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LEGAL ALERT

PER DIEM:

UNDERSTANDING THE TAX TREATMENT OF TRAVEL ALLOWANCES AND REIMBURSEMENTS

What is it?

Per diem is a Latin phrase meaning “per day” that describes a fixed daily allowance given to employees to cover expenses incurred while travelling for work, or a daily pay rate for temporary workers.

A per diem is intended to cover one or more of the following:

1. Accommodation
2. Meals and refreshments
3. Incidental expenses such as minor personal expenses
4. Transport and movements

By this definition, instead of an employer requiring an employee to pay for every expense and later submit receipts for reimbursement, an employer may give the employee a predetermined daily amount before or during each trip.

Whether the employee spends slightly more or less than the per diem depends on the employer’s policy. Some employers allow employees to retain any savings on per diem, while others require accountability and repayment of any unused amounts.

What does the law say?

Section 19(1) of the Income Tax Act defines employment income as any income or benefit an employee receives from employment, whether it is paid in cash or provided in another form. Employment income includes both regular salary and other payments or benefits arising from the employment relationship.

Although the term “per diem” is commonly used in practice, the Income Tax Act does not use this term. Section 19(2)(d) instead exempts it from tax, referring to it as any allowance, reimbursement, or discharge of expenditure.

This exemption applies provided that the per diem or reimbursement does not exceed the cost actually incurred, or likely to be incurred, for accommodation, travel, meals, or refreshments while the employee is travelling in the course of performing employment duties.

Therefore, per diem is not subject to PAYE provided that it:

1. is paid for official business travel;
2. is intended to cover travel expenses; and
3. does not exceed the actual or reasonably expected cost of those expenses.

Instead of paying a per diem upfront, an employer may also reimburse an employee after the employee has incurred the expenditure while on travel. For example, an employee pays for a hotel during an official business trip and submits receipts to the employer. If the employer reimburses those actual costs, the reimbursement is not treated as taxable employment income.

When can a per diem be taxable?

A per diem may be treated as taxable employment income if, in substance, it amounts to additional remuneration for employment duties performed rather than compensation for business travel expenses.

Examples of this include:

1. paying a daily allowance even when the employee is not travelling for work;
2. paying amounts that are significantly higher than the expected travel costs without justification;
3. paying the "per diem" regularly and consistently, such that it effectively becomes a monthly supplement to an employee's salary.

In these situations, the payment may no longer fall within the exemption in Section 19(2)(d), and it could be subject to PAYE.

In the case of ***Bollore Transport & Logistics LTD v Uganda Revenue Authority (Civil Appeal No 49 of 2021),*** the High Court held that the employer-provided fuel cards used in private cars by employees for travel are subject to Pay As You Earn tax if the employer fails to prove that the travel was explicitly in the course of employment. The Court further stated that the employer must prove that the employee incurred, or will incur, those expenses in the course of employment, and that the allowance does not exceed the expenses actually incurred or likely to be incurred in the course of that work. Only reimbursable work-related travel expenses fall under Section 19(2)(d)(i) of the Income Tax Act.

Safeguards against PAYE assessments

Although the Income Tax Act exempts qualifying per diem and reimbursements from tax, employers should maintain adequate documentation to demonstrate that the payments fall within the definition in Section 19(2)(d) by maintaining records of the following:

1. Travel authorisations or travel schedules;
2. Receipts and invoices where reimbursements are made;
3. Hotel bills and invoices;
4. Transport records, invoices, and fuel receipts;
5. Employee per diem requisitions;
6. Evidence showing the purpose and duration of the official travel;
7. Internal travel and per diem policies setting out how allowances are determined.

Employers should generally be able to demonstrate that the employee actually travelled on official business and that the allowances or payments related to that travel. This is because URA usually examines whether there was actual official travel rather than merely whether a payment was labelled "per diem."

Also under Uganda's tax laws, the burden rests on the taxpayer in this case the employer, to demonstrate that the tax exemption of per diem applies.

Conclusion

Section 19(2)(d) ensures that employees are not taxed on genuine work-related travel expenses. Allowances, reimbursements, or discharge of costs for accommodation, transport, meals, and refreshments are excluded from employment income where they relate to official travel and do not exceed the actual or reasonably expected cost.

Employers should therefore distinguish genuine business travel payments from fixed cash allowances that form part of an employee's remuneration, and maintain records and a clear per diem policy setting out the applicable per diem rates.

Employers may also benchmark their travel policies against the Public Service Duty Facilitating Allowances for Public Officers available online.

Where employers cannot demonstrate that payments satisfy the provisions of the Act stated above, URA may recharacterise the amounts as employment income subject to PAYE, together with interest and penalties.

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Our team combines a breadth of experience, education, and training in the best institutions in the world. We are always on the lookout for the most talented and ambitious professionals to join the team. With a mix of lawyers and accountants across the board, our service offerings are unequalled in both tax & legal assignments.

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