

IRS Says Business Meal Deductions Still Apply

The Tax Cuts and Jobs Act (TCJA) of 2017 generally disallowed all deductions for business entertainment, amusement, and recreation (see the May 2018 Sapient CPA Client Bulletin). However, the TCJA did not specifically turn thumbs up or down on the deductibility of business meal expenses.

Example: Jim Morgan, who owns a roof cleaning business, takes a prospect to lunch and pays the \$60 bill. Under the old law, Jim could take a \$30 (50%) tax deduction.

Is this still the case? In Notice 2018-76, issued in the second half of last year, the IRS clarified that such business meals generally remain 50% tax deductible. Proposed regulations will be published in the future, but business owners can rely on Notice 2018-76 in the interim.

Essentially, this notice confirms that anything that might be considered entertainment won't be a deductible expense. The IRS's list includes night clubs, theaters, country clubs, sports events, and so on. Regular business meals, on the other hand, may still qualify for the 50% deduction.

Five Points

Drilling down, the IRS listed five tests that must be passed in order to support the deduction:

1. The expense must be an ordinary and necessary expense, paid or incurred in carrying on a trade or business.
2. The meal can't be considered lavish or extravagant, considering the business context.
3. The taxpayer (or an employee) must be present.
4. The other party must be a current or potential business customer, client, consultant, or similar business contact.
5. In the case of food and beverages provided during or at an entertainment activity, the food and beverages must be purchased separately from the entertainment, or the cost of the food and beverages must be stated separately from the cost of the entertainment on one or more bills, invoices, or receipts and must be priced reasonably.

Client Bulletin

Example: Carol Clark takes a client to a baseball game, where Carol buys hot dogs and drinks for herself and the client. The cost of the game tickets is not deductible. Carol can deduct 50% of the cost of the food and beverages as long as she can show that these outlays were separate from the ticket cost.

Note that the IRS uses the expression “food and beverages” in this notice. This may imply that the cost of taking a business contact out for coffee or alcoholic drinks may be 50% deductible, even if no meal was served.

It’s also worth noting that activities generally perceived to be entertainment may be deductible business expenses — if you’re in an appropriate business. The IRS gives examples of a professional theater critic attending a play and a garment manufacturer conducting a fashion show for retailers. Our office can let you know if some type of entertainment could be considered deductible advertising or public relations for your company.