupation in which you incurred expenses Sales
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Part I Employee Business Expenses and Reimbursements

	Column A Other Than Meals and Entertainment		Column B Meals and Entertainment	
STEP 1 Enter Your Expenses				
1 Vehicle expense from line 22 or line 29	1	4,368		
2 Parking fees, tolls, and transportation, including train, bus, etc., that did not involve overnight travel or commuting to and from work	2	1,190		
3 Travel expense while away from home overnight, including lodging, airplane, car rental, etc. Do not include meals and entertainment	3			
4 Business expenses not included on lines 1 through 3. Do not include meals and entertainment	4			
5 Meals and entertainment expenses (see instructions).	5			
6 Total expenses. In Column A, add lines 1 through 4 and enter the result. In Column B, enter the amount from line 5	6	5,558		

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

STEP 2 Enter Reimbursements Received From Your Employer for Expenses Listed in STEP 1

7 Enter reimbursements received from your employer that were not reported to you in box 1 of Form W-2. Include any reimbursements reported under code "L" in box 13 of your Form W-2 (see instructions)	7	2,940		
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STEP 3 Figure Expenses To Deduct on Schedule A (Form 1040)

8 Subtract line 7 from line 6	8	2,618		
Note: If both columns of line 8 are zero, stop here. If Column A is less than zero, report the amount as income on Form 1040, line 7.				
9 In Column A, enter the amount from line 8. In Column B, multiply the amount on line 8 by 50% (.50). If either column is zero or less, enter -0- in that column	9	2,618		
10 Add the amounts on line 9 of both columns and enter the total here. Also, enter the total on Schedule A (Form 1040), line 20. (Fee-basis state or local government officials, qualified performing artists, and individuals with disabilities: See the instructions for special rules on where to enter the total.) ▶	10		2,618	

For Paperwork Reduction Act Notice, see instructions.

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Form **2106** (1997)

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

Section A—General Information		(a) Vehicle 1	(b) Vehicle 2
11	Enter the date vehicle was placed in service	11 1 / 6 / 97	/ /
12	Total miles vehicle was driven during 1997	12 20,000 miles	miles
13	Business miles included on line 12	13 14,000 miles	miles
14	Percent of business use. Divide line 13 by line 12	14 70 %	%
15	Average daily round trip commuting distance	15 10 miles	miles
16	Commuting miles included on line 12	16 2,400 miles	miles
17	Other miles. Add lines 13 and 16 and subtract the total from line 12	17 3,600 miles	miles
18	Do you (or your spouse) have another vehicle available for personal purposes?	<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No	
19	If your employer provided you with a vehicle, is personal use during off-duty hours permitted? <input type="checkbox"/> Yes <input type="checkbox"/> No <input checked="" type="checkbox"/> Not applicable		
20	Do you have evidence to support your deduction?	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No	
21	If "Yes," is the evidence written?	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No	

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

22	Multiply line 13 by 31½¢ (.315). Enter the result here and on line 1. (Rural mail carriers, see instructions.)	22	
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Section C—Actual Expenses		(a) Vehicle 1		(b) Vehicle 2	
23	Gasoline, oil, repairs, vehicle insurance, etc.	23	3,080		
24a	Vehicle rentals	24a			
b	Inclusion amount (see instructions)	24b			
c	Subtract line 24b from line 24a	24c			
25	Value of employer-provided vehicle (applies only if 100% of annual lease value was included on Form W-2—see instructions)	25			
26	Add lines 23, 24c, and 25	26	3,080		
27	Multiply line 26 by the percentage on line 14	27	2,156		
28	Depreciation. Enter amount from line 38 below	28	2,212		
29	Add lines 27 and 28. Enter total here and on line 1	29	4,368		

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

		(a) Vehicle 1		(b) Vehicle 2	
30	Enter cost or other basis (see instructions)	30	18,500		
31	Enter amount of section 179 deduction (see instructions)	31			
32	Multiply line 30 by line 14 (see instructions if you elected the section 179 deduction)	32	12,950		
33	Enter depreciation method and percentage (see instructions)	33	200DB 20%		
34	Multiply line 32 by the percentage on line 33 (see instructions)	34	2,590		
35	Add lines 31 and 34	35	2,590		
36	Enter the limit from the table in the line 36 instructions	36	3,160		
37	Multiply line 36 by the percentage on line 14	37	2,212		
38	Enter the smaller of line 35 or line 37. Also, enter this amount on line 28 above	38	2,212		

THIS IS NOT AN OFFICIAL INTERNAL REVENUE FORM

Table 7. Weekly Traveling Expense and Entertainment Record

From: August 3, 1997

To: August 9, 1997

Name: Bill Wilson

Expenses	Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday	Total
1. Travel Expenses:								
Airlines								
Excess baggage								
Bus - Train								
Cab and Limousine								
Tips								
Porter								
2. Meals and Lodging:								
Breakfast			6 75	6 00	5 25	7 00		25 00
Lunch		9 75	10 00	9 25	8 25	8 50		45 75
Dinner		22 00	18 25	17 50				57 75
Hotel and Motel (Detail in Schedule B)		50 00	50 00	50 00	45 00			195 00
3. Entertainment (Detail in Schedule C)					50 00			50 00
4. Other Expenses:								
Postage								
Telephone & Telegraph		1 50				1 00		2 50
Stationery & Printing								
Stenographer								
Sample Room			15 00	15 00				30 00
Advertising								
Assistant(s) & Model(s)			20 00	20 00				40 00
Trade Shows								
5. Car Expenses: (List all car expenses - the division between business and personal expenses may be made at the end of the year.) (Detail mileage in Schedule A.)								
Gas, oil, lube, wash								
Repairs, parts								
Tires, supplies								
Parking fees, tolls		4 00			3 00	3 00		10 00
6. Other (Identify)								
Total		87 25	120 00	117 75	111 50	19 50		456 00
Note: Attach receipted bills for (1) ALL lodging and (2) any other expenses of \$75.00 or more.								
Schedule A - Car								
Mileage: End		57,600	57,620	57,650	57,660	57,840		
Start		57,445	57,600	57,620	57,650	57,660		
Total		155	20	30	10	180		395
Business Mileage		155	20	30	10	170		385
Schedule B - Lodging								
Hotel or Motel	Name	Bay Hotel	Bay Hotel	Bay Hotel	Modern Hotel			
	City	Albany	Albany	Albany	Troy			
Schedule C - Entertainment								
Date	Item	Place	Amount	Business Purpose	Business Relationship			
August 9, 1997	Bar	John's Steak House	15 00	Discuss purchases	Smith-Attire Co.			
	Dinner	Troy	35 00					

