

# Overview of Meals and Entertainment Expenses<sup>©</sup>

## Temporary Rules for 2021 and 2022

The Tax Cuts and Jobs Act of 2017 made major changes to the tax treatment of Entertainment and Meals that began in tax year 2018. The chart below summarizes the various categories and deductible percentage for each in a “normal” year. However, see further below for temporary 2021-2022 rule changes.

<b>Business Related Meals &amp; Entertainment As Applied to Private Practice Dentists</b>	Percentage Tax Deductible		
	100%	50%	0%
Sporting or Entertainment Events*			X
Year-end Party for Referral Sources*			X
Meals with Clients and Prospects (Patients, Referral Sources) **		X	
Business Meals with Staff, Partners, Etc. **		X	
Meals while Traveling Away from Home Overnight on Business		X	
Meals for Local Travel - Long Day Outside of Normal Commute		X	
Employee Meals Onsite for the Convenience of the Employer ***		X	
Employee Meals Required for Business Related Meeting		X	
Meals at Business/Civic Organization Meetings		X	
Food and Beverage in Office for Employees (Coffee, Snacks, etc.)		X	
Year-end Party (or Summer Outing) For Staff and Spouses	X		
Team-Building Activity with Employees	X		

\* Entertainment is non-deductible including meals; unless the meals are separately billed and paid for.

\*\* “Business” meals of this sort were accidentally made fully non-deductible by Congress when they passed this tax act. However, this was an error and the Internal Revenue Service has corrected this in a recent pronouncement.

\*\*\* Employee meals, onsite for the convenience of the employer were previously 100% deductible.

## Temporary 2021-2022 Rules

In response to the Coronavirus impact on restaurants, the IRS has allowed a 100% deduction for certain meals that would otherwise be limited to 50%. This only applies to expenses incurred between January 1, 2021 and December 31, 2022.

To get the full deduction, the meal must be purchased from a restaurant, defined as “a business that prepares and sells food or beverages to retail customers for immediate consumption, regardless of whether the food or beverages are consumed on the business’s premises.” In other words, it does not apply to pre-packaged food and drinks purchased from grocery stores, liquor stores, convenience stores, vending machines, kiosks, etc. Thus, you will need to separate out your expenses (for 2021-2022) depending on whether they meet this restaurant definition.

## Chart of Accounts: QuickBooks or Other Accounting Software

In order to properly classify your meals and entertainment deductions you will likely need to modify your chart of accounts with the changes that went into effect in 2018. You may want to add another account that will only be used for 2021 and 2022. Also, if you are not the one keeping the books, please determine how to best communicate classifications of meals or entertainment expenses with the one who does!

### Under Staff Costs:

- Staff Outings/Parties (100%)
- Staff Meals (on Premise) (50%)
- Staff Restaurant Meals (100%) – only use in 2021-2022

### Under General & Admin

- Meals on Premise (Dr.) (50%)
- Meals – Business (50%)
- Restaurant Meals (100%) – only use in 2021-2022
- Entertainment (0%)
- Travel & Parking (100%)

***Now that we know the correct tax-deductible category – we still must meet the basic tax deductibility requirements!***

### There are two overriding aspects to optimizing your Meal deductions:

- Understanding what expenditures are potentially deductible
- Understanding the mandatory documentation rules

### 50% Limitation for (most) Business Meals

In general, all otherwise deductible business meals will only be deductible to the extent of 50% of the actual cost (or 100% for 2021-2022), including tips and tax.

In order for a business meal expense to be deductible, the expenditure must either be “directly related to” and/or “associated with” the active conduct of your trade or business. Simplified, this means that an actual and meaningful business discussion is held before, during or after the meal.

A general “goodwill” lunch is not deductible unless active business has been conducted immediately before, during, or after the meal.

