

Expenses for Business Meals Under § 274 of the Internal Revenue Code

Notice 2018-76

PURPOSE

This notice provides transitional guidance on the deductibility of expenses for certain business meals under § 274 of the Internal Revenue Code. Section 274 was amended by the Tax Cuts and Jobs Act, Pub. L. No. 115-97, § 13304, 131 Stat. 2054, 2123 (2017) (the Act). As amended by the Act, § 274 generally disallows a deduction for expenses with respect to entertainment, amusement, or recreation. However, the Act does not specifically address the deductibility of expenses for business meals.

This notice also announces that the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) intend to publish proposed regulations under § 274, which will include guidance on the deductibility of expenses for certain business meals. Until the proposed regulations are effective, taxpayers may rely on the guidance in this notice for the treatment under § 274 of expenses for certain business meals.

BACKGROUND

Section 162(a) allows a deduction for ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business. However, § 274(a)(1), as revised by the Act, generally disallows a deduction for any item with respect to an activity that is of a type generally considered to constitute entertainment, amusement, or recreation.

Section 274(k) generally provides that no deduction is allowed for the expense of any food or beverages unless (A) such expense is not lavish or extravagant under the circumstances, and (B) the taxpayer (or an employee of the taxpayer) is present at the furnishing of such food or beverages. Section 274(n)(1) generally provides that the amount allowable as a deduction for any expense for food or beverages shall not exceed 50 percent of the amount of the expense that otherwise would be allowable.

Prior to amendment by the Act, § 274(a)(1)(A) generally prohibited a deduction with respect to an activity of a type considered to constitute entertainment, amusement, or recreation (“entertainment expenses”). However, § 274(a)(1)(A) provided exceptions to that prohibition if the taxpayer established that: (1) the item was directly related to the active conduct of the taxpayer’s trade or business (the “directly related” exception), or (2) in the case of an item directly preceding or following a substantial and bona fide business discussion (including business meetings at a convention or otherwise), that the item was associated with the active conduct of the taxpayer’s trade or business (the “business discussion” exception).

Prior to amendment by the Act, § 274(n)(1) generally limited the deduction of food and beverage (meal) expenses and entertainment expenses to 50 percent of the amount that otherwise would have been allowable. Thus, under prior law, taxpayers could deduct 50 percent of meal expenses and could deduct 50 percent of entertainment expenses that met the directly related or business discussion exceptions.

The Act repealed the directly related and business discussion exceptions to the general prohibition on deducting entertainment expenses in § 274(a)(1)(A). Thus, entertainment expenses are no longer deductible. The Act also amended the 50

percent limitation in § 274(n)(1) to remove the reference to entertainment expenses. Otherwise allowable meal expenses remain deductible, subject to the 50 percent limitation in § 274(n)(1).

Section 1.274-2(b)(1)(i) of the Income Tax Regulations provides that the term “entertainment” means any activity which is of a type generally considered to constitute entertainment, amusement, or recreation, such as entertaining at night clubs, cocktail lounges, theaters, country clubs, golf and athletic clubs, sporting events, and on hunting, fishing, vacation, and similar trips, including such activity relating solely to the taxpayer or the taxpayer’s family. The term “entertainment” may include an activity, the cost of which is claimed as a business expense by the taxpayer, which satisfies the personal, living, or family needs of any individual, such as providing food and beverages, a hotel suite, or an automobile to a business customer or the customer’s family. The term “entertainment” does not include activities which, although satisfying personal, living, or family needs of an individual, are clearly not regarded as constituting entertainment, such as (a) supper money provided by an employer to an employee working overtime, (b) a hotel room maintained by an employer for lodging of employees while in business travel status, or (c) an automobile used in the active conduct of trade or business even though also used for routine personal purposes such as commuting to and from work. On the other hand, the providing of a hotel room or an automobile by an employer to an employee who is on vacation would constitute entertainment of the employee.

Section 1.274-2(b)(1)(ii) provides that an objective test shall be used to determine whether an activity is of a type generally considered to constitute

entertainment. Thus, if an activity is generally considered to be entertainment, it will constitute entertainment for purposes of § 274(a) and § 1.274-2 regardless of whether the expenditure for the activity can also be described otherwise, and even though the expenditure relates to the taxpayer alone. This objective test precludes arguments such as that “entertainment” means only entertainment of others or that an expenditure for entertainment should be characterized as an expenditure for advertising or public relations. However, in applying this test the taxpayer’s trade or business shall be considered. Thus, although attending a theatrical performance would generally be considered entertainment, it would not be considered entertainment for a professional theater critic attending in a professional capacity. Similarly, if a manufacturer of dresses conducts a fashion show to introduce its products to a group of store buyers, the show generally would not be considered to constitute entertainment. In contrast, if an appliance distributor conducts a fashion show for its retailers, the fashion show generally would be considered to constitute entertainment.

Section 274(e) enumerates nine specific exceptions to § 274(a). Expenses that are within one of the exceptions in § 274(e), which may include certain meal expenses, are not disallowed under § 274(a). However, those expenses may be subject to the 50 percent limit on deductibility under § 274(n). The Treasury Department and the IRS intend to issue separate guidance addressing the treatment under § 274(e)(1) and 274(n) of expenses for food and beverages furnished primarily to employees on the employer’s business premises.