WEEKLY REIMBURSEMENTS:
 Travel and transportation expenses N/A
 Other reimbursements _____
 TOTAL _____

Unreimbursed Employee Business Expenses

1997

Attachment
Sequence No. **54A**

Department of the Treasury
Internal Revenue Service

▶ **Attach to Form 1040.**

Your name <p style="text-align: center;">Bill Wilson</p>	Social security number <p style="text-align: center;">555 : 00 : 5555</p>	Occupation in which you incurred expenses <p style="text-align: center;">Sales</p>
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Part I General Information

You May Use This Form ONLY if All of the Following Apply:

- You are an employee deducting expenses attributable to your job.
- You **do not** get reimbursed by your employer for any expenses (amounts your employer included in box 1 of your Form W-2 are not considered reimbursements).
- If you are claiming vehicle expense,
 - a You own your vehicle, and
 - b You are using the standard mileage rate for 1997 **and** also used it for the year you first placed the vehicle in service.

Part II Figure Your Expenses

1 Vehicle expense using the standard mileage rate. Complete Part III and multiply line 8a by 31½¢ (.315)	1	6,300	
2 Parking fees, tolls, and transportation, including train, bus, etc., that did not involve overnight travel or commuting to and from work	2	325	
3 Travel expense while away from home overnight, including lodging, airplane, car rental, etc. Do not include meals and entertainment	3	8,975	
4 Business expenses not included on lines 1 through 3. Do not include meals and entertainment	4	430	
5 Meals and entertainment expenses: \$ <u>4,502</u> x 50% (.50)	5	2,251	
6 Total expenses. Add lines 1 through 5. Enter here and on line 20 of Schedule A (Form 1040) . (Fee-basis state or local government officials, qualified performing artists, and individuals with disabilities: See the instructions for special rules on where to enter this amount.)	6	18,281	

Part III Information on Your Vehicle. Complete this part ONLY if you are claiming vehicle expense on line 1.

- 7 When did you place your vehicle in service for business purposes? (month, day, year) ▶ 1 / 3 / 95
- 8 Of the total number of miles you drove your vehicle during 1997, enter the number of miles you used your vehicle for:
- a Business 20,000 b Commuting 2,600 c Other 2,400
- 9 Do you (or your spouse) have another vehicle available for personal use? **Yes** **No**
- 10 Was your vehicle available for use during off-duty hours? **Yes** **No**
- 11a Do you have evidence to support your deduction? **Yes** **No**
- b If "Yes," is the evidence written? **Yes** **No**

7.

How To Get More Information

You can get help from the IRS in several ways.

Free publications and forms. To order free publications and forms, call 1-800-TAX-FORM (1-800-829-3676). You can also write to the IRS Forms Distribution Center nearest you. Check your income tax

package for the address. Your local library or post office also may have the items you need.

For a list of free tax publications, order Publication 910, *Guide to Free Tax Services*. It also contains an index of tax topics and related publications and describes other free tax information services available from IRS, including tax education and assistance programs.

If you have access to a personal computer and modem, you also can get many forms and publications electronically. See *Quick and Easy Access to Tax Help and Forms* in your income tax package for details.

Tax questions. You can call the IRS with your tax questions. Check your income tax package or telephone book for the local number, or you can call 1-800-829-1040.

TTY/TDD equipment. If you have access to TTY/TDD equipment, you can call 1-800-829-4059 to ask tax questions or to order forms and publications. See your income tax package for the hours of operation.

Appendices

There are two appendices at the end of this publication.

Appendix A shows the standard meal allowance rates you can use for travel away from home in 1997. (See chapter 1.)

Appendices B-1 through B-6 show the lease inclusion amounts that you may need to include in income if you lease a car for 30 days or more. If this applies to you, use the Appendix for the year you first leased the car. (See chapter 4.)

