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Joseph Perry: "Decisions about season tickets often have more to do with the team's performance than tax implications." (Photo by Bob Giglione)

Feds end deduction for entertaining clients

By: Claude Solnik July 16, 2018

For decades, companies have been able to deduct 50 percent of the cost of entertaining clients. Uncle Sam helped pick up the cost for that Islanders game, that golf outing and even that junket to the Bahamas.

The idea was that these were all business expenses, essentially a type of marketing. The government would pick up part of the tab as companies sought to grow their business. Let the good times roll. The government will be there to help you pay the bill.

But under new laws that include a corporate tax cut, the government isn't as generous when it comes to mixing business and pleasure: entertainment is no longer deductible.

The federal government will give you a 50 percent deduction for a business meal, but the deduction for entertainment – professional sports, golf, theater and other things – has evaporated.

That change in tax law at least in theory could change how, whether, where and when companies entertain, or at least increase the cost. In other words, companies can celebrate the tax cut. But if they take out their clients as part of that, they will only get a deduction for the meal.

The impact the tax law has on entertainment, however, may not be noticeable, at least so far. And many regulations regarding the details have yet to be finalized, clarifying some gray areas.

“I don’t have any evidence that people have changed their minds about things. But these types of things usually have an impact,” said Lance Christensen, tax practice leader at Margolin, Winer & Evens, in Garden City. “People may not go to some of these business entertainment functions or they may get fewer tickets or medium range seats instead of the front row.”

The decision to eliminate the entertainment deduction, Christensen said, came in the context of a major corporate tax cut – pumping more cash into companies.

“People do lavish things. It’s hard for them to audit. Is there really business being conducted?” Christensen said. “They needed some pay-fors. This was a negotiation between the Republicans and the Democrats. They needed things to bring the deficit down.”

Christensen said professionals such as accountants and attorneys who often entertain will see their costs rise as well as others who entertain clients.

Professional sports leagues also could take a hit. Major League Baseball’s average attendance has fallen about 1,200 people per game, although it’s unlikely that this is due to the tax changes.

“No-one gets into buying boxes for the tax deduction. That’s not where your head is when you do this,” said Timothy Speiss, partner in charge of the personal wealth advisors practice, EisnerAmper based in Manhattan with Syosset operations. “You say you have an important client or want to do something nice for your employees.”

A team’s performance, instead, may prove to be the decisive factor, more than the deduction, when companies decide whether and how often to go to games.

“I hear about Mets and Islanders tickets, but not about the Yankees,” said Joseph Perry, national leader of tax and business services for Marcum, based in Manhattan with Melville operations. “If a team is doing well, they don’t care about the disallowance. When a team doesn’t do well and you pay extra for the tickets, you decide whether you really need the tickets.”

Golf courses also could take a hit, if businesses spend less – since more goes to taxes. But companies can still eat, drink and be merry – with deductions.

“For restaurants, it’s neutral. Rather than playing golf, go to a nice restaurant. Indirectly, it could help that,” Christensen said. “Maybe you go to the baseball game, get cheaper seats, but eat at the steak house at the stadium.”

Perry said business meals have to be “ordinary and necessary” as part of any deduction. Companies could find that they are exceeding their right to take the meal deduction, if they spend excessively.

“We’re going out and I try to get your business, and we go out for a meal. If I order a $40 bottle of wine, it’s OK. If I order a $40,000 bottle of wine, is that ordinary and necessary?” Perry asked. “Some people have said that some meals are entertainment versus a meal that’s allowed. Some firms question when you cross the line between a meal and entertainment.”

Perry added that companies need to show there is a business cause and connection to any meals that they deduct.

“You always had to document your entertainment expense,” he said. “You have to document it appropriately and the purpose has to be business, the way you write it up in the intent.”

So does the end of the entertainment deduction spell the end of an era when it comes to business entertainment? Not likely.

Christensen believes firms that entertain will continue to do so, or risk losing business, a much bigger price to pay.

“You need to entertain your clients or somebody else would,” he said. “The price went up significantly. If you’re going to do it no matter what, you do it. But you might do it fewer times or with less expensive seats.”

The real impact of ending the entertainment deduction could come in the future, as firms decide whether and how to renew season tickets.

“I have heard some people say, we have our season ticket planned for this year, but at the end of this year or early next year, we’ll keep that in mind,” Christensen said. “Whether they change their plan or reduce the number of games, I don’t know. Companies may think twice. Instead of a full season, they might get a half season.”

Firms also may no longer be as eager to pick up big tabs for events held in scenic locations – without that deduction.

“Is that a seminar expense for educating clients? Is it entertainment?” Perry said of seminars held in vacation areas. “They’re changing those programs. They’re not giving them for free anymore. And they’re being more discriminating in terms of who they invite.”

Others said that the travel industry might feel a pinch from Uncle Sam’s refusal to give entertainment deductions.

“It does hurt travel, if the economy’s bad,” Perry said. “Right now the economy’s doing well and companies are doing well. What do people cut when the economy doesn’t do well? Vacations. It’s a discretionary expense. The same will happen with companies.”

Others agreed that a weak economy could make the absence of this deduction a bigger deal. But for now, most people don’t believe the deduction has had a huge impact on businesses’ efforts to entertain.

“The economy’s been going pretty well. When we go into a recession, that’s when people really start looking at budgets,” Christensen said. “It could be a secondary impact. Things are going well. But when things turn, then they may pay closer attention to these items.”