

Miller & Chevalier Employee Benefits Webinar: Final Regulations on Deductions for Entertainment Use of Business Aircraft

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Five years after the issuance of proposed regulations addressing the deductibility of entertainment expenses under Section 274(e)(2) of the Internal Revenue Code, as amended by the American Jobs Creation Act of 2004, the Internal Revenue Service has issued final regulations. Section 274(e)(2) disallows deductions for entertainment goods, services and facilities provided to "specified individuals" to the extent the expenses exceed the amount that the service recipient treats as compensation. Although the statute does not specifically reference aircraft, the intent of the amendment was to override the Tax Court's holding in *Sutherland Lumber-Southwest, Inc. v. Commissioner*, which sustained the taxpayer's deduction of expenses for its executives' entertainment flights on company aircraft that were valued for compensation purposes using the special valuation rules for flights on noncommercial aircraft, known as the SIFL rules.

The final regulations, which were effective August 1, 2012, adopt very few of the suggestions made by commentators following the issuance of the 2007 proposed regulations and Notice 2005-45, but do offer several clarifications. This webinar reviewed the regulatory rules for identifying specified individuals, characterizing the nature of their flights, and determining how to allocate aircraft expenses based on each passenger's reason for being on a flight, including depreciation expenses. In addition to highlighting the clarifications set forth in the final regulations, we highlighted what we consider to be the unanswered issues that taxpayers will face when applying these rules to use of their aircraft by employees and independent contractors (including board members).

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