INTERIM GUIDANCE FOR BUSINESS MEALS

The Act did not change the definition of entertainment under § 274(a)(1); therefore, the regulations under § 274(a)(1) that define entertainment continue to apply. The Act did not address the circumstances in which the provision of food and beverages might constitute entertainment. However, the legislative history of the Act clarifies that taxpayers generally may continue to deduct 50 percent of the food and beverage expenses associated with operating their trade or business. See H.R. Rep. No. 115-466, at 407 (2017) (Conf. Rep.).

The Treasury Department and the IRS intend to publish proposed regulations under § 274 clarifying when business meal expenses are nondeductible entertainment expenses and when they are 50 percent deductible expenses. Until the proposed regulations are effective, taxpayers may rely on the guidance in this notice for the treatment under § 274 of expenses for certain business meals.

Under this notice, taxpayers may deduct 50 percent of an otherwise allowable business meal expense if:

1. The expense is an ordinary and necessary expense under § 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.

EXAMPLES

For each example, assume that the food and beverage expenses are ordinary and necessary expenses under § 162(a) paid or incurred during the taxable year in carrying on a trade or business and are not lavish or extravagant under the circumstances. Also assume that the taxpayer and the business contact are not engaged in a trade or business that has any relation to the entertainment activity.

Example 1. (i) Taxpayer A invites B, a business contact, to a baseball game. A purchases tickets for A and B to attend the game. While at the game, A buys hot dogs and drinks for A and B.

(ii) The baseball game is entertainment as defined in § 1.274-2(b)(1)(i) and, thus, the cost of the game tickets is an entertainment expense and is not deductible by A. The cost of the hot dogs and drinks, which are purchased separately from the game tickets, is not an entertainment expense and is not subject to the § 274(a)(1) disallowance. Therefore, A may deduct 50 percent of the expenses associated with the hot dogs and drinks purchased at the game.

Example 2. (i) Taxpayer C invites D, a business contact, to a basketball game. C purchases tickets for C and D to attend the game in a suite, where they have access to food and beverages. The cost of the basketball game tickets, as stated on the invoice, includes the food and beverages.

(ii) The basketball game is entertainment as defined in § 1.274-2(b)(1)(i) and, thus, the cost of the game tickets is an entertainment expense and is not deductible by C. The cost of the food and beverages, which are not purchased separately from the game tickets, is not stated separately on the invoice. Thus, the cost of the food and beverages also is an entertainment expense that is subject to the § 274(a)(1) disallowance. Therefore, C may not deduct any of the expenses associated with the basketball game.

Example 3. (i) Assume the same facts as in Example 2, except that the invoice for the basketball game tickets separately states the cost of the food and beverages.

(ii) As in Example 2, the basketball game is entertainment as defined in § 1.274-2(b)(1)(i) and, thus, the cost of the game tickets, other than the cost of the food and beverages, is an entertainment expense and is not deductible by C. However, the cost of the food and beverages, which is stated separately on the invoice for the game tickets, is not an entertainment expense and is not subject to the § 274(a)(1) disallowance. Therefore, C may deduct 50 percent of the expenses associated with the food and beverages provided at the game.

REQUEST FOR COMMENTS

The Treasury Department and the IRS request comments for future guidance to further clarify the treatment of business meal expenses and entertainment expenses under § 274. In particular, comments are requested concerning the following issues:

- (1) whether and what further guidance is needed to clarify the treatment of (a) entertainment expenses under § 274(a)(1)(A) and (b) business meal expenses;
- (2) whether the definition of entertainment in § 1.274-2(b)(1)(i) should be retained and, if

so, whether and how it should be revised; (3) whether the objective test in § 1.274-2(b)(1)(ii) should be retained and, if so, whether and how it should be revised; and (4) whether and what additional examples should be addressed in guidance.

WHERE TO SEND COMMENTS

Comments must be submitted by December 2, 2018. Comments, identified by Notice 2018-76, may be sent by one of the following methods to the applicable address listed below:

- By Mail:

Internal Revenue Service
Attn: CC:PA:LPD:PR (Notice 2018-76)
Room 5203
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

- By Hand or Courier Delivery: Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to:

Courier's Desk
Internal Revenue Service
Attn: CC:PA:LPD:PR (Notice 2018-76)
1111 Constitution Avenue, NW
Washington, DC 20224

- Electronically: Submissions may be made electronically to

Notice.Comments@irsounsel.treas.gov, with "Notice 2018-76" in the subject line.

All submissions will be available for public inspection and copying in room 1621, 1111 Constitution Avenue, NW, Washington, DC, from 9 a.m. to 4 p.m.

DRAFTING INFORMATION

The principal author of this notice is Patrick M. Clinton of the Office of Associate

Chief Counsel (Income Tax & Accounting). For further information regarding this notice, contact Patrick M. Clinton at (202) 317-7005 (not a toll-free call).