

# Keeping Records to Protect Travel and Expense Deductions

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Typically, a small-business owner can realize tax benefits for travel and entertainment (T&E) expenses incurred during the year. But this remains a prime audit target for IRS examiners, so be careful to observe the letter of the tax law. Keeping that in mind, here is an overview of some of the key tax rules for T&E expenses.

## Business Travel Expenses

If you travel away from home on business, you can deduct your transportation costs (e.g., airfare), meals, lodging, and related incidental expenses such as cab fare and tips while you are away on business. The deduction for meals is limited to 50% of the cost, while other travel expenses are fully deductible. However, you must keep records of your business travel expenses by contemporaneous diary or some other means.

The records for business travel must show:

1. the dates you left and returned, and the number of days away on business;
2. the destination of the business travel;
3. the reason for the business trip; and
4. the cost of each travel expense.

In addition, you must keep receipts of all lodging expenses and other business-related expenses over \$75. Other special rules may apply to deductions for vehicles used for business driving, including deduction limits on so-called "luxury cars." In lieu of deducting actual business-related auto expenses for 2012, you may qualify for a deduction based on a flat rate of 55.5 cents per business mile (plus business-related tolls and parking fees).

## Business Entertainment Expenses

Generally speaking, you can deduct qualified entertainment expenses either directly related to your business or associated with your business. The deduction is equal to 50% of the cost.

- **Directly related entertainment:** Entertainment is considered “directly related to” your business if you actually discuss business during the entertainment and you have more than a general expectation of deriving a business benefit from the meeting. Furthermore, the entertainment must take place in an atmosphere conducive to discussing business.
- **Associated-with entertainment:** Entertainment is considered “associated with” your business if it precedes or follows a substantial business discussion. It is not necessary to talk about business matters during the entertainment. If the client comes from out of town, the business discussion can take place the day before or the day after the entertainment.

Note that the cost of “lavish” or “extravagant” entertainment is not deductible. However, that does not mean you cannot go first-class if the situation warrants it.

Similar to business travel expenses, you must keep detailed records of your entertainment expenses. It is generally advisable to use a contemporaneous diary or log.

The records for business entertainment must show:

- the date, location and nature of the entertainment;
- the amount spent on the entertainment;
- the business reason for the entertainment or the benefit you expect to derive;
- the person or people entertained and their business relationship to you; and
- the details of the substantial business discussion (e.g., date, duration and nature of the meeting) for any associated-with entertainment.

Finally, be sure to keep receipts or credit card statements for expenditures of \$75 or more. This limit has not been raised in years. For questions on your travel and expense deductions don't hesitate to contact your Henry & Horne, LLP tax advisor.

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**Rick Schultz, CPA, Partner possesses an extensive knowledge of individual and partnership tax planning, preparation and compliance as well as small business consulting for Henry & Horne, LLP. For questions contact Rick at (480) 483-1170 or RickS@hhcpa.com.**



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