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NBAA

NBAA PERSONAL USE OF BUSINESS AIRCRAFT HANDBOOK

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Quick Reference Guide for Personal Flights

The charts below review common flight classifications and the resulting treatment of employer deductions and potential imputed income to the employee. The second chart analyzes the same flight classifications for sole proprietors. This is only a high-level summary, and readers should carefully review the entire Personal Use of Business Aircraft Handbook for additional information.

Employer-Provided Flights*		
Purpose of Flight	**Employer Deduction on Form 1120, Form 1065, Form 1120-S**	**Income to Employee (Form W-2), Independent Contractor/Director (Form 1099), Partner (Form K-1 guaranteed payment), S Corporation Owners (Form W-2)**
Business	100% Deduction	No Income Inclusion
Business Entertainment	No Deduction (unless exception applies)	No Income Inclusion
Personal	100% Deduction	Income Inclusion: Charter Rate or SIFL
Personal Entertainment (specified employee)	No Deduction	Income Inclusion: Charter Rate or SIFL
Commuting by employee	No Deduction (unless to ensure the safety of the employee)	Income Inclusion: Charter Rate or SIFL
**The resultant tax effects will appear on two tax returns – an entity's tax return and an individual's tax return.*		
Sole Proprietor Flights*		
Purpose of Flight	**Deduction (Schedule C [Form 1040])**	**Income to Sole Proprietor**
Business	100% Deduction	N/A
Business Entertainment	No Deduction (unless exception applies)	N/A
Personal	No Deduction	N/A
Personal Entertainment (specified employee)	No Deduction	N/A
Commuting	No Deduction (even if to ensure the safety of the sole proprietor)	N/A
**The resultant tax effect for a flight by a sole proprietor will appear on one tax return. [See Section V for further details for sole proprietor and employee provided flights.]*		

This NBAA publication is intended to provide members with an introduction to the tax rules and considerations that relate to the topic of personal use of business aircraft. Readers are cautioned that this publication is not intended to provide more than an illustrative introduction to the subject matter, and since the materials are necessarily general in nature, they are no substitute for the advice of legal and tax advisors addressing a specific set of facts. This version of the handbook is dated July 21, 2022, and does not incorporate any statutes, regulations, or guidance released after that date.

Overview and What's New

The *NBAA Personal Use of Business Aircraft Handbook* ("Personal Use Handbook") Section I summarizes the tax rules for employer companies to calculate the amount of the taxable fringe benefit to report to their employees, partners, directors, and independent contractors who use the company's aircraft for personal purposes. Section II summarizes the tax rules governing the calculation of a company's nondeductible expenses under the entertainment disallowance as amended by the American Jobs Creation Act of 2004 as well as other miscellaneous deduction issues. New to this publication of the Personal Use Handbook is the deduction-disallowance rules for Commuting flights and Business Entertainment flights as added by the Tax Cuts and Jobs Act ("TCJA") of 2017. Effective October 9, 2020, proposed regulations were finalized interpreting the new provisions for Business Entertainment, the definition of entertainment which generally excludes meals, and several exceptions provided in Internal Revenue Code Section 274(e) to the general entertainment disallowance. Proposed and then final regulations were also issued addressing the new Commuting deduction disallowance rules of Section 274(l).

Sections III and IV provide information regarding the Securities and Exchange Commission (SEC) and Federal Aviation Administration (FAA) rules respectively. Section V covers the tax deduction rules for sole proprietors and employee-provided flights.

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Also new are the charts above, which provide a summary of the income inclusion and deductions, with one chart providing the illustration for employer companies and the second chart providing the illustration for sole proprietors.

The Personal Use Handbook emphasizes the importance of detailed records to substantiate the business purposes of Business flights and whether the flight was an entertainment flight, the nonentertainment purposes of Personal nonentertainment flights, and whether the flight involved commuting. The appendices provide sample calculations and a table of illustrative examples covering common scenarios.