Appendix A. Locations Eligible for Higher Standard Meal Allowance

KEY CITY ¹	COUNTY/LOCATION ^{2,3}	AMOUNT	KEY CITY ¹	COUNTY/LOCATION ^{2,3}	AMOUNT
ALABAMA			FLORIDA		
Birmingham	Jefferson	\$ 38	Altamonte Springs	Seminole	\$ 34
Gulf Shores	Baldwin	34	Cocoa Beach	Brevard	34
Huntsville	Madison	34	Daytona Beach	Volusia	34
Mobile	Mobile	38	Fort Lauderdale	Broward	34
ARIZONA			Fort Myers	Lee	34
Flagstaff	Coconino	34	Gainesville	Alachua	34
Grand Canyon	Coconino	38	Gulf Breeze	Santa Rosa	34
Nat'l Park/Kaibab			Key West	Monroe	42
Nat'l Forest			Miami	Dade	42
Phoenix/Scottsdale	Maricopa	38	Naples	Collier	38
Prescott	Yavapai	34	Orlando	Orange	34
Tucson	Pima; Davis-Monthan AFB	34	Pensacola	Escambia	34
CALIFORNIA			Punta Gorda	Charlotte	34
Clearlake	Lake	34	Saint Augustine	Saint Johns	34
Death Valley	Inyo	42	Sarasota	Sarasota	34
Eureka	Humboldt	34	Stuart	Martin	34
Fresno	Fresno	34	Tallahassee	Leon	34
Gualala/Point Arena	Mendocino	42	Tampa/St. Petersburg	Hillsborough, Pinellas	38
Los Angeles	Los Angeles, Kern, Orange & Ventura; Edwards AFB; China Lake Naval Center	42	West Palm Beach	Palm Beach	38
Mammoth Lakes/ Bridgeport	Mono	42	GEORGIA		
Merced	Merced	34	Athens	Clarke	34
Modesto	Stanislaus	34	Atlanta	Clayton, Cobb, De Kalb Fulton, Gwinnett	38
Monterey	Monterey	38	Savannah	Chatham	34
Napa	Napa	42	IDAHO		
Oakland	Alameda, Contra Costa, Marin	34	Boise	Ada	34
Ontario/Barstow/ Victorville	San Bernardino	38	Coeur d'Alene	Kootenai	34
Palm Springs	Riverside	38	Idaho Falls	Bonneville	34
Palo Alto/San Jose	Santa Clara	42	Ketchum/Sun Valley	Blaine	38
Redding	Shasta	34	McCall	Valley	34
Sacramento	Sacramento	38	Stanley	Custer	34
San Diego	San Diego	38	ILLINOIS		
San Francisco	San Francisco	42	Champaign/Urbana	Champaign	34
San Luis Obispo	San Luis Obispo	38	Chicago	DuPage, Cook, Lake	42
San Mateo/Redwood City	San Mateo	38	Peoria	Peoria	34
Santa Barbara	Santa Barbara	34	Rockford	Winnebago	38
Santa Cruz	Santa Cruz	38	INDIANA		
Santa Rosa	Sonoma	38	Bloomington/Crane	Monroe, Martin	34
South Lake Tahoe	El Dorado	38	Carmel	Hamilton	38
Stockton	San Joaquin	34	Evansville	Vanderburgh	34
Tahoe City	Placer	38	Indianapolis	Marion; Fort Benjamin Harrison	38
Visalia	Tulare	38	Lafayette	Tippecanoe	34
Yosemite Nat'l Park	Mariposa	42	IOWA		
COLORADO			Cedar Rapids	Linn	34
Aspen	Pitkin	42	KANSAS		
Boulder	Boulder	38	Kansas City	Johnson, Wyandotte	42
Denver	Denver, Adams, Arapahoe, Jefferson	34	Wichita	Sedgwick	34
Durango	La Plata	34	KENTUCKY		
Glenwood Springs	Garfield	34	Covington	Kenton	34
Keystone/Silverthorne	Summit	42	Lexington	Fayette	34
Steamboat Springs	Routt	34	Louisville	Jefferson	38
Telluride	San Miguel	38	LOUISIANA		
Vail	Eagle	42	Baton Rouge	East Baton Rouge	34
CONNECTICUT			New Orleans	Jefferson, Orleans, Plaquemines, St. Bernard	42
Bridgeport/Danbury	Fairfield	38	Shreveport	Caddo	34
New London/Groton	New London	34	MAINE		
Salisbury/Lakeville	Litchfield	34	Bar Harbor	Hancock	34
DELAWARE			Kennebunk/Sanford	York	34
Dover	Kent	34	Kittery	Portsmouth Naval Shipyard	34
Lewes	Sussex	38	Portland	Cumberland	38
Wilmington	New Castle	38	Rockport	Knox	34
DISTRICT of COLUMBIA					
Washington, DC	Virginia counties of Arlington, Loudoun, and Fairfax AND the cities of Alexandria, Fairfax, and Falls Church Maryland counties of Prince George's and Montgomery	42			

Appendix A. (Continued)

KEY CITY ¹	COUNTY/LOCATION ^{2,3}	AMOUNT	KEY CITY ¹	COUNTY/LOCATION ^{2,3}	AMOUNT
MARYLAND (See also District of Columbia)			NEW JERSEY (<i>cont'd</i>)		
Annapolis	Anne Arundel	\$ 38	Parsippany/Dover	Morris; Picatinny Arsenal	\$ 38
Baltimore	Baltimore, Harford	38	Princeton/Trenton	Mercer	38
Columbia	Howard	42	Tom's River	Ocean	34
Frederick	Frederick	38	NEW MEXICO		
Grasonville	Queen Annes	34	Albuquerque	Bernalillo	34
Lexington Park/St.Inigoes/ Leonardtown	Saint Marys	34	Farmington	San Juan	34
Lusby	Calvert	34	Los Alamos	Los Alamos	34
Ocean City	Worcester	42	Sante Fe	Sante Fe	42
Saint Michaels	Talbot	38	Taos	Taos	34
Salisbury	Wicomico	34	NEW YORK		
MASSACHUSETTS			Albany	Albany	38
Andover	Essex	38	Batavia	Genesee	34
Boston	Suffolk	42	Binghamton	Broome	34
Cambridge/Lowell	Middlesex	34	Buffalo	Erie	38
Hyannis	Barnstable	38	Corning	Steuben	34
Martha's Vineyard/ Nantucket	Dukes, Nantucket	42	Glens Falls	Warren	38
Pittsfield	Berkshire	34	Kingston	Ulster	34
Quincy	Norfolk	34	Lake Placid	Essex	34
MICHIGAN			Monticello	Sullivan	34
Detroit	Wayne	38	New York City	Manhattan, Staten Island Bronx, Brooklyn, Queens; Nassau, Suffolk	42
Gaylord	Otsego	34	Niagara Falls	Niagara	34
Grand Rapids	Kent	34	Palisades/Nyack	Rockland	34
Mackinac Island	Mackinac	38	Plattsburgh	Clinton	34
Petosky	Emmet	34	Rochester	Monroe	42
Pontiac/Troy	Oakland	38	Saratoga Springs	Saratoga	38
Port Huron	St. Clair	38	Schenectady	Schenectady	34
Sault Ste Marie	Chippewa	34	Syracuse	Onondaga	34
St. Joseph/Niles/ Benton Harbor	Berrien	34	Utica	Oneida	34
Traverse City	Grand Traverse	34	White Plains	Westchester	42
MINNESOTA			NORTH CAROLINA		
Duluth	St. Louis	38	Asheville	Buncombe	34
Minneapolis/St. Paul	Anoka, Dakota, Hennepin, Ramsey; Detachment BRAVO at Fort Snelling, Rosemount	38	Charlotte	Mecklenburg	38
MISSISSIPPI			Duck/Outer Banks	Dare	34
Biloxi/Bay St. Louis/ Gulfport/Pascagoula	Harrison, Jackson, Hancock	34	Greensboro/High Point	Guilford	34
Jackson	Hinds	34	Raleigh/Chapel Hill/ Durham/Research Park	Wake, Durham, Orange	38
Ridgeland	Madison	34	Winston-Salem	Forsyth	34
MISSOURI			OHIO		
Kansas City	Clay, Jackson, Platte	42	Akron	Summit	34
Lake Ozark	Miller	34	Cincinnati/Evendale	Hamilton, Warren	34
Osage Beach	Camden	34	Cleveland	Cuyahoga	38
Springfield	Greene	34	Columbus	Franklin	34
St. Louis	St. Charles, St. Louis	42	Springfield	Clark	34
NEBRASKA			Toledo	Lucas	34
Omaha	Douglas	34	OREGON		
NEVADA			Ashland/Medford	Jackson	38
Incline Village		38	Beaverton	Washington	38
Las Vegas	Clark; Nellis AFB	38	Crater Lake/Klamath Falls	Klamath	38
Reno	Washoe	34	Eugene/Florence	Lane	34
Stateline	Douglas	38	Lincoln City/Newport	Lincoln	38
NEW HAMPSHIRE			Portland	Multnomah	38
Conway	Carroll	34	PENNSYLVANIA		
Hanover	Grafton; Sullivan	38	Allentown	Lehigh	34
Portsmouth/Newington	Rockingham; Pease AFB	34	Chester/Radnor	Delaware	42
NEW JERSEY			Gettysburg	Adams	34
Atlantic City	Atlantic	38	Harrisburg	Dauphin	34
Belle Mead	Somerset	34	King of Prussia/ Ft. Washington	Montgomery	38
Camden/Moorestown	Camden; Burlington	38	Lancaster	Lancaster	34
Edison	Middlesex	38	Philadelphia	Philadelphia	38
Flemington	Hunterdon	34	Pittsburgh	Allegheny	38
Freehold/Eatontown	Monmouth; Fort Monmouth	34	Scranton	Lackawanna	34
Millville	Cumberland	34	State College	Centre	34
Newark	Bergen, Essex, Hudson, Passaic, Union	42	Valley Forge/Malvern	Chester	38
			Warminster	Bucks; Naval Air Center	34
			York	York	34
			RHODE ISLAND		
			East Greenwich	Kent; Naval Construction Center in Davisville	34
			Newport/Block Island	Newport; Washington	42
			Providence	Providence	42

