

Pilot Travel Expenses and Per Diem Update for 2015

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This article reviews the federal rules for U.S. pilots regarding the taxation and deductibility of travel expenses, including per diem reimbursements, for tax year 2015 (for which individual tax returns are due, generally, by April 15, 2016). For the benefit of your tax advisers, the official rules for tax year 2015 are set forth in IRS Notice 2015-63. General information is also contained in IRS Publication 463, Travel, Entertainment, Gift, and Car Expenses; IRS Publication 1542, Per Diem Rates; and Revenue Procedure 2011-47. These documents are available at www.irs.gov.

A U.S. pilot flying the line is always on business travel, therefore his or her qualifying travel expenses are deductible as ordinary and necessary business expenses, by either the airline or the pilot. ALPA's Retirement & Insurance Department has put together the following information you should consider as you prepare your taxes.



TAXATION OF PER DIEM

Many of ALPA's collective bargaining agreements provide that the airline will pay each pilot a fixed amount, often called "per diem," to cover meals and incidental expenses (M&IE) that pilots incur while on a trip. When an airline makes these per diem payments (or otherwise reimburses pilots for travel expenses), the airline may exclude all or a portion of these payments or reimbursements from a pilot's taxable income reported on Form W-2. The amount excluded from a pilot's income generally is the amount paid to the pilot that doesn't exceed the federal per diem rates. Per diem payments paid for day or other nonovernight trips (trips that do not require sleep or rest) and amounts paid in excess of the federal per diem rates are included in the employee's taxable income and are reported on the pilot's Form W-2. Frequently, the amount of per diem the airline pays or reimburses is not enough to cover reasonable business travel expenses. In those cases, pilots may be entitled to claim an itemized deduction for the expenses not covered.

If a pilot receives no per diem payments or reimbursements from the employer, or receives per diem payments

that the airline includes in taxable income, the pilot may be entitled to claim an itemized deduction for expenses incurred while on business travel.



EXPENSES FOR "OVERNIGHT TRIPS"

For travel expenses to be excluded from the pilot's taxable income or to be claimed by the pilot as an itemized deduction, the pilot's expense must be incurred while on a business trip that requires sleep or rest (an "overnight trip"). Expenses incurred on trips that are not overnight do not satisfy this requirement. For pilots, the expenses at issue are usually M&IE expenses, because the airline pays for lodging directly or reimburses the pilot for it separately.



SUBSTANTIATING EXPENSES

Recognizing the burden of substantiating expenses, the IRS provides that a designated amount of expenses relating to overnight trips may be deemed substantiated. For amounts deemed substantiated, pilots need not maintain any records of the amounts actually spent while on the trip.

If the employer pays for lodging separately, then the expenses that may be deemed substantiated are those for M&IE. The amount that is deemed substantiated is generally equal to the standard amount the federal government would pay its own employees



for M&IE when they travel to the same locality or the amount determined under special M&IE rates applicable to transportation industry employees.

The federal government publishes standard M&IE rates for every locality in the world. The M&IE rates for CONUS (for Continental United States) and OCONUS (for Outside CONUS) can be found at www.gsa.gov. For 2015, the daily M&IE rates for CONUS ranged from \$46 to \$71, and from \$1 to \$299 for OCONUS. These rates may change on a monthly basis.

The IRS also provides special transportation industry M&IE rates for CONUS and OCONUS. For 2015, the transportation industry M&IE rate is \$63 for CONUS and \$68 for OCONUS.

Pilots may use either the standard M&IE rates or the special transportation industry M&IE rates to determine the amount deemed substantiated for claiming itemized tax deductions. For any calendar year, a pilot must use either the standard M&IE rates for *all* CONUS travel or the special transportation industry M&IE rates for *all* CONUS travel, and the same applies for all OCONUS travel.

WHAT'S NOT INCLUDED IN THE M&IE RATES?



The M&IE rates aren't reduced due to any meals that an airline or a hotel provides a pilot. Furthermore, the "incidental expense" portion of the M&IE rates doesn't include such expenses as cab fares to and from lodging and the business place and the place where meals are taken, telephone calls, laundry, cleaning and pressing, the mailing costs of filing travel vouchers, and payments for employer-sponsored credit card billings. These expenses, to the extent they constitute reasonable business expenses, are deductible by the payor

(airline or pilot) as business expenses (subject to applicable limits).



