

HOLIDAY PARTY AND GIFTS: WHAT YOU CAN AND CANNOT DEDUCT ON YOUR BUSINESS TAX RETURN

You can deduct no more than \$25 for business gifts you give directly or indirectly to each person during your tax year

It does not mean that you cannot spend more than \$25, just know that the cost beyond \$25 will not reduce your taxable income. If you give a gift to a member of your client's family, it is considered that you gave an indirect gift to your client. However, if you have an independent business connection with that family member and the gift is not intended for your customer's eventual use, the rule for indirect gift does not apply.

\$25 LIMIT DOES NOT APPLY:

... if you give a gift to an entire company, unless the gift is intended for a particular person or group of people within the company

FOR EXAMPLE, you send a \$100 basket with a selection of teas, coffees and chocolates to your client, ABC Company. You know that employees have a coffee station and your gift will be enjoyed by everyone. You also send an identical \$100 basket to the president of ABC Company. \$100 basket to employees is a company-wide gift and is not subject to \$25 limit. The basket to the president of the company was intended for his personal use and is subject to the limit.

... to incidental costs of engraving, packaging, insuring and mailing gifts to recipients

It means that you can spend \$25 on a gift and additional \$10 on packaging and mailing it to your customer, vendor or business associate. However, the cost is incidental only if it does not add substantial value to the gift.

FOR EXAMPLE, if you are buying an ornamental basket for packaging fruit, the cost of the basket might not be considered incidental if its cost is significant compared to the cost of fruit.

Some items are not considered gifts for the purpose of \$25 limit:

1. An item that costs \$4 or less and
 - Has your name clearly and permanently imprinted on it and
 - Is one of a number of identical items you widely distribute, like pens, desk sets, plastic bags, etc
2. Signs, display racks, or other promotional material to be used on the business premises of the recipient

EXAMPLES

If both you and your spouse give a business gift to the same recipient, for tax purposes you are treated as one taxpayer

It means that \$25 limit is applied on the combined cost of the gifts from both of you. This holds true even if you and your spouse have separate businesses, are separately employed, or each of you has an independent business affiliation with the recipient of the gift.

If you give your customer tickets to a theater performance or sporting event, do you treat it as a gift or entertainment expense?

It depends...

If you do not go with the customer to the event, you have a choice of treating it as a gift expense or entertainment expense.

If you go with the customer to the event, you must treat the cost of the tickets as an entertainment expense (50% tax-deductible).



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You are throwing an office **HOLIDAY BASH**, to which you invite your employees with their spouses, customers, vendors, other business associates and your family members. *Do you deduct the 100% of the party as a business expense or do you deduct 50% of the party as a business entertainment expense?*

The rules are not that straightforward as you might think...

- **100% write off** is available for the cost of the party associated with your employees and their spouses
- **50% write off** is available for the cost of the party associated with customers, vendors, independent contractors, and other business associates if your party is either directly related to the active conduct of your business or associated with a directly related discussion that preceded or followed the party
- There is **no write off** for the attendance by family members even though they are employees or owners

So to get back to the example about a holiday party with employees, family members and business contacts... Let's say, the total number of guests was 100 people, with 50 employees, 40 business guests and 10 family members and your total cost was \$1,000. You may deduct 100% of 50% of the cost, or \$500, for employees; 50% of 40% of the cost, or \$200, for business contacts, and \$0 for family members. Your total deduction is \$700 and your total non-deductible amount is \$300 (\$200 for business contacts and \$100 for family members).



TIPS

And a few small tips that might help you prove business purpose and get that much-needed tax deduction for the holiday party:

- Keep a guest list/ask people to RSVP so you can prove tax deduction allocation
- Make sure your invitation states a business purpose of the party. For example, "Come join us for a holiday drink and see what new products are about to hit the market"
- Take pictures/record video of the event that would prove business purpose, like a new product demonstration
- Keep receipts of all expenses incurred
- Do not go overboard with lavishness



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