

5. Recordkeeping

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If you deduct travel, entertainment, gift, or transportation expenses, you must be able to prove (substantiate) certain elements of expense. This chapter discusses the records you need to keep to prove these expenses.



If you keep timely and accurate records, you will have support to show the IRS if your tax return is ever examined. You will also 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 <u>Reimbursements</u>.

How To Prove Expenses

<u>Table 5-1</u> is a summary of records you need to prove each expense discussed in this publication. You must be able to prove the elements listed across the top portion 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.

You should keep adequate records to prove your expenses or have sufficient evidence that will support your own statement. You must generally prepare a written record for it to be considered adequate. This is because written evidence is more reliable than oral evidence alone. However, if you prepare a record on a computer, it is considered an adequate record.

What Are Adequate Records?

You should keep the proof you need in an account book, diary, log, statement of expense, trip sheets, or similar record. You should also keep documentary evidence that, together with your record, will support each element of an expense.

Documentary evidence. You generally must have documentary evidence, such as receipts, canceled checks, or bills, to support your expenses.

Exception. Documentary evidence is not needed if any of the following conditions apply.

- 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. (<u>Accountable plans</u> and <u>per diem allowances</u> are discussed in chapter 6.)
- Your expense, other than lodging, is less than \$75.
- · You have a transportation expense for which a receipt is not readily available.

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 all of the following information.

- The name and location of the hotel.
- · The dates you stayed there.
- 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 all of the following information.

- The name and location of the restaurant.
- · The number of people served.
- · 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.

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.

http://www.irs.gov/publications/p463/ch05.html

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Timely-kept records. You should record the elements of an expense or of a business use at or near the time of the expense or use and support it with sufficient documentary evidence. A timely-kept record has more value than a statement prepared later when generally there is a lack of accurate recall.

You do not need to write down the elements of every expense on the day of the expense. If you maintain a log on a weekly basis that accounts for use during the week, the log is considered a timely-kept record.

If you give your employer, client, or customer an expense account statement, it can also be considered a timely-kept record. This is true if you copy it from your account book, diary, log, statement of expense, trip sheets, or similar record.

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.

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.

What If I Have Incomplete Records?

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

- · Your own written or oral statement containing specific information about the element, and
- · 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, the supporting evidence must be either direct evidence or documentary evidence. Direct evidence can be written statements or the oral testimony of your guests or other witnesses setting forth detailed information about the element. Documentary evidence can be receipts, paid bills, or similar evidence.

If the element is either the business relationship of your guests or the business purpose of the amount spent, the supporting evidence can be circumstantial rather than direct. For example, the nature of your work, such as making deliveries, provides circumstantial evidence of

Table 5-1. 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 Business Relationship							
Travel	lodging, and meals. Incidental expenses may be totaled in reasonable categories	Dates you left and returned for each trip and number of days spent on business.	(name of city, town, or other	Purpose: Business purpose for the expense or the business benefit gained or expected to be gained. <u>Relationship</u> : N/A							
Entertainment	expenses such as taxis, telephones, etc.,	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</i> <i>Purpose</i> .)	Purpose: 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.								
Transportation	expenses, the cost of the car and any improvements, the date you started using it for business, the mileage for each business.	Date of the expense. For car expenses, the date of the use of the car.	Your business destination.	<u>Purpose:</u> Business purpose for the expense. <u>Relationship:</u> N/A							

the use of your car for business purposes. Invoices of deliveries establish when you used the car for business.

Sampling. You can keep an adequate record for parts of a tax year and use that record to prove 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 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 your family use the car for personal purposes. You keep 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. You can satisfy the substantiation requirements with other evidence 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.

- You were unable to obtain evidence for an element of the expense or use that completely satisfies the requirements explained earlier under <u>What Are Adequate Records</u>.
- You are unable to obtain evidence for an element that completely satisfies the two rules listed earlier under <u>What If I Have Incomplete Records</u>.
- · You have presented other evidence for the element that is the best proof possible under the circumstances.

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Destroyed records. If you cannot produce a receipt because of reasons beyond your control, you can prove a deduction by reconstructing your records or expenses. Reasons beyond your control include fire, flood, and other casualty.

Separating and Combining Expenses

This section explains when expenses must be kept separate and when expenses can be combined.