**Example:** *A specialist takes a group of referring dentists to dinner. No business is discussed or documented. This would not qualify under the “directly related to” or the “associated with” test.*

*This problem could be resolved easily with a short presentation by the specialist having to do with her practice. The meal then becomes “associated with” the active conduct of business.*

If a meal expense is incurred when traveling away from home **on business** overnight, it is deductible at 50% (or 100% for 2021-2022) of the cost regardless of fitting either the “directly related to” and/or “associated with” tests. This is also true when you travel locally, but far enough away from your normal commute that an additional meal is required. An example of the latter is that Dr. Dentin drove to Portland for a clinical seminar. The seminar ends at 4:00 and Dr. Dentin is driving home. Dr. Dentin’s dinner is 50% deductible (or 100% for 2021-2022) – even though he was not away overnight.

**EXCEPTIONS:** Some meal expenses are 100% deductible. The major categories or exceptions are:

1. Traditional employee recreation (holiday party, summer outing, etc.). (Categorize these expenses in a category other than meals and entertainment – e.g. “Staff Outings/Parties 100%” under staff costs).
2. Packaged food as a business gift (fruit of the month, bottle of wine, etc. – but limited to \$25 per year per person under the “gift” limitation rule) categorized under marketing/advertising/promotion.

**Tickets to Entertainment – Including Sporting, Theatre or other Events: *No longer deductible!***

### **Recordkeeping**

1. If you maintain your own books and records, you should set up separate accounts to track the different types of business meals and non-deductible entertainment as shown on Page 2 of this Resource.
2. If you are using credit cards for meals and entertainment expenses, and/or otherwise have cash disbursements that may cover a variety of expense categories, you will need to separately break out the portion of these payments relating to business meals versus entertainment and other expenditures. (Note: In QuickBooks, use a separate Credit Card register for each card used for business – this greatly simplifies matters and helps to make sure you obtain the tax deduction when you charge the expense versus when it is paid).

**DOCUMENTATION:** In order to be deductible, all business meals must have contemporaneous documentation as to the expense, the business relationship, business purpose and actual topic or topics. ***Without contemporaneous documentation your deduction will be flatly denied, and there are no Mulligans!***

**What Documentation is Required:** First, for all expenditures that exceed \$75, you must have proof of the expenditure itself in the form of a receipt. In addition, the following are generally required:

- The amount of the expense

- The time and place of the meal
- The business purpose of the expenditure
- The business relationship of the various parties who attended

As noted above, without such records, your deduction will be flatly denied – even if you can prove the expenditure, unless you have contemporaneous documentation that meets the criteria above your deduction will be denied.

- Recordkeeping Idea: Most of us will use a credit card for most if not all of our business meals. Consider documenting the items above on your receipt and then maintaining these receipts by tax year.
- Scanning: To reduce your paperwork and to avoid the problem of fading credit card slips, consider scanning your receipts by year and by date – perhaps with the vendor name included for easy correlation to your credit card bill. You can hand write the information noted above before scanning and/or if your software allows, you can type the information after scanning. You can delegate to a staff member to scan for you.
- Either way you have a well organized and retrievable set of documentation for your meal expenditures by year – which will be very handy if audited.
- Onsite meals or meals while out of town on business also need to be documented with the business purpose or occasion.

### **Club Dues and Entertainment Facilities Generally Not Deductible**

Dues for clubs organized for business, pleasure, recreation or other social purposes, are not deductible. However, actual expenses for qualified meals can be deductible in part or whole. Exceptions to this rule include civic/charitable organizations such as Kiwanis, Rotary, professional/trade organizations and societies.

**LAVISH AND EXTRAVAGANT.** In addition to the above, to be deductible, meals must be an ordinary and necessary expense of the business. To the extent that the expenditures are considered “lavish and extravagant” they will not be deductible. “Lavish and extravagant” are relative terms which are based on the facts and circumstances.

With very limited exception, entertainment facility base expenses (dues, rents, etc.) are not deductible. Examples include yachts, hunting or fishing lodges, swimming pools, tennis courts, airplanes, apartments, condos, etc. However, out of pocket expenses for “business” meals that meet the rules discussed previously can qualify for 50% deduction.

For more information or answers to your specific expenditures, please call or e-mail.