



DID YOU KNOW... *Entertainment Tax Deductions*



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The ins and outs of entertainment business deductions

For a business, whether a business expense is “entertainment” will generally also determine whether the cost is deductible. If the expenditure can be shown to be directly connected with the carrying on of a business, it should be deductible.

The example of someone taking a client out to lunch can certainly be shown to be in connection with a business. However, there is still a lurking danger within the relevant sections of the tax law that says that if such an expense also represents “entertainment”, by the Australian Taxation Office (ATO) view, then that cost can be taken out of the deductibility equation.

The definition of “entertainment”

The relevant legislation simply defines entertainment as meaning “entertainment by way of food, drink, or recreation”. The ATO look at four very simple questions — why, what, where and when. The viability of a claim does not live or die on the strength of any one of the answers to those questions, but on a balance of the answers. If an expense is deemed to be entertainment, it is of course non-deductible for income tax purposes and no GST credit is ascribed to it. If it is not entertainment and therefore a business cost, it is deductible.

Looking at the “why” question first, we must ask: is the consumption of the food and drink tied to a social reason, or is there a business reason? We can use the example above of taking a client out to lunch, which is underpinned by a solid business reason. However, the next answer needs to back this up.

The answer to “what” should bear out the reason assumed for lunching with a client, meaning that a lavish four-course meal is out of the question. The logic is that if the parties are meeting for business reasons, the food and drink will be no more than functional. So if we’re looking at sandwiches or muffins, with coffee or orange juice, the “what” bears out the “why”, the deductibility of the expense looks safer. Note, however, that if alcohol is involved, the “what” answer will have much less credibility.



Generally, the “why” and the “what” must be satisfied in order to make a successful claim for deductibility, but the next question – “where” – can undermine the direction of the logic. If the food and drink is consumed on the business’s premises, naturally there is more weight to the argument that the expense is a business cost. Being at a restaurant or café does not necessarily count against the viability of the claim, but the answer to the next question – “when” – helps if the food and drink expense is incurred during business hours.

Wriggle room for entertainment claims

There are some specific expenses that are generally accepted as deductible. Refreshments made available at a presentation to staff on business premises (such as sandwiches, biscuits and tea or coffee) are generally accepted as a business cost, and deductible. The ATO views this sort of food and drink as sustenance, or employee amenities. And again, alcohol has no place in tax deduction considerations in these situations.

Another scenario where food and drink would never be considered entertainment by ATO standards is where expenditure is incurred by an employee who is travelling away from home. In this situation also, there is less of a requirement that the items consumed be merely functional.

Within the tax law that denies the deductibility of the costs of food and drink that are entertainment is a proviso that can be called “promotion and advertising”. So if a business hosts a product launch, for example, and serves up a spread of various food and drinks for the guests, including alcohol, the costs of this entertainment will be deductible. The food and drink are relevant and incidental to the promotional event of the business.

Another proviso within the entertainment deduction prohibition rules is where food and drink are consumed incidental to attendance at a seminar of at least four hours’ duration. Clearly, the time frame is important to allow for an unchallengeable deduction claim. Note also that the word “seminar” covers events such as workshops, training sessions, conferences, lectures and so on.



Assessing the strength of deduction claims

When determining whether an expense is “entertainment”, and therefore deductible or non-deductible, the taxpayer’s position is more assured by having a “reasonably arguable position”.

The ATO has power to impose various penalties and fines, which can be a disincentive in situations where the outcome is not certain.

However, it is equally the case that taxpayers might be missing out on some very legitimate tax deductions by merely not exploring their books and taking too conservative a view that their expenditure is off the table.

If you suspect that there could be “entertainment” deductions your business is missing out on, you need to contact our office for help.

Over the course of a year, these otherwise unidentified pockets of expenditure could add up to thousands of dollars in forgone tax savings.

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