Appendix A. (Continued)

KEY CITY ¹	COUNTY/LOCATION ^{2,3}	AMOUNT	KEY CITY ¹	COUNTY/LOCATION ^{2,3}	AMOUNT
SOUTH CAROLINA			WASHINGTON		
Charleston	Charleston, Berkeley	\$ 34	Anacortes/Mt. Vernon/ Whidbey Island	Skagit; Island	\$ 34
Greenville	Greenville	38	Bellingham	Whatcom	34
Hilton Head	Beaufort	34	Friday Harbor	San Juan	38
Myrtle Beach	Horry; Myrtle Beach AFB	34	Kelso/Longview	Cowlitz	34
TENNESSEE			Lynnwood/Everett	Snohomish	34
Gatlinburg	Sevier	34	Ocean Shores	Grays Harbor	34
Knoxville	Knox; city of Oak Ridge	34	Port Angeles	Clallam	34
Nashville	Davidson	38	Seattle	King	38
TEXAS			Spokane	Spokane	38
Austin	Travis	34	Vancouver	Clark	34
Dallas/Fort Worth	Dallas, Tarrant	42	WEST VIRGINIA		
El Paso	El Paso	34	Wheeling	Ohio	34
Galveston	Galveston	42	WISCONSIN		
Houston	Harris; LBJ Space Center; Ellington AFB	38	Brookfield	Waukesha	38
Lubbock	Lubbock	34	Eau Claire	Eau Claire	34
Plano	Collin	34	La Crosse	La Crosse	34
San Antonio	Bexar	34	Lake Geneva	Walworth	34
UTAH			Madison	Dane	34
Bullfrog	Garfield	34	Milwaukee	Milwaukee	34
Park City	Summit	42	Oshkosh	Winnebago	34
Provo	Utah	34	Racine/Kenosha	Racine, Kenosha	34
Salt Lake City/Ogden	Salt Lake, Weber, Davis; Dugway Proving Ground; Tooele Army Depot	38	Wisconsin Dells	Columbia	38
St. George	Washington	34	WYOMING		
VERMONT			Jackson	Teton	42
Burlington	Chittenden	34			
Manchester	Bennington	34			
Middlebury	Addison	34			
VIRGINIA (See also District of Columbia)					
Charlottesville		42			
Lynchburg		34			
Norfolk/Virginia Beach/ Portsmouth/Chesapeake	Virginia Beach	34			
Richmond	Chesterfield, Henrico; Defense Supply Center	38			
Roanoke	Roanoke	34			
Williamsburg/Hampton/ Newport News	Williamsburg, York; Naval Weapons Station, Yorktown	34			
Wintergreen	Nelson	42			

