

Rules Regarding the Deductibility of Meals

Meals can only be deducted as a business expense if they are directly related or associated with the active conduct of a trade or business. There must be valid business purpose to the meal for it to be a deductible expense. Once this test is established, the expense falls into two categories: 50% deductible or 100% deductible. There is an additional caveat that if a meal is considered "lavish and extravagant" under the circumstances, the extra portion attributable to extravagance is not deductible at all. Meals with employees or business partners are only deductible if there is a direct or indirect business purpose.

50% DEDUCTIBLE

- Meal expenses for business meetings of employees, stockholders, agents, and directors. Office meetings and partner meetings fall into this category. If there is no business function to the meal, it is completely non-deductible for tax purposes. (Certain meals provided on the employer's premises may be 100% deductible. See below).
- Generally, any meals during business travel. If a portion of a business trip can be considered personal and not related to the business function of the trip, then a portion of the meals expense should also be considered personal and not deductible.
- Meals at a convention, seminar, or any type of meeting even if the meals cost is not separately stated from the cost of the event. If not separately stated, it must be calculated by the taxpayer based on reasonableness or per diem rates for that location.
- Meals with people related to the business such as clients, customers and vendors provided that there is a business purpose or some benefit to the business will result.
- Meal expenses by an employee during a business trip and reimbursed to that employee are still only deductible at 50%, even though the employee was reimbursed 100% for the cost of the meals.
- Reimbursements using Per Diem rates are always only 50% deductible. However, if you are reimbursing an independent contractor, it will be added to their 1099 income and therefore will be fully deductible and should fall under the general ledger account of Contract Services instead of Meals and Entertainment.

100% DEDUCTIBLE

- Meal expenses for a company picnic or holiday party.
- Office Snacks - coffee, soft drinks, bottled water, donuts, and similar snacks or beverages provided to employees on the business premises.
- Food made available to the public for free - usually as part of a promotional campaign.
- Meals provided on the employer's premises to more than half of the employees for the convenience of the employer. Translation: if you are providing meals to the employees in order to keep them working late, working weekends, or being on call, it is for your convenience to have them at work and the meal is a means of enticement.

- If the meals expense is included as taxable compensation to the employee and included on the W2, then the expense is fully deductible to the employer.
- If a professional firm bills actual meal expenses separately when invoicing the client and is reimbursed by the client, the actual meal expenses for that engagement are fully deductible. However, if the meals expense is included in the invoice but is not separately stated at actual cost, then those meal expenses are only 50% deductible.
- Meals and food as part of a charity sporting event are fully deductible. To qualify, a charitable sporting event must be organized for the primary purpose of benefiting a 501(c)(3) organization, must contribute 100% of its net proceeds to the organization, and must use volunteers for substantially all the work performed in carrying out the event.

Remember, you must have appropriate documentation (such as a receipt) to substantiate these expenses. The IRS will disallow expenses that do not have appropriate backup documentation. It is best to set up two General Ledger accounts for Meals and Entertainment. One for the 50% deductible meals and one for the 100% deductible meals

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