NEW RULES
for Meals and Entertainment

Tax Reform Changes Every Business Owner Needs to Know

Executive Summary:

Effective January 1, 2018, following passage of the Tax Cuts and Jobs Act of 2017 (TCJA), the tax deductions for meals and entertainment (M&E) generally fall into these three categories (the 100-50-0 rules):

- 100% deductible – these did not change:
    - M&E for recreational and social purposes primarily for employees' benefit
    - M&E included in employees' or others' taxable compensation (Form W-2 or 1099)
    - M&E sold to or reimbursed by customers and clients
    - food and beverages made available to the general public, such as presentations
- 50% deductible –
    - meals provided to current and potential clients and customers, consultants or similar business contacts where business is conducted and the taxpayer or employee is present
    - employees' in-office meals, drinks, snacks, and dining facilities for convenience of employers (formerly 100% deductible)
    - employee meals while traveling and attending meetings outside the office on business
    - M&E incurred during business meetings among employees, officers, directors and stockholders
- 0% deductible –
    - entertainment for clients, customers and prospects, including travel and parking (formerly 50% deductible)
    - meals when combined with non-deductible entertainment and not itemized on the bill (formerly 50% deductible)
    - dues and usage fees for clubs organized for social, recreational or sports purposes (usage formerly 50% deductible)
    - meals with employees, current and potential clients and customers, consultants or similar business contacts where NO business is conducted

Background – the rules through 2017:

For many years, business meals and entertainment were 50% tax deductible as long as business was conducted. Furthermore, meals provided to employees in the office were 100% deductible. Across the board, all meals and entertainment had to pass the IRS tests of being ordinary and necessary but not lavish or extravagant, and requiring the presence of the taxpayer or an employee of the taxpayer.

New rules starting in 2018:

In summary, as of January 1, 2018, the new rules retain deductibility of business meals at 50% but reduce the deductibility of most employee meals from 100% to 50%, and no longer allow a deduction for customer-based entertainment expenses. These new rules have necessitated further separation of meals and entertainment in your accounting records. At a minimum, I recommend using the 100/50/0 categories shown above. The IRS plans to issue proposed regulations to further define meals and entertainment, which are expected to be effective later in 2019.

Business meals:

Half of the cost of business meals with customers, consultants or prospects is deductible provided the taxpayer claiming the deduction, or an employee of the taxpayer, is present. When entertainment is also provided, the cost of food and beverages must be shown separately on the invoice or other document or it will be lumped with entertainment and disallowed. The IRS refers to sporting events in its examples whereby the cost of game tickets are not deductible, including club box rentals. If food and beverages are bought, the cost must be clearly marked on the tickets or invoice, or purchased separately. If these requirements aren't met, meals are disallowed.

- Documentation rules have not changed. Here is what you need to show if audited by the IRS:
- Brief description of business discussed.
- Name of the vendor or restaurant providing the food and/or beverages.
- Name of the person(s) you provided the meal to, and the employee present.
- Copy of the receipt if the cost is $75 or greater showing amount, time and date.

Employee meals:

The tax deduction for food and beverages provided by a company to its employees reduced from 100% to 50%. Typically, this covers snacks and drinks stocked in the company kitchen or meals brought in for employees for the employer's convenience. The 50% rule extends to the operation of a company eating facility, as well as meals served at meetings of employees, stockholder and directors. For meal costs added to an employee's taxable income or reimbursed by a customer, the deduction is still 100%.

An exception still exists for food and beverages served as part of recreational, social or similar expenses for employees. These costs are still 100% deductible, and are intended to include events primarily for the benefit of employees, such as holiday parties, picnics, outings, and similar events.

Entertainment:

Business-related entertainment expenses are no longer deductible. Some narrow exceptions remain, such as the cost of entertainment billed to customers, and entertainment connected with your business (e.g., the cost of movie tickets to a film critic). Entertainment included with recreational activities to benefit employees are still 100% deductible along with the meals.

The official definition of entertainment in the tax rules includes:

- Activity or facility that constitutes entertainment, amusement or recreation.
- Those that meet an individual's personal, living, or family needs.

Amusement or recreation includes entertaining at night clubs, cocktail lounges, theaters, country clubs, golf and athletic clubs, sporting events, and on hunting, fishing, or vacation trips. Personal needs relate to paying for a customer's hotel, vehicle or food as a courtesy.

While dues paid for social, athletic or sporting clubs (typically 501(c)(7) organizations) have been non-deductible for years, now the cost of activities associated with these clubs is also non-deductible. Dues and event fees paid to 501(c)(6) business organizations, such as trade associations and chambers of commerce, are still deductible, subject to the lobbying expense restrictions. Finally, the new tax law made charitable golf outing costs non-deductible, except for sponsorship fees and a charitable contribution for the profit made by the charity.

In summary, meals and entertainment expenses were curtailed in some areas but not others. It is very important to understand how these expenses differ within the three categories of 100% deductible, 50% deductible, and non-deductible, and adjust the accounting for these expenses accordingly.

Finally, be sure to keep adequate documentation, and look for more M&E changes by the IRS in the near future. ■

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