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

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

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

Appendix B-1. Inclusion Amounts for Cars First Leased in 1997

Fair Market Value		Tax Year of Lease ¹				
Over	Not Over	1st	2nd	3rd	4th	5th and Later
\$ 15,800	\$ 16,100	\$ 1	\$ 5	\$ 5	\$ 8	\$ 10
16,100	16,400	4	10	13	18	21
16,400	16,700	6	15	22	27	32
16,700	17,000	9	20	30	36	44
17,000	17,500	12	28	40	49	58
17,500	18,000	16	37	53	65	77
18,000	18,500	20	46	66	82	95
18,500	19,000	24	55	80	97	114
19,000	19,500	28	64	93	113	132
19,500	20,000	32	73	106	129	151
20,000	20,500	36	82	120	145	169
20,500	21,000	40	91	133	161	187
21,000	21,500	45	99	147	177	205
21,500	22,000	49	108	160	193	224
22,000	23,000	55	122	180	216	252
23,000	24,000	63	140	206	249	288
24,000	25,000	71	158	233	280	326
25,000	26,000	79	176	259	313	362
26,000	27,000	88	193	287	344	399
27,000	28,000	96	211	313	377	435
28,000	29,000	104	229	340	408	473
29,000	30,000	112	247	366	441	509
30,000	31,000	120	265	393	472	546
31,000	32,000	128	283	420	504	583
32,000	33,000	137	301	446	536	620
33,000	34,000	145	319	472	568	657
34,000	35,000	153	337	499	600	693
35,000	36,000	161	355	526	631	731
36,000	37,000	169	373	552	664	767
37,000	38,000	178	391	578	696	804
38,000	39,000	186	409	605	727	841
39,000	40,000	194	427	632	759	878
40,000	41,000	202	445	658	791	915
41,000	42,000	210	463	685	823	951
42,000	43,000	218	481	712	854	989
43,000	44,000	227	498	739	886	1,026
44,000	45,000	235	516	765	919	1,062
45,000	46,000	243	534	792	951	1,098
46,000	47,000	251	552	819	982	1,136
47,000	48,000	259	570	845	1,015	1,172
48,000	49,000	268	588	871	1,047	1,209
49,000	50,000	276	606	898	1,078	1,246
50,000	51,000	284	624	925	1,110	1,282
51,000	52,000	292	642	951	1,142	1,320
52,000	53,000	300	660	978	1,174	1,356
53,000	54,000	308	678	1,004	1,206	1,394
54,000	55,000	317	695	1,032	1,237	1,430
55,000	56,000	325	713	1,058	1,270	1,467
56,000	57,000	333	732	1,084	1,301	1,504
57,000	58,000	341	750	1,110	1,334	1,540
58,000	59,000	349	768	1,137	1,365	1,578
59,000	60,000	358	785	1,164	1,397	1,615
60,000	62,000	370	812	1,204	1,445	1,670
62,000	64,000	386	848	1,257	1,509	1,743
64,000	66,000	403	884	1,310	1,573	1,817
66,000	68,000	419	920	1,363	1,637	1,890
68,000	70,000	435	956	1,417	1,700	1,964
70,000	72,000	452	991	1,470	1,764	2,038
72,000	74,000	468	1,027	1,524	1,827	2,112
74,000	76,000	484	1,063	1,577	1,891	2,186
76,000	78,000	501	1,099	1,630	1,955	2,259
78,000	80,000	517	1,135	1,683	2,019	2,333
80,000	85,000	546	1,198	1,776	2,130	2,462
85,000	90,000	587	1,287	1,909	2,291	2,645
90,000	95,000	627	1,377	2,042	2,450	2,830
95,000	100,000 ²	668	1,467	2,175	2,609	3,014

¹For the last tax year of the lease, use the amount for the preceding year.

²If the fair market value of the car is more than \$100,000, see Revenue Procedure 97-20 (1997-11 IRB 10).

Appendix B-2. Inclusion Amounts for Cars First Leased in 1996

Fair Market Value		Tax Year of Lease ¹				
Over	Not Over	1st	2nd	3rd	4th	5th and Later
\$ 15,500	\$ 15,800	\$ 3	\$ 6	\$ 8	\$ 10	\$ 10
15,800	16,100	5	11	16	19	21
16,100	16,400	7	16	24	27	32
16,400	16,700	10	21	31	37	42
16,700	17,000	12	26	39	46	53
17,000	17,500	15	33	49	58	67
17,500	18,000	19	42	61	73	84
18,000	18,500	23	50	74	88	102
18,500	19,000	27	59	86	104	119
19,000	19,500	31	67	99	119	136
19,500	20,000	35	75	112	134	154
20,000	20,500	38	84	125	149	171
20,500	21,000	42	93	137	164	189
21,000	21,500	46	101	150	179	207
21,500	22,000	50	110	162	194	225
22,000	23,000	56	122	182	217	250
23,000	24,000	64	139	207	247	286
24,000	25,000	71	157	232	277	320
25,000	26,000	79	174	257	308	355
26,000	27,000	87	191	282	338	390
27,000	28,000	95	207	308	369	425
28,000	29,000	103	224	333	399	460
29,000	30,000	110	242	358	429	495
30,000	31,000	118	259	383	459	531
31,000	32,000	126	276	408	490	565
32,000	33,000	134	293	433	520	600
33,000	34,000	141	310	459	550	635
34,000	35,000	149	327	484	581	670
35,000	36,000	157	344	509	611	705
36,000	37,000	165	361	535	641	740
37,000	38,000	172	378	560	672	775
38,000	39,000	180	395	585	702	810
39,000	40,000	188	412	611	732	844
40,000	41,000	196	429	636	762	880
41,000	42,000	203	446	661	793	915
42,000	43,000	211	463	687	822	950
43,000	44,000	219	480	712	853	985
44,000	45,000	227	497	737	883	1,020
45,000	46,000	235	514	762	914	1,054
46,000	47,000	242	531	788	944	1,089
47,000	48,000	250	548	813	974	1,125
48,000	49,000	258	565	838	1,005	1,159
49,000	50,000	266	582	863	1,035	1,195
50,000	51,000	273	599	889	1,065	1,230
51,000	52,000	281	616	914	1,096	1,264
52,000	53,000	289	633	939	1,126	1,299
53,000	54,000	297	650	964	1,157	1,334
54,000	55,000	304	668	989	1,186	1,370
55,000	56,000	312	684	1,015	1,217	1,404
56,000	57,000	320	701	1,040	1,247	1,440
57,000	58,000	328	718	1,066	1,277	1,474
58,000	59,000	336	735	1,091	1,307	1,509
59,000	60,000	343	753	1,115	1,338	1,544
60,000	62,000	355	778	1,154	1,383	1,597
62,000	64,000	370	812	1,205	1,443	1,667
64,000	66,000	386	846	1,255	1,504	1,737
66,000	68,000	402	880	1,305	1,565	1,807
68,000	70,000	417	914	1,356	1,626	1,876
70,000	72,000	433	948	1,406	1,686	1,947
72,000	74,000	448	982	1,457	1,747	2,016
74,000	76,000	464	1,016	1,508	1,807	2,086
76,000	78,000	479	1,050	1,558	1,868	2,156
78,000	80,000	495	1,084	1,609	1,928	2,226
80,000	85,000	522	1,144	1,697	2,034	2,349
85,000	90,000	561	1,229	1,823	2,186	2,523
90,000	95,000	600	1,314	1,950	2,337	2,698
95,000	100,000 ²	638	1,400	2,075	2,489	2,873

¹For the last tax year of the lease, use the dollar amount for the preceding year.

