

Anchin Alert

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Is the Tax Cuts and Jobs Act (“TCJA”) Eating Law Firms Breakfasts, Lunches and Dinners?

The TCJA made significant changes to the Internal Revenue Code (“IRC”) regarding business deductions involving not just entertainment but, in many aspects, employee benefits and traditional meals as well. These changes affect law firms and their clients regardless of entity type; however, significant guidance is still needed from the IRS.

Here are the latest rules on meals and entertainment expenses and employee fringes:

- Entertainment expenses are no longer deductible. Entertainment generally is considered to include any venue which provides a distraction to a business discussion. As such, the costs of sporting events, theatre tickets and other venues such as golf outings are no longer deductible. Unfortunately, prior IRS regulations make it clear that entertainment is not marketing.
- Business meals with clients, prospects and referral sources still appear to be 50% deductible, so long as someone from the firm is present and they are not deemed to be lavish or extravagant under the circumstances. Keep in mind that substantiation requirements have not changed and will still need to be met in order to support the deduction and keep these from being re-classed as non-deductible upon IRS audit (see substantiation criteria at end).
- *So if entertainment is not deductible yet business meals are still deductible, what about food/drinks at the entertainment venue?* We believe there is a position that such food/drink expenses are still 50% deductible, so long as the substantiation requirements are met.
- Food for marketing meetings, internal meetings, coffee, etc. are now 50% deductible (previously 100% deductible), as long as there is a true business purpose.
- Meals provided for staff for lunch or, working late or cash meal allowances are no longer *deminimis* fringe benefits, but taxable fringe benefits and are includable in compensation.
- Office functions benefitting all personnel and not limited to highly compensated employees would still qualify for the 100% deduction, e.g. – office holiday parties.
- Professional association tables – table should be 100% deductible; food should be broken out separately and limited to 50%.
- Charity benefit tables should still be 100% deductible as a charitable deduction, with the food portion limited to 50%.
- Gifts to outsiders are still limited to \$25 per person, cumulatively per year. Gifts to employees will now be considered compensation. *If employee gifts are not treated as compensation, it would be fully non-deductible and, as such, there could be separate employment tax issues.*
- Transit passes are still pre-tax compensation to employees. However the commensurate amounts are now non-deductible to businesses. This notwithstanding that in New York City and other jurisdictions providing transit passes is mandated by law.
- Car service home for employees will now be considered compensation. *If car service is not treated as compensation, it would be fully non-deductible and, as such, there could be separate employment tax issues similar to gifts (there is an exception for hourly workers if, infrequent occurrence and due to safety concerns).*

Expenses that are billed to your clients, will shift the burdens and limitations to the client provided the Firm details the nature of the expenditures.

Substantiation Requirements – Firms will need to enforce the substantiation requirements or, 50% deductible meals may be re-classed upon audit as non-deductible similar to entertainment. In order to substantiate the deductibility of the expense, the contemporaneous receipt must provide for:

1. The amount;
2. Date;
3. Name, address & location of the venue;
4. Details regarding the business purpose or, benefit to be gained;
5. The identities of the persons who took part in the business discussion and their relationship to the company, i.e. – names, titles and companies.

It should be noted that Items 1 - 3 are often part of the receipt; Items 4 and 5 require additional compliance.

Finally, as mentioned above, further guidance from the IRS is still required. Current controversy surrounds the deductibility of business meals as to whether or not they fall under the non-deductible entertainment rules or, are still deductible under the Internal Revenue Code as an item separate and apart from entertainment. As such, the American Institute of Certified Public Accountants (as well as The American Bar Association) have sent formal requests to the Treasury Department to clarify the 50% deductibility issue. Considering business meals impact almost every business, we might have expected Congress to have legislated at least this one item to have been as clear as vodka?

For more information on how the new tax reform can impact your business, please contact your Anchin Relationship Partner or Steven Lando, Services Industry Tax Leader at steven.lando@anchin.com.



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