I. Imputed Income or Personal Flights Provided by Employer Company

A. GENERAL OVERVIEW OF IMPUTED-INCOME RULES FOR PERSONAL FLIGHTS

The amount includable in the employee's income for personal use of an employer-provided aircraft will be based on either the fair market value of the transportation at fair-market charter rates or the Standard Industry Fare Level ("SIFL") rates. Under either method, the amount of imputed income to the employee – a term that includes partners, independent contractors, and S corporation owners – with respect to any Personal flight is reduced by any reimbursement received by the employer for the flight.[1]

The income-reporting rules discussed in this Section and the deduction-disallowance rules discussed in Section II operate independently of each other. An amount cannot be excluded from an employee's income simply because the employer is willing to forgo the deduction of such amounts.

B. AIRCRAFT ARRANGEMENTS SUBJECT TO IMPUTED INCOME RULES

1. Personal Flights Provided to Service Providers – Referred to as "Employees"

The imputed-income rules apply to flights provided in connection with the performance of services.[2] These rules apply even when the person providing the services is not a common-law employee. For convenience, the imputed-income rules use the term "employee" to include all such service providers, including partners, directors, and independent contractors.[3] The rules also apply to flights provided to former employees[4] and to S corporation owners providing services. Accordingly, the term "employee" is used in this Personal Use Handbook to refer to this expanded definition of employee.

Taxable Personal flights provided to common-law employees are reported on Form W-2, including S corporation employees, and are subject to employment tax withholding. Personal flights provided to partners are reported as a guaranteed payment on Form K-1 and are treated as income subject to self-employment tax. Personal flights provided to independent contractors, including directors, are reported on Form 1099-NEC and are also subject to self-employment tax.

2. Guests of Employees

When personal guests including family members of an employee are on board, the employee – not the guest – is considered to have received the fringe benefit for tax purposes.[5] Therefore, the value of a flight provided to an employee's personal guest is included in the imputed income reported to the employee, at the rate applicable according to the employee's status, (e.g., control or non-control employee). It may be challenging to determine whether a passenger is a personal guest of an employee, for example, when a nonbusiness passenger is provided a flight by the employer but authorized by the CEO or when a father who is an executive employee provides a flight to his son, also an employee. The determination of whether a passenger is in fact the guest of an employee and results in imputed income to that employee is based on all the facts and circumstances.

The value of a flight for a passenger younger than two years old is always zero.[6]

Pets and luggage do not result in additional imputed income.

3. Identification of "Employer"

For purposes of these rules, the "employer" is the company for whom the employee performs the services in return for which the fringe-benefit flight is provided.[7] Therefore, when an employee performs services for Company A and a flight is provided to the employee by Company B as compensation for the employee's services to Company A, the fringe benefit would ordinarily be reported to the employee by Company A[8].

4. Sole Proprietors [*See also* Section V]

The tax rules with respect to sole proprietors are discussed in Section V. The imputed-income rules generally do not apply to an individual's personal use of his own aircraft, because such an aircraft is not employer-provided. For example, when an individual operates an aircraft in the individual's sole-proprietorship business, the individual's Personal flights on that aircraft would not constitute employer-provided flights and would not be subject to the imputed-income rules.

Instead, the sole proprietor would not be entitled to deduct the costs attributed to the Personal flights against income from the sole proprietorship on Schedule C of Form 1040. Sole proprietorships generally include businesses operated directly by the individual as well as businesses operated under a disregarded entity owned by the individual, such as a single-member limited-liability company (LLC).

5. Flights Not Provided as Compensation; Excessive Compensation

The Treasury Regulations governing the valuation of employer-provided flights (including the SIFL rules) apply to flights provided in connection with the performance of services.[9] Accordingly, when the individual receiving the flight did not perform any services, and is not a guest of an employee, the regulations governing employer-provided flights (including the SIFL rules) may not be applicable.

For instance, when a noncompensatory flight is provided by the company to an individual for company business reasons, such as to an employee of another company on a flight to inspect company property in connection with the negotiation of a sale of the property, no imputed income would be required.[10] Moreover, when a flight is provided to a non-guest individual for that individual's personal travel, the noncompensatory flight likewise would not appear to be governed by the fringe-benefit regulations in Treasury Regulations Sections 1.61–21. The result may be that the SIFL rules discussed below ("SIFL Rate Method") are unavailable to calculate the value of Personal flights provided to an individual such as a stockholder who performs no services and is not a guest of an employee.[11] Whether the value of such flights must be reported on Form 1099 is unclear and may depend on the circumstances.[12] Factors to consider are whether the flight would be considered "fixed and determinable income" pursuant to IRC Section 6041 and whether the value is in excess of $600.

