

Per Diem Frequently Asked Questions

This PDF is compiled with the most popular questions. These questions and answers, in addition to many others, are also available in our KnowledgeBase-

www.watsoncpagroup.com/kb

How does per diem work?

The question comes up in different forms, but essentially it is the same- people want to know how to compute per diem allowances, how to deduct them on their tax returns, and what is the net-net of all the hoopla. Here we go-

The government has established the costs for lodging, meals and incidentals throughout the United States (referred to as CONUS for contiguous states, and OCONUS for Alaska, Hawaii, etc.) and throughout the international community. These rates typically come in two forms- (a) lodging, and (b) meals and incidentals expense (M&IE).

Pilots and flight attendants are typically only interested in the meals and incidentals portion of the per diem allowance since the company pays for the lodging. In addition most flight crew are paid an hourly rate for their time away from base, which is used to offset the costs of traveling. However in most cases the airline falls short and does not pay for the full amount of per diem allowed. This difference when aggregated over the year becomes your deduction on your tax return.

Let's look at an example. You show for work at 1100, overnight in ASE and get released at 1300. You were away from base for 26 hours, and were paid \$1.65 per hour for a total of \$42.90. ASE allows \$71 towards meals and incidentals per night. Since you had a partial day on either side of the overnight, your total allowance is actually \$106.50 ($\$71 \times 2 \times \frac{3}{4}$ -day). Therefore you have a **shortfall, or gap, of \$63.60**. This computation method is considered the city-by-city method (in this example, the standard daily rate would be much lower).

To recap- the IRS has allowed you to deduct \$106.50. The company paid you \$42.90 (bummer). Therefore your deduction has been reduced because of a partial reimbursement to \$63.60.

What do you do with this number? Typically if you were a regular, garden-variety employee, you would only be able to deduct 50% of the \$63.60. However, if you are subjected to Department of Transportation (DOT) rules regarding duty limitations and rest requirements then you may deduct 80% of the \$63.60. Pilots, flight attendants, truck drivers, railroad engineers, etc. are all subjected to DOT regulations.

As an aside, the more efficient the trip and / or the higher the per diem allowance (such as Southwest), the smaller the per diem deduction will be.

What mistakes can be made with per diem?

In reviewing prior tax returns from CPAs and tax professionals who did not fully understand the per diem calculation and deduction, **we found errors in three areas-**

1. the incorrect computation of the per diem allowance
2. the failure to apply the per diem paid by the company and
3. the misapplication of the 50% / 80% rule for DOT employees.

All three of these areas are important for an accurate and comprehensive tax return.

Is deducting per diem allowances really that important?

Yes! For most of our flight crew tax clients, correctly calculating and deducting your per diem will result in several hundreds of dollars in additional tax refund. This industry and career can be frustrating, at least take advantage of this benefit. And if you fly a lot of international trips, the per diem deduction can be quite large.

If necessary, we can also review your last three tax returns to ensure your per diem allowance was properly computed and deducted.

Which method should I use? The City By City or Standard Daily Rate?

There are two ways to calculate your per diem allowance- standard daily rate and city by city. Each has its advantages. Domestically, either method might yield the best result however if you fly a lot of international pairings, city by city is clearly the best option, hands down.

Per diem rates are broken down into three parts-

CONUS (domestic) – US GSA Office, and reprinted in IRS Publication 1542

OCONUS (Hawaii, US territories, etc.) – Department of Defense Travel Management Office

International – US State Department

Several per diem allowance rates exist, and it is important to choose the correct one. For example, Aspen (ASE) currently has a \$288 per diem allowance (during ski season of course), but this includes lodging which is typically paid for by the airline. The amount associated with Meals and Incidentals Expense (M&IE) is only \$71 per night. This is using the city by city method.

Conversely, the standard daily rate is currently \$52 for domestic, and it changes slightly for Q4 (Oct-Dec) and international destinations.

3/4 Day Convention

Per diem allowance will automatically get adjusted to a 3/4-day for the beginning and end of your trip, and your last overnight will be used to compute the per diem for the last day of your trip (return to base). Regardless of what you have read in IRS Publication 463, the Tax Court and industry practices typically apply the 3/4-day convention to the first and last day. Yes, you can use any method that is reasonable and applied consistently, but keep reading below.

Some per diem calculators break it down by the hour, but using a 3/4-day convention will consistently provide larger allowances. In the theory of large numbers, your start and end times will generally move towards the middle of the workday, or a 1/2-day. So using a 3/4-day will give you larger deductions.

Having said that, if you consistently fly the same pairings, and the pairings have unusual show and release times, we'll take into account if it is to your advantage to do so. For example, maintenance domiciles or out-station type domiciles will see early show times and / or late release times. International pairings have some nuances too.

Here are some examples-

Overnights	City by City Per Diem	Standard Daily Per Diem
ASE, SFO, ORD	\$53.25 + \$71 + \$71 + \$53.25 = \$249	\$39 + \$52 + \$52 + \$39 = \$182
ASE, GRB, SFO	\$53.25 + \$46 + \$71 + \$53.25 = \$224	\$39 + \$52 + \$52 + \$39 = \$182
FAR, GRB, FSD	\$34.50 + \$46 + \$46 + \$34.50 = \$161	\$39 + \$52 + \$52 + \$39 = \$182

As you can see, each method has its advantages. If you fly to a lot of smaller cities, generally speaking the standard daily rate is preferred versus a mix of larger and smaller cities. If you fly internationally even occasionally, the city by city method is generally preferred. Heck, LHR is over \$180 per night.