PRORATING THE M&IE LIMIT

The full M&IE amount is available only for a full calendar day of business travel, i.e., from 12:01 a.m. through midnight. For a partial day of travel, the taxpayer must prorate the applicable M&IE amount. The IRS allows 75 percent of the full M&IE amount to be claimed. Assume, for example, that a pilot's trip begins at 11:55 p.m. on Monday and ends at 12:05 a.m. on Wednesday and that the pilot's required rest occurred in cities with an applicable M&IE per diem rate of \$46. Applying the IRS's allowed method of proration, the amount deemed substantiated would be \$34.50 (.75 x \$46) for Monday, \$46 for Tuesday, and \$34.50 (.75 x \$46) for Wednesday.



ITEMIZED DEDUCTIONS

If a pilot has business travel expenses that the employer did not reimburse, then the pilot may be able to claim an itemized deduction on his or her tax return. If a pilot claims this deduction, Form 2106, Employee Business Expenses, must be completed. This form, and all other IRS forms and publications, may be obtained at www.irs.gov or by calling the IRS at 1-800-TAXFORM.

To claim any business travel expense as an itemized deduction, a pilot must be able to substantiate the time, place, and business purpose of the business travel, and the amount of the expense. The time, place, and business purpose must be substantiated with actual records, such as a pilot's logbook. The amount of the business expense must also be substantiated; but in the case of M&IE, the amount may be deemed substantiated (no written records will be required). Other business travel expenses must

be substantiated with records. (If the expense is less than \$75, the IRS won't require a receipt to substantiate the amount spent on any single purchase. But this rule doesn't apply to lodging expenses—receipts are necessary even if the expense is less than \$75.)

Generally, a pilot's itemized deduction for M&IE is subject to an 80 percent limit and a 2 percent threshold. Under a special rule applicable to pilots, 80 percent of the M&IE amount deemed substantiated is deductible in 2015. In addition, no itemized deduction for M&IE may be claimed unless the pilot's aggregate miscellaneous itemized deductions (including business expenses) exceed 2 percent of his or her adjusted gross income. Union dues constitute deductible employee business expenses and count toward the 2 percent threshold.



APPLYING THE FEDERAL M&IE RATES USING THE STANDARD M&IE RATES

For an example of how the federal M&IE rates are applied, assume a collective bargaining agreement entitles a pilot to per diem payments equal to \$3.50 per hour. Assume also that a pilot covered by the agreement flies a two-day trip in 2015, with report for duty at 12:01 a.m. on the first day, an overnight stay in Chicago, Ill., and release from duty at midnight on the second day.

The 2015 federal M&IE rate for Chicago is \$71, so the maximum excludable amount for this trip is \$142 (\$71 x 2). The pilot is actually paid per diem of \$168 (\$3.50/hour x 48 hours), so \$142 is excluded from the pilot's taxable income and is shown on the pilot's Form W-2, Box 12, Code L. The remaining \$26 is included in the pilot's taxable income and is shown on the pilot's Form W-2 in Box 1 (and Boxes 3 and 5, as applicable) as taxable wages.

Alternatively, assume the collective bargaining agreement entitles the pilot

to per diem payments equal to only \$1.00 per hour, and the pilot makes the same two-day trip in 2015. In this case, the entire per diem payment of \$48 (\$1.00 x 48 hours) would be excluded from the pilot's taxable income because this amount is less than the maximum excludable amount of \$142. However, in this case, the pilot may claim an itemized deduction of \$94 for the difference between the excluded payment of \$48 and the federal M&IE rate of \$142, without needing to substantiate the M&IE expenses actually incurred (subject to the 80 percent limit and 2 percent threshold discussed above).

What if this pilot's M&IE exceed \$142? Regardless of the amount excluded from the pilot's income, if the pilot's expenses exceed the federal M&IE rate of \$142, an itemized deduction is available for all reasonable amounts spent (less the amount excluded from the pilot's taxable income), but only if the pilot can actually substantiate all expenses (both above and below the deemed substantiated amount of \$142).

For example, if the airline paid the pilot excluded (nontaxable) per diem payments of \$48, but the pilot's actual, reasonable M&IE were \$200, the pilot could claim an itemized deduction of \$152 (\$200 minus \$48)—but only if the pilot could actually substantiate the entire \$200 in expenses. Alternatively, the pilot could claim an itemized deduction of \$94 (\$142

minus \$48) without substantiating any expenses, since all expenses up to \$94 are deemed substantiated. (All of the pilot's itemized deductions would be subject to the 80 percent limit and 2 percent threshold.)