Similarly, when the value of flights provided to an employee would constitute excessive compensation with respect to the services performed, the result may be that the SIFL rules are not applicable. The tax treatment of such flights (e.g., as dividends in the case of a stockholder) will depend on the relevant circumstances.[13]

6. Employer-Provided Aircraft *Without* Pilot

The imputed-income rules generally will apply to employer-provided Personal flights, irrespective of the means by which the employer obtains the use of the aircraft. It does not matter whether the aircraft is wholly owned, owned as a fractional interest, leased, or chartered by the employer. However, when the employer provides the use of an aircraft without a pilot, only the fair rental value of the aircraft is imputed to the employee.[14] Nevertheless, the Treasury Regulations do not appear to preclude the use of the SIFL valuation rules for such flights which often would result in less imputed taxable income.

C. DISTINGUISHING PERSONAL FLIGHTS FROM BUSINESS FLIGHTS

1. General Rules

Because individuals are taxed on "gross income from whatever source derived," generally the value of an employer-provided flight for the employee's personal purposes must be imputed to the employee. However, in the case of a sole proprietor, the costs attributable to Personal flights of the sole proprietor may not be deducted by the sole proprietor's business, rather than resulting in imputed income. [See "Sole Proprietor Flights" in Section V.] Favorably, no imputed income is required for an employer-provided flight for the employer's business purposes. Such flights are excludable from the employee's income as a "working-condition fringe."[15] A working-condition fringe benefit is any property or service provided by an employer to an employee to the extent that the property or service would have been deductible by the employee as an ordinary and necessary business expense if the employee had paid the expense.[16] Therefore, to be excludable as a working-condition fringe, a Business flight must satisfy the "ordinary and necessary business expense" requirement under IRC Section 162(a) and the substantiation requirements of IRC Section 274(d).

Since imputed income applies to each passenger traveling for personal purposes, the business or personal character of a flight must be determined separately for each passenger.[17]

a. Ordinary and Necessary Business Expenses

The "ordinary and necessary business expense" standard requires that the expense be "appropriate" and "helpful" in carrying on the taxpayer's business, that it be a common and accepted practice, and that it be reasonable in amount.[18] The courts, including the Supreme Court, provide that the purpose of the term *ordinary* in Section 162(a) is to distinguish between capital expenditures and current expenses. [See *Commissioner v. Tellier*, 383 U.S. 687, 689–690 [17 A.F.T.R.2d 633] (1966); *Welch v. Helvering*, 290 U.S. 111, 113–116 [12 A.F.T.R. 1456] (1933); *Raymond Bertolini Trucking Co. v. Commissioner*, 736 F.2d 1120, 1122–25 [54 A.F.T.R.2d 84-5413] (6th Cir. 1984); *NCNB Corp. v. United States*, 651 F.2d 942, 948 [48 A.F.T.R.2d 81-5298] (4th Cir. 1981).] The requirement that the use of a private aircraft be a common and accepted practice is easily met since the courts have recognized that it is common practice for an executive in charge of a large project to use a private aircraft for transportation.[19]

(1) Reasonableness of Use of Private Aircraft

To establish that the use of a private aircraft is reasonable, it is often helpful to show that the private aircraft saves time for the passengers and enables the passengers to attend more meetings and otherwise be more productive than they would be traveling on commercial airlines.[20] There are, of course, other facts that may support the conclusion that the use of a private aircraft is ordinary and necessary, such as the additional security benefit, ability to discuss confi-

dential business while traveling, access to more remote airports, and flexibility in scheduling.

In assessing the reasonableness of the use of a private aircraft, courts compare the costs of operating the aircraft with the revenue derived from the business activity.[21] In making this comparison, the costs of operating the aircraft should not include depreciation expense. [22]

Companies using private aircraft for business purposes may want to identify these advantages in an aircraft-use policy, approved by their board of directors when applicable. It also may be useful to document the increased productivity and other benefits to the company through internal studies or with the assistance of outside consultants.