²If the fair market value of the car is more than \$100,000, see Revenue Procedure 96-25 (1996-1 CB 681).

Appendix B-3. Inclusion Amounts for Cars First Leased in 1995

Fair Market Value		Tax Year of Lease ¹				
Over	Not Over	1st	2nd	3rd	4th	5th and Later
\$ 15,500	\$ 15,800	\$ 4	\$ 8	\$ 11	\$ 13	\$ 14
15,800	16,100	7	15	21	25	28
16,100	16,400	10	22	31	37	43
16,400	16,700	13	28	42	50	56
16,700	17,000	16	35	52	62	71
17,000	17,500	20	45	65	78	89
17,500	18,000	26	56	82	98	113
18,000	18,500	31	67	99	119	136
18,500	19,000	36	79	116	139	159
19,000	19,500	41	90	133	159	184
19,500	20,000	46	102	150	179	207
20,000	20,500	52	113	167	200	230
20,500	21,000	57	124	184	220	254
21,000	21,500	62	136	201	240	277
21,500	22,000	67	147	218	261	301
22,000	23,000	75	164	244	291	336
23,000	24,000	86	187	277	332	383
24,000	25,000	96	210	311	373	429
25,000	26,000	106	233	345	413	477
26,000	27,000	117	256	378	454	524
27,000	28,000	127	279	412	495	570
28,000	29,000	138	301	447	535	617
29,000	30,000	148	324	481	575	665
30,000	31,000	159	347	514	616	711
31,000	32,000	169	370	548	657	758
32,000	33,000	179	393	582	698	804
33,000	34,000	190	416	616	738	851
34,000	35,000	200	439	650	778	899
35,000	36,000	211	461	684	819	946
36,000	37,000	221	484	718	860	992
37,000	38,000	232	507	751	901	1,039
38,000	39,000	242	530	785	942	1,086
39,000	40,000	253	552	820	982	1,133
40,000	41,000	263	576	853	1,022	1,180
41,000	42,000	273	599	887	1,063	1,227
42,000	43,000	284	621	921	1,104	1,274
43,000	44,000	294	644	955	1,145	1,320
44,000	45,000	305	667	989	1,185	1,367
45,000	46,000	315	690	1,022	1,226	1,415
46,000	47,000	326	712	1,057	1,266	1,462
47,000	48,000	336	735	1,091	1,307	1,508
48,000	49,000	346	759	1,124	1,347	1,556
49,000	50,000	357	781	1,158	1,388	1,603
50,000	51,000	367	804	1,192	1,429	1,649
51,000	52,000	378	827	1,226	1,469	1,696
52,000	53,000	388	850	1,260	1,510	1,743
53,000	54,000	399	872	1,294	1,551	1,790
54,000	55,000	409	895	1,328	1,591	1,837
55,000	56,000	419	919	1,361	1,632	1,884
56,000	57,000	430	941	1,395	1,673	1,931
57,000	58,000	440	964	1,429	1,714	1,977
58,000	59,000	451	987	1,463	1,754	2,024
59,000	60,000	461	1,010	1,497	1,794	2,072
60,000	62,000	477	1,044	1,548	1,855	2,142
62,000	64,000	498	1,089	1,616	1,937	2,235
64,000	66,000	519	1,135	1,683	2,018	2,330
66,000	68,000	539	1,181	1,751	2,100	2,423
68,000	70,000	560	1,227	1,819	2,180	2,517
70,000	72,000	581	1,272	1,887	2,262	2,611
72,000	74,000	602	1,318	1,955	2,343	2,704
74,000	76,000	623	1,364	2,022	2,424	2,799
76,000	78,000	644	1,409	2,090	2,506	2,892
78,000	80,000	665	1,455	2,158	2,586	2,986
80,000	85,000	701	1,535	2,277	2,729	3,150
85,000	90,000	753	1,650	2,445	2,932	3,385
90,000	95,000	806	1,763	2,616	3,135	3,619
95,000	100,000 ²	858	1,878	2,784	3,339	3,853

¹For the last tax year of the lease, use the dollar amount for the preceding year.

²If the fair market value of the car is more than \$100,000, see Revenue Procedure 95-9 (1995-1 CB 498).

