

TAX PLANNING LETTER

JULY 2018, #362

Determining Which Meal and Entertainment Expenses Remain Deductible under TCJA (Part 2)

The Tax Cuts and Jobs Act (TCJA) ushered in significant changes to familiar business expenses . . . expenditures for meals and entertainment. This Tax Planning Letter, as well as Part 1 (#356), seeks to demonstrate that, while the deductibility of many entertainment expenses have been terminated after 2017, some do remain. A number of meal expenses also evade the clampdown. Part 2 covers:

- the rules for the deduction of employer-provided employee meals on company premises, and
- genres of expenses exempt from statutory restrictions on meals and entertainment

See Part 1 (#356) for an overview of TCJA changes and a discussion of whether a so-called "business meal" (one in which a substantial and bona fide business discussion is present during the event) continues to be deductible under TCJA.

EMPLOYER-PROVIDED EMPLOYEE MEALS ON COMPANY PREMISES

PRE-TCJA

Expenses for food and beverages (in addition to the facilities used to serve them) provided on company premises which are primarily for employees were exempt from the rule which limited entertainment-type expenses to those which were "directly related to" or "associated with" a trade or business. Moreover, meals evaded the 50% deduction limit to the extent that they were excludable from the employee's income as a *de minimis* fringe benefit. Nonetheless, such meals were subject to additional restrictions on business meals.

Generally speaking, meals are excludable from the recipient's income as a *de minimis* fringe in situations in which:

- Dinner (or funds given to employees to purchase dinner) is an occasional happenstance facilitating employee's ability to work overtime.
- An eating facility (operated by the employer) is located on or near the employer's business premises, the revenue of which ordinarily equals, or is in excess of, its direct operating costs.

From the employee's perspective, an employee is not required to include in gross income the value of meals furnished to such employee for the convenience of the employer at the place of business, nor for meals furnished to such employee's spouse or dependent children. The employee that is entitled to this exclusion is treated as though they had paid an amount for the meal equal to the facility's direct operating costs attributable to the meal. It is this treatment that makes the meals excludable as a *de minimis* fringe benefit. Hence, under pre-TCJA law, employers had been allowed to fully deduct the cost of business meals (that were excludable from the employees' taxable income) due to the fact that they were (1) provided at an employer-operated eating facility, (2) for the convenience of the employer.

UNDER TCJA

Employee meals on company premises, defined as under pre-TCJA law (above), are subject to two sets of rules:

After 2017 and before 2026

These meals are exempt from the general (100%) disallowance of deductions for entertainment, as well as for entertainment associated facilities. Nonetheless, since the exemption for *de minimis* fringe benefits was repealed by TCJA, these meals are not exempt from the 50% limit on deductions for meals.)

TABLE OF CONTENTS

Employer-provided employee meals on company premises	1
Other exempted expenses	2
Questions?	3

After 2025

No deduction will be allowed for:

- any expense for the operation of an employer-operated eating facility,
- any expense for food or beverages, including those associated with an employer-operated eating facility, or
- any expense for meals furnished to employees for the convenience of the employer

OTHER EXEMPTED EXPENSES

A few expenses were exempt from key pre-TCJA entertainment-related restrictions and continue to enjoy their exempt status under TCJA.

These restrictions are:

- the former rule limiting entertainment-type expenses to those which are "directly related to" or "associated with" a trade or business, and
- the current rule disallowing deductions for entertainment, amusement or recreation

plus:

- the former rule placing a 50% deduction limit on meals and entertainment, and
- the current rule placing a 50% deduction limit on meals.

Moreover, the expenditures exempt from the foregoing restrictions also are exempt from the following additional restrictions on business meals which are unchanged by the TCJA:

- can't be lavish or extravagant
- taxpayer or taxpayer's agent must be present

These exempted expenses are:

Recreational, etc., expenses for employees

Expenses incurred by the taxpayer for a "recreational, social, or similar activity" primarily for the benefit of the company's employees (such as a holiday party or summer barbeque). Also applicable to this rule are expenditures for facility rental (e.g. sports field, concert/theater venue, lanes at a bowling alley, or regional park group picnic area) in conjunction with a "recreational, social or similar activity". Nonetheless, the primary purpose of such "recreational, social, or similar activity" expenditures must be for the benefit of employees other than "highly compensated employees" as defined. Among the categories included in "highly compensated employee" is "5% owner." With regards to this provision, an individual owning a <10% interest in the taxpayer's trade or business:

- is not considered a shareholder or other owner, and
- an individual's ownership interest is considered as inclusive of any interest owned by a member of such individual's family.

Items made available to the public

Expenses incurred by the taxpayer for goods, service, and facilities that are made available to the general public.

Entertainment sold to customers

Expenses incurred by the taxpayer for goods or services (including facilities usage) which the taxpayer sells in a bona fide transaction for adequate and full consideration. Hence, as an example, the cost of producing live entertainment (such as salaries paid to entertainment venue performers and associated venue employees) for sale to customers will come within this exception.

Expenses includible in income of persons who are not employees

Expenses for goods, services, or facilities provided to a person who, while they are not employed by the taxpayer, are nonetheless taxed on the value of the entertainment, amusement or recreation as the receipt of compensation for services rendered. An example of the application of this exemption might be entertainment provided to:

- a non-employee director, or
- an independent contractor of the taxpayer

Observation: For the exemption to apply, the taxpayer "payor" of the entertainment must report the item on a 1099 information return, regardless of if the value is <\$600.

Additional categories of exempted expenses

Two additional categories of expenses are exempt only from:

- the former rule limiting entertainment-type expenses to those "directly related to" or "associated with" a trade or business, and
- the current rule excluding from deductions expenditures for entertainment, amusement or recreation

These two categories of expenses are not exempt from:

- the 50% meal deduction limit in former and current §274(n), or
- the limits on business meals stating that they can't be lavish or extravagant, and the taxpayer or his or her agent must be present

which are unchanged by the TCJA.

These two categories of expenses are:

Employee, stockholder, etc., business meetings

Expenses incurred by a taxpayer which are "directly related" to business meetings of its employees, stockholders, agents, or directors (ESADs). In the case of a partnership taxpayer, a partner is considered an agent.

For the exemption to apply:

- the meeting must be convened predominantly for the discussion of business

The exemption would not apply to:

- predominantly social or non-business meetings, in which little to no possibility exists of actively conducting business, and
- meetings or other events in which the predominant purpose is the rewarding of ESADs for their services

Observation: Prior to 2018, expenses directly related to business meetings of ESADs, could have been eligible for 100% deduction under the pre-TCJA law, which exempted expenses from the 50% deduction limit if they qualified as a de minimis fringe benefit. This option is no longer available after 2017 however, as the de minimis fringe benefit exception was repealed by TCJA

Meetings of business leagues, etc.

Expenses for entertainment which is directly related to, and/or are otherwise necessary to attendance at business meetings or other events of:

- organizations described in §501(c)(6) (e.g. business leagues, chambers of commerce, and boards of trade), and
- are exempt from tax under §501(a)



Questions?

For more details on information presented in this Tax Planning Letter or other issues, please feel free to call Roger Rossmeisl, CPA direct at (714) 325-0442 or via e-mail at roger@khopatel.com.

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