



Deductibility of Meals & Entertainment Expenses under the Tax Cuts and Jobs Act

The Tax Cuts and Jobs Act (“TCJA”) of December 2017 makes several significant changes to the deduction for meals and entertainment related to a taxpayer’s business. These changes will affect almost all taxpayers and may necessitate changes to accounting systems or reimbursement policies to ensure compliance with the new rules. The following discussion reviews the changes under the TCJA and which expenses remain 100% deductible, 50% deductible or not deductible at all.

Entertainment Expenses

Under pre-TCJA law, entertainment expenses were 50% deductible if directly related or associated with the active conduct of the taxpayer’s trade or business. Generally, to meet this requirement, an activity was required to generate an expected business benefit or include substantial business discussions before or after the activity. Entertainment expenses are those for any activity of the type generally considered to constitute entertainment, amusement or recreation. Examples of these activities include sporting events, entertaining at night clubs, fishing, hunting and golf outings.

Effective January 1, 2018, no deduction is allowed for entertainment expenses, even if directly related or associated with a taxpayer’s business. There are certain exceptions for business meals and other exempted activities (see below).

Example: A partner at a law firm takes a client to a sporting event and discusses current and prospective projects before and after the event. The cost of the tickets is no longer deductible effective January 1, 2018.

Directly-Related Business Meals

Similar to entertainment expenses, expenditures for meals (that is, food and beverages) directly related or associated with a taxpayer’s trade or business were 50% deductible under pre-TCJA law. To be eligible for 50% deductibility, a meal expenditure could not be lavish or extravagant, and either the taxpayer or an agent was required to be present at the meal. Additionally, meal costs for a taxpayer or the taxpayer’s employees while traveling away from home were also 50% deductible as business meals.

These provisions were not changed by the new tax law, so the 50% deduction for business meals (including meals incurred while traveling) remains in place.

Example: A business owner meets with a current client at a restaurant. During the meal, they discuss the health of each other and their families, recent developments affecting the client’s industry and current and expected future projects for the client. The meal consists of food and

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beverages that are not lavish or extravagant. The taxpayer is still entitled to deduct 50% of the cost of the meals.

However, it is not clear which meals will constitute “entertainment” and thus be disallowed under the TCJA. Additional IRS guidance has been requested as to how the new rules will be applied when meal expenditures are incurred in connection with entertainment activities. Some commentators have suggested that the cost of a meal will only be deductible if it is separately stated from the cost of the entertainment activity.

Example: A partner at a law firm takes a client to a sporting event and discusses current and prospective projects before and after the event. During the event, they leave their seats to purchase a meal at a restaurant inside the stadium. The AICPA has recommended that the IRS provide guidance stating that the cost of the business meal is deductible, subject to the 50% limit, provided it is separately stated from the cost of the tickets. While further guidance is needed, it is recommended that businesses begin to capture this information to be in a position to deduct the meal expenses should the IRS rule favorably on this issue.

Employee Meals on Company Premises

Prior to 2018, taxpayers with employer-operated eating facilities (such as a company cafeteria) could deduct 100% of any costs associated with the operation of that facility, provided that the facility was located on the employer’s premises and met several other requirements. Additionally, food and beverages provided to employees on company premises that qualified as de minimis fringe benefits were also 100% deductible. To qualify as de minimis fringe benefits, the food and beverages were required to be provided for the convenience of the employer (i.e. to allow employees to work overtime or avoid disruptions in work flow), or to be so minimal in value that accounting for them would be impractical.

Under the new tax law, expenditures for employer-operated eating facilities, and food and beverages that previously qualified as de minimis fringe benefits, will be subject to the 50% limitation imposed on all business meals for tax years 2018 – 2025. After 2025, if no additional legislation is enacted, no deduction will be allowed for these expenses.

Example: A bank provides lunch to its employees on company premises since the bank’s peak business occurs during lunch hours. Beginning in 2018 the cost of the meals will be 50% deductible, and after 2025 no deduction will be allowed.

Example: A restaurant provides meals to its employees, served on its business premises, at no cost or at a discount. Beginning January 1 of this year the costs will be only 50% deductible, and will not be deductible after December 31, 2025. The AICPA has recommended that, for administrative convenience and ease of compliance, the IRS provide a safe harbor method for an employer to calculate the nondeductible portion of the cost of the food and beverages.



Example: A company provides pantry items such as coffee, soft drinks, water, snacks, etc. in a break room. Beginning in 2018 these expenses are only 50% deductible.

Exempted Expenses

While the TCJA imposes new limitations and reduces the deductibility of several categories of meal and entertainment expenses, certain expenses remain deductible at the same level as under pre-TCJA law.

- **Recreational expenses:** expenses by a taxpayer for recreational, social, or similar activities that are open to all employees and do not discriminate in favor of highly compensated employees, such as happy hours or office holiday parties, picnics, or summer outings, are still eligible for 100% deductibility.
- **Available to general public:** expenditures for goods and services made available to the general public, such as coffee and doughnuts available to customers in a waiting area, remain 100% deductible.
- **Entertainment sold to customers:** if the taxpayer receives full consideration in a bona fide transaction for entertainment provided to customers, the cost of producing that entertainment (such as salaries for employees at a night club and amounts paid to performers) is 100% deductible.
- **Expenses includible in income of non-employees:** if the value of meals or entertainment provided to an independent contractor is reported on a Form 1099, the taxpayer can take a 100% deduction for the amount paid.
- **Meetings of employees or stockholders:** the cost of meals and entertainment provided at a meeting of employees or stockholders where the principal purpose of the meeting is for a business discussion, such as refreshments at a meeting where employees are instructed on a new procedure, or a shareholders' meeting to elect directors and discuss corporate affairs, remains 50% deductible.
- **Meetings of business leagues:** expenditures for attending meetings or conventions of any business league, real estate board or chamber of commerce are eligible for 50% deductibility.

As under prior law, taxpayers must retain records regarding the time, place, amount, and business purpose of meal and entertainment expenses to properly substantiate any deductions taken.

As with all of the TCJA amendments to the tax law, taxpayers should analyze how the changes to the meals and entertainment deduction will affect them and determine any steps that should be taken to comply with the new requirements. Tax planning opportunities may also exist with regard to employee and client meal expenditures to ensure that they are eligible for the maximum deductibility under the new rules. If you have questions about these changes and how they might affect your business, please contact your Bennett Thrasher tax advisor by calling 770.396.2200.