Appendix B-4. Inclusion Amounts for Cars First Leased in 1994

Fair Market Value		Tax Year of Lease ¹				
Over	Not Over	1st	2nd	3rd	4th	5th and Later
\$ 14,600	\$ 14,900	\$ 0	\$ 1	\$ 1	\$ 2	\$ 2
14,900	15,200	2	5	6	9	11
15,200	15,500	4	9	14	17	20
15,500	15,800	6	14	21	25	30
15,800	16,100	8	19	27	34	39
16,100	16,400	10	24	34	42	49
16,400	16,700	12	28	41	51	58
16,700	17,000	14	33	48	59	68
17,000	17,500	17	39	57	70	81
17,500	18,000	21	47	68	84	97
18,000	18,500	24	55	80	97	113
18,500	19,000	28	62	92	111	129
19,000	19,500	31	70	104	124	145
19,500	20,000	35	78	115	138	161
20,000	20,500	39	85	127	152	176
20,500	21,000	42	93	138	166	193
21,000	21,500	46	101	149	180	208
21,500	22,000	49	109	161	193	225
22,000	23,000	54	121	178	214	248
23,000	24,000	62	136	201	242	280
24,000	25,000	69	151	224	270	312
25,000	26,000	76	167	247	297	344
26,000	27,000	83	182	270	325	376
27,000	28,000	90	198	293	352	408
28,000	29,000	97	213	317	379	440
29,000	30,000	104	229	339	408	471
30,000	31,000	111	244	363	435	503
31,000	32,000	118	260	385	463	535
32,000	33,000	125	276	408	490	567
33,000	34,000	132	291	431	518	599
34,000	35,000	139	307	454	545	631
35,000	36,000	146	322	478	573	662
36,000	37,000	153	338	500	601	694
37,000	38,000	161	353	523	628	726
38,000	39,000	168	368	547	656	757
39,000	40,000	175	384	569	684	790
40,000	41,000	182	399	593	711	822
41,000	42,000	189	415	615	739	854
42,000	43,000	196	431	638	766	886
43,000	44,000	203	446	661	794	918
44,000	45,000	210	462	684	821	950
45,000	46,000	217	477	708	849	981
46,000	47,000	224	493	730	877	1,013
47,000	48,000	231	508	754	904	1,045
48,000	49,000	238	524	776	932	1,077
49,000	50,000	245	539	800	959	1,109
50,000	51,000	252	555	822	987	1,141
51,000	52,000	260	570	845	1,015	1,172
52,000	53,000	267	585	869	1,042	1,204
53,000	54,000	274	601	892	1,069	1,236
54,000	55,000	281	617	914	1,097	1,268
55,000	56,000	288	632	938	1,125	1,299
56,000	57,000	295	648	960	1,153	1,331
57,000	58,000	302	663	984	1,180	1,363
58,000	59,000	309	679	1,006	1,208	1,395
59,000	60,000	316	694	1,030	1,235	1,427
60,000	62,000	327	717	1,065	1,276	1,475
62,000	64,000	341	748	1,111	1,332	1,538
64,000	66,000	355	780	1,156	1,387	1,602
66,000	68,000	369	811	1,202	1,442	1,666
68,000	70,000	383	842	1,248	1,497	1,730
70,000	72,000	397	873	1,294	1,553	1,793
72,000	74,000	412	903	1,341	1,608	1,857
74,000	76,000	426	935	1,386	1,663	1,921
76,000	78,000	440	966	1,432	1,718	1,985
78,000	80,000	454	997	1,478	1,774	2,048
80,000	85,000	479	1,051	1,559	1,870	2,160
85,000	90,000	514	1,129	1,674	2,008	2,319
90,000	95,000	550	1,206	1,789	2,146	2,478
95,000	100,000 ²	585	1,284	1,904	2,284	2,637

¹For the last tax year of the lease, use the dollar amount for the preceding year.

²If the fair market value of the car is more than \$100,000, see Revenue Procedure 94-53 (1994-2 CB 712).

Appendix B-5. Inclusion Amounts for Cars First Leased in 1993

Fair Market Value		Tax Year of Lease ¹				
Over	Not Over	1st	2nd	3rd	4th	5th and Later
\$ 14,300	\$ 14,600	\$ 1	\$ 1	\$ 2	\$ 2	\$ 3
14,600	14,900	3	5	7	9	9
14,900	15,200	4	9	13	15	17
15,200	15,500	6	13	18	22	25
15,500	15,800	8	16	24	29	32
15,800	16,100	9	20	30	35	40
16,100	16,400	11	24	35	42	48
16,400	16,700	13	27	41	49	55
16,700	17,000	14	32	46	55	63
17,000	17,500	17	36	54	64	73
17,500	18,000	20	42	63	75	87
18,000	18,500	22	49	72	86	99
18,500	19,000	25	55	82	97	112
19,000	19,500	28	61	91	108	125
19,500	20,000	31	67	100	120	137
20,000	20,500	34	74	109	130	150
20,500	21,000	37	80	118	142	163
21,000	21,500	39	86	128	153	175
21,500	22,000	42	92	138	163	189
22,000	23,000	47	101	151	181	207
23,000	24,000	52	114	170	202	233
24,000	25,000	58	127	187	225	259
25,000	26,000	64	139	206	247	285
26,000	27,000	69	152	224	270	310
27,000	28,000	75	164	243	292	335
28,000	29,000	81	176	262	313	362
29,000	30,000	86	189	280	336	387
30,000	31,000	92	201	299	358	412
31,000	32,000	98	214	317	380	438
32,000	33,000	103	226	336	402	464
33,000	34,000	109	239	354	424	490
34,000	35,000	115	251	373	446	515
35,000	36,000	120	264	391	469	540
36,000	37,000	126	276	410	491	566
37,000	38,000	132	288	429	513	591
38,000	39,000	137	301	447	535	617
39,000	40,000	143	314	465	557	643
40,000	41,000	149	326	484	579	669
41,000	42,000	154	339	502	601	695
42,000	43,000	160	351	521	623	720
43,000	44,000	166	363	539	646	746
44,000	45,000	171	376	558	668	771
45,000	46,000	177	388	577	690	796
46,000	47,000	183	401	594	713	822
47,000	48,000	189	413	613	735	847
48,000	49,000	194	426	631	757	874
49,000	50,000	200	438	650	779	899
50,000	51,000	206	450	669	801	925
51,000	52,000	211	463	687	824	950
52,000	53,000	217	475	706	846	975
53,000	54,000	223	488	724	867	1,002
54,000	55,000	228	501	742	890	1,027
55,000	56,000	234	513	761	912	1,052
56,000	57,000	240	525	780	934	1,078
57,000	58,000	245	538	798	956	1,104
58,000	59,000	251	550	817	978	1,130
59,000	60,000	257	563	835	1,000	1,155
60,000	62,000	265	581	863	1,034	1,194
62,000	64,000	277	606	900	1,078	1,245
64,000	66,000	288	631	937	1,123	1,295
66,000	68,000	299	656	974	1,167	1,347
68,000	70,000	311	681	1,011	1,211	1,398
70,000	72,000	322	706	1,048	1,255	1,450
72,000	74,000	333	731	1,085	1,300	1,500
74,000	76,000	345	756	1,121	1,345	1,551
76,000	78,000	356	781	1,158	1,389	1,603
78,000	80,000	367	806	1,195	1,434	1,654
80,000	85,000	387	849	1,261	1,510	1,744
85,000	90,000	416	911	1,353	1,622	1,871
90,000	95,000	444	974	1,445	1,733	1,999
95,000	100,000 ²	472	1,036	1,538	1,843	2,128

¹For the last tax year of the lease, use the dollar amount for the preceding year.

