

# Entertainment expenses

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## I. General information

Entertainment expenses can either be qualified as not deductible private expenses or deductible business expenses.

The decisive factors for the deductibility are the following:

- Reason for entertainment
- Who is entertained
- Whether the entertainment is adequate
- Proof via a proper invoice

There are four steps to determine whether the entertainment expenses are deductible:

1. Step: Are the costs caused by the company?

2. Step: Is the entertainment “business-related” (e.g. entertainment of business partners) or “generally operational” (e.g. entertainment of employees)? In the first scenario the adequate entertainment expenses may be deducted by 70%.

3. Step: Are the expenses adequate? Inadequately high expenses need to be split up in an inadequate and thus non-deductible portion and an adequate portion (see step 2).

4. Step: Was the entertainment expense and the business reason properly recorded?

## II. Entertainment expenses as business expenses

The entertainment of business partners is considered business related whenever it serves the business relation or the establishment of a business relationship. This is the case for the entertainment of the following groups of persons:

- Customers or potential customers,
- Suppliers,
- Commercial agents,
- Candidates,
- Visitors of the company in course of public relations,
- Consultants.

Accompanying persons, such as secretaries or spouses, are included. The expenses related to the host and his employees or family members can be considered business related.

The entertainment of business partners in a private house or apartment can be difficult to justify. The German tax authority assumes that the private character overweighs in these instances. A possible exception could be, for instance, when a foreign business partner is not used to entertainments in a restaurant, when his health does not allow for it or when a business conversation needs to be kept secret.

Entertainments on private occasions, such as birthdays, are also critical. The tax authority generally denies the business deductibility of the related expenses, even if mostly business partners are invited.

**Note:** When entertainment expenses are incurred during business trips, the daily allowances for food may be claimed in addition to the entertainment expenses.

## III. Restriction of deduction (70%)

Entertainment expenses that are business related can only deducted at 70%. The non-deductible portion of 30% is assumed to be the saving of the anyway necessary food consumption.

**Note:** The former restriction of the input VAT deductibility of 70% does not apply anymore. The input VAT is 100% deductible even on the portion of the non-deductible entertainment expense.

## IV. Entertainment expenses based on general operational reasons

The entertainment of employees – for instance during company events or Christmas parties – is not “business-related” but “generally operationally induced”. As such, these costs are fully deductible. Also, the costs for the employees’ family members and other people that contribute to the arrangement of the event are fully deductible. The entertainment of foreign employees, e.g. of the business partner or related companies are “business related” and thus only deductible at 70%. Likewise, the entertainment of freelancers or commercial agents is only deductible at 70%, even for in-house trainings.

## IV. Definition of entertainment expenses

Entertainment expenses are mainly costs for

- Food, beverages and other products that are consumed immediately (e.g. tobacco), but also
- Additional costs, that inevitable incur in connection to the entertainment (e.g. tip, fee for coat check), but no accommodation or travel costs.

The food must be clearly in the foreground, which is not the case, for example, for visits of night clubs or dance shows. Here the food costs typically only make up a small portion of the total costs, which is why these costs usually are of private nature and thus non-deductible.

**Note:** Corporate hospitality expenses such as beverages and cookies for meetings are no business expenses and can be fully deducted.

Entertainment costs from in-house cafeterias and canteens are only deductible at 70%. For simplification reasons, an amount of EUR 15 per entertainment and per person can be used, of which EUR 4,50 are non-deductible.

**Note:** Product and goods tastings are not considered entertainment expenses. They are directly related to the sale of the product and are fully deductible as business expenses.

## VI. Adequateness

Inadequate expenses are not deductible. Whether and to which extent entertainment expenses are adequate depends on the individual circumstances, the general opinion and the respective industry environment (e.g. size of the company, revenue, profit, importance of the business relation, competition, etc.). When the entertainment expense is inadequate with regards to the type (e.g. visit of a night club) it is not deductible. When the entertainment expense is inadequate with regards to the value, the expense needs to be split up into an inadequate and an adequate portion:

- The inadequate portion is non-deductible, including the respective input VAT.
- Only the adequate portion is deductible, whereas 30% of it is non-deductible for income/corporate tax purposes. The input VAT of the adequate portion is fully deductible.

## VII. Proof and record requirements

The value of business-related entertainment expenses needs to be recorded promptly (within about 10 days, latest with the monthly bookkeeping) in writing with the following information:

- Place and day,
- Participants,
- Reason for the entertainment,
- Value of entertainment expense.

The record must be signed by the taxpayer (or its employee incurring the charge).

**Note:** To prevent discussions with the tax authority, a precise reason should be documented. A generic description such as “customer service”, “company dinner” or “information talk” is usually insufficient.

For entertainments in a restaurant a hand-written recording of the reason and the participants is sufficient. The other details need to be apparent from the invoice. The invoice needs to include the following:

- Complete name and address of the restaurant,
- Tax identification or VAT identification number of the restaurant,
- Name and address of the recipient of the service (business),
- Date of issue,
- Invoice number,
- Type, amount or scope of service,
- Remuneration with tax rate and tax amount,
- Date of the entertainment.

For small amounts up to EUR 250, the name and address of the service recipient is not strictly required. Instead, it is sufficient if the invoice includes the complete name and address of the restaurant, the date of issue, type, amount or scope of service, the gross amount and the tax rate.

In order to ensure that the entertainment expenses are deductible for income tax, the following requirements should be met:

- All meals and beverages need to be listed with their individual price (common labeling such as “menu” or “Lunch-Bufferet” is sufficient).
- In addition, all participants need to be listed with name, as well as the host and participating employees and family members. The recording of the address is not required, but might be requested by the tax authority. A professional secrecy usually does not excuse from providing the names. An exception only applies when the recording of the names is unreasonable, e.g. in case of a high number of participants. In these cases a collective name is sufficient.

Also, the entertainment expenses need to be accounted for individually on a separate bookkeeping account. If these strict documentation requirements are not met, the tax authority may not accept the deduction even if there is no doubt about the value and the business reason.

**Note:** Detailed attention should be paid to the accuracy of the records. Without the proper records, in case of missing information or without separate accounting, the tax authority denies the tax deduction – even retrospectively! The information can not be caught up.

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All information in this client information sheet has been compiled to the best of our knowledge. They are, however, without guarantee. This information can not replace individual advice.