Making Sense of Per Diem: Here’s Everything to Know

The concept of a per diem is crucial for entrepreneurs to know and understand as they start, work and grow their businesses.

What is a per diem rate?

Per diem is a Latin phrase that translates to “per day.” In the modern sense, per diem refers to a daily allowance, standard rate or fixed amount of money an employer provides to a part-time or full-time employee or a contractor.

This covers the costs of food, lodging and other expenses while they are away, for example, mileage reimbursement.

The per diem work rate that you set can help your business understand and determine travel reimbursement rates and compensation.

For a business, you can understand per diem rates through a simple equation:

lodging + meals + incidentals = per diem pay

But how can you determine each factor of this rate? What are the benefits and challenges of per diem payments? And where should you incorporate this strategy in your own business?

How do per diem rates work?

People frequently travel for work incur various expenses, such as meals, transportation and lodging.

In this case, budgeting and frugal spending can be challenging to gauge. You want flexibility in this process, but you also want to be tax efficient. So how can you organize this?

What are per diem travel rates?

Per diem travel rates are daily allowances paid to employees for business purposes. By using per diem travel rates, employers can simplify the reimbursement process for their employees' travel expenses.

Instead of requiring employees to submit individual receipts for meals, lodging rates and other expenses, the employer can provide a fixed daily allowance based on the employee's travel destination and duration.

This travel policy reduces the administrative burden of processing individual expense reports and ensures that employees get adequately compensated for their travel expenses on business trips.

What are the criteria for using per diem allowances?

The standard per diem allowance includes lodging, meals and incidentals. However, every situation is different and you'll rarely find the same per diem for every workplace.

Fortunately, there are a couple of standard criteria used to calculate an employee's per diem allowance:

- The per diem rate varies by travel destination, making it essential in calculating the total allowance given.
- Per diem is also affected by the length of the trip: The longer the stay, the higher the allowance.
- This rate also should consider the purpose of the trip, simply a monetary calculation of utility for the trip.
- Finally, individual employer policies are standard for

per diem trips.

Any owner of their respective company should thoroughly research what standard rates are, even in their competition, to get a good idea of their individual per diem policies.

How are per diem rates set?

Per diem rates are typically set by the Internal Revenue Service (IRS) or the General Services Administration (GSA).

The IRS per diem rates determines the maximum tax-deductible amount an employee can claim for business travel expenses.

The GSA per diem rates determine the maximum reimbursement amount federal government employees can claim for business travel expenses. These rates are based on the average cost of lodging, meals and incidental expenses in a particular location.

The U.S. General Services Administration (GSA) provides per diem rates for domestic travel in the United States and U.S. territories. In contrast, the State Department provides per diem rates for international travel. You can always check their websites to find the per diem rates for the location you will be traveling to.

It’s important to note that both rates are always subject to change and change yearly, adjusted as surveys suggest.

Related:An Entrepreneur’s Guide to Whittling Down Travel Costs

What is a per diem employee?

Per diem employees get hired as needed and are paid daily or hourly rates instead of salaries. This is typically described as seasonal staffing.

These employees can work part-time or full-time hours but are

not considered permanent employees.

They are typically hired to cover short-term staffing needs, such as filling in for a regular employee on vacation or taking a leave of absence. For example, substitute teachers and travel nurses are often paid per diem.

Per diem employees are usually paid a higher hourly or daily rate than regular employees to compensate for the lack of benefits, such as health insurance, retirement benefits or paid time off.

Depending on their job duties and performance, they may receive additional compensation, such as overtime pay or bonuses.

Per diem employees are also responsible for their taxes, and their pay is not subject to payroll withholding.

What are the benefits of hiring per diem employees?

While having a fixed allowance for employees can seem like a risky task, especially when it is easy to overcompensate, you can use this tool with the proper research.

Streamlining and securing the accounting process

Because of the fixed allowance, there is no need to keep a record of money spent or what it was on. This is all eliminated by having a set amount of money to be spent by the employee.

Per diem can even help with budgeting and financial planning by providing a predictable and consistent way of managing business travel expenses.

Employers can set a per diem rate that is appropriate for the location and duration of the trip. This can help them estimate the cost of business travel and incorporate it into their overall budgeting process.

Less paperwork

Per diem also simplifies the reimbursement process for employees and reduces the amount of paperwork and documentation required by the accounting department.

Additionally, it reduces the risk of errors and fraud in the reimbursement process since there is less opportunity for employees to submit false or inflated expense reports.

Related: How Per Diem Payments Can Simplify Your Accounting and Taxes

Per diem payments are not taxed as wages

The good news for the employee is that the reward is tax-free as long as the per diem rate is within the IRS limit.

While the federal government does include limits, this is good news for both parties. Employees do not need to report the per diem payments as income on their tax returns and do not have to pay taxes on their payments.

Employees aren’t the only ones to benefit from the tax-free side. Per diem payments are tax deductible as a business expense, which can reduce their taxable income and save them money on taxes.

What are the downsides of hiring per diem employees?

While there are benefits to hiring per diem employees, there are also some potential downsides to consider

Per diem workers can reject shifts

Per diem employees may not be as invested in the company or its goals as full-time employees. They may be less likely to go above and beyond or attend to their job duties.

This also can create tension with low effort per diem employees working with employees paid by the hour and with tips.

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Per diem rates are often higher than standard wages

While per diem employees may be paid a higher hourly or daily rate than full-time employees, the total cost of hiring per diem employees can be higher due to additional costs such as recruiting, training and supervision.

What’s the difference between per diem rates and per diem employees?

Per diem employees are temporary or part-time employees hired on an as-needed basis. Employees are not per diem employees simply because they are given a per diem rate once.

In contrast, the per diem rate is the rate employees get paid for particular trips or activities.

How can you implement per diem in your business?

Per diem always works differently in each situation. Create a per diem policy that outlines the rules and guidelines for per diem payments specific to your company.

Test what works and what doesn’t. This policy should include the maximum per diem rates, the types of expenses covered by per diem and the conditions under which per diem will be paid.

Once the per diem policy is created, you should communicate it to all levels of staffing, especially employees who travel for business. You should communicate with management and discuss the idea of per diem with the administration of your company.

You should also explain the policy in detail, including how per diem rates are calculated and the types of expenses covered. You should also train employees on how to use the per diem system. This training should cover calculating per diem rates, submitting per diem expenses and using the online system.

Related: How Investing in Employee Training Benefits Your Business

Once per diem is introduced, it is vital to monitor the system to ensure it works effectively. This will help you to identify any issues or areas for improvement. Don’t shy away from growth and don’t be afraid of failure, for it is through failure that you learn.

Check out Entrepreneur’s other articles for more information about per diem payments, employees and other financial topics.

https://www.entrepreneur.com/growing-a-business/making-sense-of-per-diem-heres-everything-to-know/449036