International destinations currently have larger per diem allowances since the currency exchange rate between the US dollar and foreign currency favors other currencies. In other words, the US dollar is weak right now.

You can only use one method for the entire tax year. So, you cannot switch back and forth between pairings. We compute your per diem using both methods, and use the per diem allowance with the greatest deduction.

How does per diem affect your taxes?

Most domestic crewmembers who work an average of 15 days per month will have a per diem allowance of around \$9,000. Here's an example-

Per Diem Allowance	\$9,000	
Airline Reimbursement	<u>\$5,500</u>	
Difference	\$3,500	
DOT Allowance	80%	
Per Diem Deduction	\$2,800	(80% x \$3,500)

Because you are Department of Transportation (DOT) employee, the difference between the per diem allowance and the per diem paid by your employer is multiplied by 80% (if you were not a DOT employee, it would be reduced by 50% instead of 20%, so you got that going for you- which is nice).

Therefore your deduction is \$2,800 which at a tax rate of 15% equals \$420 in your pocket. International crewmembers can easily see a \$10,000 deduction which is \$1,500 in your pocket.

Seniority is everything as they say.

Can I take a per diem deduction for turns, locals or day trips?

No. For a per diem deduction, an overnight or a substantial rest period must occur. This rest requirement is not satisfied by merely napping in the crew lounge. Your relief from duty must be long enough to get necessary sleep or rest.

The Tax Court has developed the Sleep or Rest rule which is basically-

If the nature of the taxpayer's employment is such that when away from home, during released time, it is reasonable for him to need and to obtain sleep or rest in order to meet the exigencies of his employment or the business demands of his employment, his expenditures (including incidental expenses, such as tips) for the purpose of obtaining sleep or rest are deductible traveling expenses.

Here is an additional snippet from a famous case called **Bissonnette** (Tax Court Opinion 127 No. 10)-

If the nature of petitioner's employment was such that when away from home, during released time, it was reasonable for him to need and to obtain sleep or rest in order to meet the exigencies or business demands of his employment, his expenses for this purpose would be traveling expenses under section 162(a)(2). See *Williams v. Patterson*, supra at 340; Rev. Rul. 75-170, 1975-1 C.B. 60. However, the released time must be of a sufficient duration that it would ordinarily be related to a significant increase in expenses. See *United States v. Correll*, supra.

In the *Bissonnette* case, the taxpayer was a boat captain who worked a 16-hour shift and obtained a hotel during his break for rest. This caused the Tax Court to consider his rest to be substantial.

Do you calculate my per diem expenses?

Yes, we take care of this hassle for you. We take your schedule and input that into our system to calculate your per diem allowance. We subtract the non-tax per diem paid to you by the airline, then multiply the difference by the DOT standard of 80% (as of 2012). This figure is entered on your Form 2106 (Unreimbursed Employee Business Expense) and ends up on your Schedule A (Itemized Deductions).

Some airlines such as United or those who use Sabre as their crew scheduling backbone can provide a report detailing your overnights and the associated per diem allowance (such as a FLICA report). We are generally comfortable with their calculations and will use the computed per diem allowance amount. In these situations, our fee will be reduced by \$10 for domestic crewmembers and \$25 for international crewmembers.

Myth Buster: Van driver tips are not deductible. They are considered incidental expenses and have been accounted at \$5 per night in your per diem allowance. We wonder how long it will take the IRS to realize that pilots and flight attendants only spend \$2. Mum's the word.

How can I calculate my own per diem deduction?

Since per diem rates fluctuate and because there are two distinct methods for computing the per diem allowance, the Watson CPA Group developed a **free** online per diem calculator. Pilots, flight attendants, truck drivers, train engineers and business travelers can use the calculator to determine the per diem allowance using both methods.

From there a taxpayer can choose which computation provides the best tax deduction.

Several companies and websites offer a similar per diem calculator, but only the Watson CPA Group provides this service free of charge. They offer all the taste of a CPA certified tax deduction without the calories of having to pay for it.

Visit www.watsoncpagroup.com/per-diem-calculator.php to calculate your per diem deduction.

On your Form 2106, you will enter the higher of the two per diem allowance figures on line 6, column B. Next you will enter your non-tax per diem paid to you by your employer on line 7, column B. Line 8, column B will be the difference between your per diem allowance and the non-tax per diem paid. Lastly, line 9, column B is computed by taking 80% of the amount of line 8, column B.

What are the per diem rates for 2013?

In a recent U.S. GSA press release the estimated savings for the Federal government is around \$20 million for fiscal year 2013. This also indirectly maintains the tax rate for Department of Transportation (DOT) workers such as pilots, flight attendants, railroad engineers and truck drivers.

Besides DOT workers, other organizations and businesses are not excited about the frozen rates. When tackling the per diem rates for 2013, the U.S. GSA wanted a 30% decrease. But the American Hotel and Lodging Association and the U.S. Travel Association lobbied heavily to at the very least maintain 2012 per diem levels. Many government workers, military personnel and business travelers use Federal per diem rates when making lodging decisions and reservations.

Therefore if rates are frozen then hotels must be careful when considering raising lodging rates in 2013. If a hotel exceeds the Federal per diem rate, a traveler might look elsewhere. Hotel and travel lobbyists will continue to work with the U.S. GSA office to ensure economic per diem rates for the future. Sounds like fun!

Please call or email us anytime with your questions and concerns. Thank you in advance, and we look forward to working with you!

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