



Notice 2018-76: IRS Issues Transition Relief to Continue 50% Client Meal Deduction

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Yesterday, the IRS issued Notice 2018-76, providing favorable transitional guidance on the deductibility of expenses for meals under section 274 of the Internal Revenue Code (Code). The Tax Cuts and Jobs Act passed last year made significant changes to the already complex rules of Code section 274 to reduce the expenses which could be deductible. More expenses became subject to the complete 100% deduction disallowance for entertainment, amusement, and recreation (collectively referred to as “entertainment”), and also more expenses became subject to the 50% deduction disallowance. In the absence of guidance, taxpayers have been challenged when determining whether meals (any food or beverage) are subject to the harsher 100% disallowance applicable to “entertainment,” rather than just the 50% ongoing and expanded meals disallowance.

Pursuant to the Notice, the 50% rule applies to meals so long as:

1. The expense is an ordinary and necessary expense under Code section 162(a) paid or incurred during the taxable year in carrying on any trade or business;
2. The expense is not lavish or extravagant under the circumstances;
3. The taxpayer, or an employee of the taxpayer, is present at the furnishing of the food or beverages;
4. The food and beverages are provided to a current or potential business customer, client, consultant, or similar business contact; and
5. In the case of food and beverages provided during or at an entertainment activity, the food and beverages are purchased separately from the entertainment, or the cost of the food and beverages is stated separately from the cost of the entertainment on one or more bills, invoices, or receipts. The entertainment disallowance rule may not be circumvented through inflating the amount charged for food and beverages.

Until proposed regulations are issued, the Notice 2018-76 guidance may be relied upon to allow all meals meeting the requirements listed in the Notice to be deductible at 50%. In the interim, taxpayers can enjoy the relief from the administrative burden of deciphering which meals are entertainment.

The Notice requests comments on the definition of “entertainment,” so the proposed regulations may not be as favorable as the Notice and could provide criteria as to when the typical client or customer meal is deemed

entertainment. Taxpayers are well advised to continue to document the business purposes of meals, the presence of a taxpayer at the meal, the fact that the meal is not lavish or excessive under the circumstances, and to be careful to obtain separate bills where meals are part of a larger entertainment activity.

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