Separating expenses. Each separate payment is generally 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 buy 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 nonluxury box seat tickets if you rent a skybox or other private luxury box for more than one event. See <u>Entertainment tickets</u> in chapter 2.

Combining items. You can make one daily entry in your record for reasonable categories of expenses. Examples are taxi fares, telephone calls, or other incidental travel costs. Meals should be in a separate category. You can include tips for meal-related services with the costs of the meals.

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, with a single record. Minimal personal use, such as a stop for lunch on the way between two business stops, is not an interruption of business use.

Example.

You make deliveries at several different locations on a route that begins and ends at your employer's business premises and that includes a stop at the business premises between two deliveries. You can account for these using a single record of miles driven.

Gift expenses. You do not always have to record the name of each recipient of a 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 each of many customers, it is usually enough to record a general description of the recipients.

Allocating total cost. If you can prove the total cost of travel or entertainment but you cannot prove how much it cost for each person who participated in the event, you may have to allocate the total cost among you and your guests on a pro rata basis. To do so, you must establish the number of persons who participated in the event.

An allocation would be needed, for example, if you did not have a business relationship with all of your guests. See <u>Allocating between business and nonbusiness</u> in chapter 2.

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 records as long as they may be needed for the administration of any provision of the Internal Revenue Code. Generally, this means you must keep records that support your deduction (or an item of income) 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. For a more complete explanation of how long to keep records, see Publication 583, Starting a Business and Keeping Records.

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 copies of this information. However, you may have to prove your expenses if any of the following conditions apply.

- · You claim deductions for expenses that are more than reimbursements.
- Your expenses are reimbursed under a nonaccountable plan.
- · Your employer does not use adequate accounting procedures to verify expense accounts.
- · You are related to your employer as defined under PerDiem and Car Allowances, in chapter 6.

Reimbursements, adequate accounting, and nonaccountable plans are discussed in chapter 6.

Examples of Records

Tables 5-2 and 5-3 are examples of worksheets which can be used for tracking business expenses

Table 5-2. Daily Business Mileage and Expense Log Name:

			Odometer Readings			Expenses			
Date	Destination (City, Town, or Area)	Business Purpose	Start	Stop	Miles this trip	Type (Gas, oil, tolls, etc.)	Amount		
	Weekly Total								
Total Year-to-Date									

THIS IS NOT AN OFFICIAL INTERNAL REVENUE FORM

Table 5-3. Weekly Traveling Expense and Entertainment Record																	
From:To:Name:																	
Expenses		Sur	nday	Mo	Monday		sday	Wedn	esday	Thu	rsday	Frie	day	Satu	ırday	Total	
1.Travel Expenses:									ı.							,	
Airlines Excess Baggage																	
Bus – Train																	
Cab and Limousine												-					_
Tips																	_
Porter												<u> </u>					_
2. Meals and Lodging:																	_
Breakfast																	
Lunch																	
Dinner																	
Hotel and Motel																	
(Detail in Schedule B)																	
3. Entertainment (Detail in Schedule C)																	
4.Other Expenses:																	
Postage																	
Telephone & Telegraph																	
Stationery & Printing																	
Stenographer																	
Sample Room																	
Advertising																	
Assistant(s)																	
Trade Shows			I.,	Ι			I <u>.</u>	L .			Ļ						
5.Car Expenses: (List all car of (Detail mileage in Schedule A.	expenses - the .)	divisio	n betwe	en busi	ness an	d person	al expen	ses may be n	hade at the er	nd of the ye	ar.)						
Gas, oil, lube, wash																	
Repairs, parts																	
Tires, supplies																	
Parking fees, tolls																	
6.Other (Identify)																	
Total																	
Note: Attach receipted bills for	r (1) ALL lodgir	ng and	(2) any	other ex	penses	of \$75.0	0 or mor	e.									
Schedule A – Car								1									
Mileage: End																	
Start																	
Total Business Mileage																	
Schedule B – Lodging																	_
	Name											1					
Hotel or Motel	City																_
Schedule C – Entertainment																	-
Date Item Place Amoun				ount	Business Purpose Business Relationsh							ationship					
	•					WEEKL	Y REIM	BURSEMEN	rs:			•					
									ansportation	expenses							
								Other reimbu	irsements								
								TOTAL									
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