USING THE SPECIAL TRANSPORTATION INDUSTRY M&IE RATES

Assume a pilot travels away from home on business within CONUS. The airline pays the pilot a standard taxable per diem allowance of \$2.00 for each hour the pilot is away from his or her domicile. The pilot leaves the domicile at 9:00 a.m. on Monday and returns to the domicile at 9:00 a.m. on Tuesday with an overnight stay. The pilot receives \$48 (\$2.00 x 24) in taxable per diem. The CONUS special transportation industry M&IE rate is \$63 per day, so the amount deemed substantiated using the special transportation industry rate for these days is \$94.50 (\$63 x 2 x .75), i.e., the total per diem allowance under the special CONUS rates for the transportation industry, prorated as discussed above. The pilot could claim an itemized deduction \$94.50 (subject to the 80 percent limit and 2 percent threshold). If the pilot uses the special CONUS rates for the transportation industry to calculate his or her deduction for any CONUS trips in 2015, he or she must use the special CONUS M&IE rate for all CONUS trips in 2015.

In this example, if the airline had ex-

cluded the pilot's \$48 per diem payment from his or her income, rather than including it as a taxable per diem allowance, he or she would be entitled to take an itemized M&IE deduction of \$46.50 (\$94.50 minus \$48) without substantiation, using the special transportation industry M&IE rates (subject to the 80 percent limit and 2 percent threshold).

When a pilot uses the special transportation industry M&IE rates, the deduction may be somewhat less than if the standard M&IE rates are used, especially if the pilot usually travels to higher-cost destinations.



WHAT IF A PILOT REGULARLY TRAVELS OUTSIDE THE U.S.?

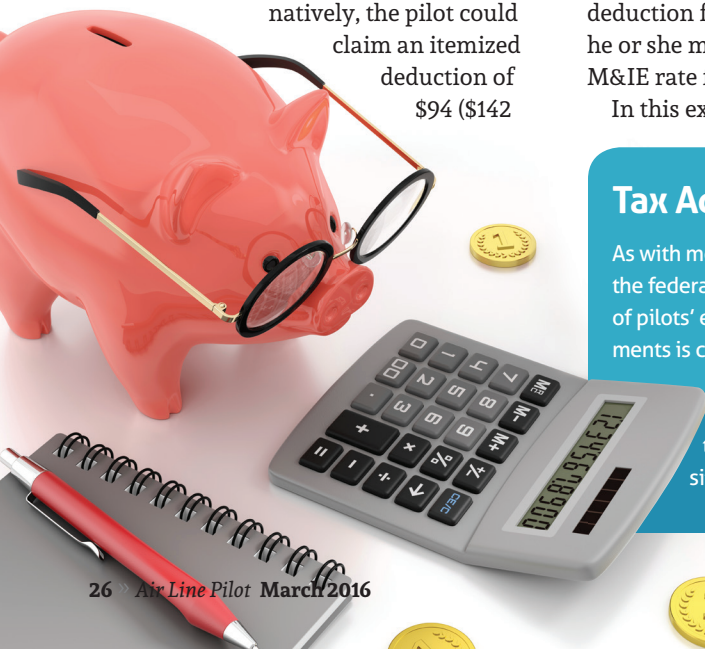
If a pilot generally travels to high-cost areas of the world

away from home on business outside the U.S., he or she may be entitled to a larger deduction using the M&IE rates for the specific location of travel. Assume, for example, that the airline pays per diem at the rate of \$68 per day for an overseas trip that is excluded for income tax purposes. If the pilot uses the special transportation industry M&IE rate to calculate the itemized deductions for OCONUS for 2015, he or she won't be entitled to any itemized deduction since the special transportation industry M&IE rate for OCONUS is \$68 per day. However, by using the standard M&IE rates for all OCONUS travel that year, this pilot may be able to claim an itemized deduction for tax purposes.

Assume the pilot travels to Narita, Japan; the standard OCONUS M&IE rate for Narita is \$84 per day. Using the standard OCONUS M&IE rates, the pilot generally would be able to claim an itemized deduction of \$16 (\$84 minus \$68) for each full day of a trip to Narita, without substantiation (subject to the 80 percent limit and the 2 percent threshold). ☒

Tax Advice

As with most matters concerning taxes, the federal law governing the taxation of pilots' expenses and per diem payments is complex. All pilots are urged to obtain competent tax advice about applying the information in this article to their own situation.



Note: The examples in this article are for illustrative purposes only.