²If the fair market value of the car is more than \$100,000, see Revenue Procedure 93-35 (1993-2 CB 472).

Appendix B-6. Inclusion Amounts for Cars First Leased in 1987 through 1992

Fair Market Value		Tax Year of Lease ¹				
		For Lease Term Beginning in 1987 or 1988	For Lease Term Beginning in 1989 or 1990	For Lease Term Beginning in 1991	For Lease Term Beginning in 1992	
Over	Not Over	5th and Later	5th and Later	5th and Later	4th	5th and Later
\$ 12,800	\$ 13,100	\$ 9	\$ 2	\$ 0	\$ 0	\$ 0
13,100	13,400	28	9	0	0	0
13,400	13,700	47	26	6	0	0
13,700	14,000	65	45	18	2	4
14,000	14,300	84	64	32	13	15
14,300	14,600	103	83	45	23	26
14,600	14,900	122	101	58	32	38
14,900	15,200	140	120	71	43	49
15,200	15,500	159	139	85	52	61
15,500	15,800	178	158	98	62	72
15,800	16,100	196	176	112	72	84
16,100	16,400	215	195	124	82	95
16,400	16,700	234	213	138	92	106
16,700	17,000	253	232	151	102	118
17,000	17,500	277	258	169	115	133
17,500	18,000	309	289	191	132	152
18,000	18,500	340	319	213	148	171
18,500	19,000	371	351	235	164	190
19,000	19,500	402	382	257	181	209
19,500	20,000	433	413	279	198	228
20,000	20,500	465	445	301	214	247
20,500	21,000	496	476	323	230	267
21,000	21,500	527	507	345	247	285
21,500	22,000	558	538	368	263	305
22,000	23,000	605	585	401	288	333
23,000	24,000	667	647	445	321	371
24,000	25,000	729	709	489	354	409
25,000	26,000	792	772	534	387	447
26,000	27,000	854	834	578	420	485
27,000	28,000	917	897	622	453	523
28,000	29,000	979	959	666	486	561
29,000	30,000	1,041	1,021	710	518	600
30,000	31,000	1,104	1,084	755	552	637
31,000	32,000	1,166	1,146	799	584	676
32,000	33,000	1,228	1,209	843	618	713
33,000	34,000	1,291	1,270	888	650	752
34,000	35,000	1,353	1,333	931	684	789
35,000	36,000	1,415	1,396	976	716	828
36,000	37,000	1,478	1,458	1,020	750	865
37,000	38,000	1,540	1,520	1,064	783	904
38,000	39,000	1,602	1,583	1,109	816	942
39,000	40,000	1,665	1,644	1,153	849	980
40,000	41,000	1,727	1,707	1,197	882	1,018
41,000	42,000	1,789	1,770	1,241	915	1,056
42,000	43,000	1,852	1,832	1,285	948	1,094
43,000	44,000	1,914	1,894	1,330	981	1,132
44,000	45,000	1,976	1,956	1,374	1,013	1,171
45,000	46,000	2,039	2,019	1,418	1,047	1,208
46,000	47,000	2,101	2,081	1,462	1,079	1,247
47,000	48,000	2,164	2,144	1,506	1,113	1,284
48,000	49,000	2,226	2,205	1,551	1,145	1,323
49,000	50,000	2,288	2,268	1,595	1,179	1,360
50,000	51,000	2,351	2,331	1,639	1,211	1,399
51,000	52,000	2,413	2,393	1,684	1,245	1,436
52,000	53,000	2,475	2,455	1,727	1,277	1,475

Appendix B-6. (Continued)

Fair Market Value		Tax Year of Lease ¹				
		For Lease Term Beginning in 1987 or 1988	For Lease Term Beginning in 1989 or 1990	For Lease Term Beginning in 1991	For Lease Term Beginning in 1992	
Over	Not Over	5th and Later	5th and Later	5th and Later	4th	5th and Later
\$ 53,000	\$ 54,000	\$ 2,538	\$ 2,517	\$ 1,772	\$ 1,311	\$ 1,513
54,000	55,000	2,600	2,580	1,816	1,343	1,551
55,000	56,000	2,662	2,643	1,860	1,377	1,589
56,000	57,000	2,725	2,705	1,905	1,409	1,627
57,000	58,000	2,787	2,767	1,949	1,442	1,666
58,000	59,000	2,849	2,829	1,993	1,475	1,703
59,000	60,000	2,912	2,892	2,037	1,508	1,741
60,000	62,000	3,005	2,985	2,103	1,557	1,799
62,000	64,000	3,130	3,110	2,192	1,623	1,875
64,000	66,000	3,255	3,235	2,280	1,689	1,951
66,000	68,000	3,379	3,360	2,369	1,755	2,027
68,000	70,000	3,504	3,484	2,457	1,821	2,103
70,000	72,000	3,629	3,609	2,546	1,887	2,179
72,000	74,000	3,753	3,733	2,634	1,953	2,255
74,000	76,000	3,878	3,858	2,723	2,019	2,331
76,000	78,000	4,003	3,983	2,811	2,085	2,407
78,000	80,000	4,128	4,107	2,900	2,150	2,484
80,000	85,000	4,346	4,325	3,054	2,267	2,617
85,000	90,000	4,658	4,638	3,276	2,431	2,807
90,000	95,000	4,969	4,949	3,497	2,595	2,998
95,000	100,000 ²	5,281	5,261	3,718	2,761	3,188

¹For the last tax year of the lease, use the dollar amount for the preceding year.

²If the fair market value of the car is more than \$100,000, see the document listed for the first year of the lease.

For 1992, Revenue Procedure 92-43 (1992-1 CB 873)

For 1991, Revenue Procedure 91-30 (1991-1 CB 563)

For 1990, Revenue Procedure 90-22 (1990-1 CB 504)

For 1989, Revenue Procedure 89-64 (1989-2 CB 783)

For 1987 or 1988, I.T. Regulation 1.280F-7(a)

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