(2) Business Purpose Is Based on Primary Purpose of Flight

When a flight is partly for business purposes and partly for personal purposes, its classification as a Business flight or a Personal flight for each passenger is determined based on the *primary* purpose for the trip.[23] There is no bright-line test as to how much business and how much personal activity must occur for a trip to be classified as primarily for business. It is a facts-and-circumstances determination.[24] Courts look to the proximate relationship between the business activity and the transportation costs incurred.[25]

(3) Examples of Business Travel

Travel to meet with customers, suppliers, and other business associates will typically be respected as ordinary business travel.[26] Travel in connection with a taxpayer's farming activity conducted for profit also can meet the "ordinary and necessary business expense" requirement.[27] In addition, travel in connection with management services provided for a fee by one company to a commonly owned company can meet the "ordinary and necessary business expense" test.[28]

Travel to meet a business associate at a vacation location can be business if there are sufficient business discussions or a sufficient business purpose.[29] Despite the fact that Business Entertainment flights do not result in imputed taxable income, such flights now are nondeductible pursuant to the TCJA.

The "ordinary and necessary business expense" test can be met through meetings with other business people and service on the board of directors of other corporations or charitable organization for networking purposes or comparison of views on matters such as trade or economics that are important to the company's business.[30] In addition, expenditures for institutional or "good will" advertising are ordinary and necessary business expenses if the expenditures are related to the business that the company reasonably expects to receive in the future.[31] For example, in *Leo A. Daly Co. v. Vinal*, 23 A.F.T.R.2d 69-843 (D. Neb. 1968), expenses of an architect's service on the board of a civic organization were found to be deductible business expenses as a form of institutional advertising. However, in another case, a court held that an individual's service on the board of a college served no business purpose.[32]

The deductibility of an employee's attendance at conventions and other meetings depends on whether there is a sufficient relationship with the employer's trade or business.[33] When the convention or seminar program includes subjects designed to make those present more effective in their business activities, it would ordinarily be deductible.[34] In *Manning v. Commissioner*, T.C. Memo (RIA) 1993-127, a radiologist's travel to meetings directly related to his work such as International Congress of Radiology meeting and Pennsylvania Radiology Society radiology meeting at Harvard, was treated as business, but other meetings were not business when they bore a weaker relationship to business and involved more-personal activities.[35] Likewise, in another case, general business seminars not related to particular business matters relevant to the attendees did not meet the "ordinary and necessary business expense" test.[36]

(4) Examples of Personal Travel

In contrast, a trip undertaken primarily for personal purposes is not treated as business only because of some incidental business activity on the trip, as shown in the following examples. A trip to the Super Bowl was primarily for personal purposes in view of the relatively insignificant amount of business conducted.[37] Travel to a passenger's rental property primarily to engage in personal activities was not converted to business travel merely because the passenger had observed some repairs that needed to be made on the rental property.[38] Similarly, the wedding of a family member was not treated as business simply because of some business connections with guests attending the wedding.[39] Travel on a honeymoon was held to be personal travel, even though the taxpayer, a professional sportswriter, had done some research on Roberto Clemente's background while on the trip.[40]

As explained above, travel to a vacation location for a business meeting can qualify as business travel. However, travel to a vacation home simply to have a more relaxed place to work would ordinarily be regarded as personal. In *Beckley v. Commissioner*, T.C. Memo (RIA) 1975-37, the individual worked as a writer at his vacation home. However, there was no sufficient business reason for traveling to the vacation home to do the writing when it could have been done at the taxpayer's home or regular place of business.

In summary, simply working at a given location would not make the travel there excluded from income as a business trip. Rather, the reason for the travel to the location must be based on business needs.

(5) Commuting Versus Business Travel

Business travel generally does not include transporting the employee from the employee's residence, when he is there for personal reasons, to the employee's principal place of business.[41] Flights for business purposes from the em-

ployee's residence located near the principal place of work to destinations other than the location of the principal place of work may be considered business travel.[42] Sometimes an employee resides near a secondary place of business (i.e., not the employee's principal place of business). In that case, a flight from the principal place of business to the secondary place of business would generally be business travel if there was a business purpose for traveling to the minor place of business.[43]

Determining the principle place of business was addressed by the Supreme Court in *Commissioner v. Flowers*, 326 U.S. 465 (1946). There, an attorney worked in the city, where he had his residence and another office, rather than in his assigned office at the employer-company headquarters. The decision there, which declared the company offices to be the principal place of work, made sense in the pre-technology and pre-COVID-19 days, where work from the formal employer offices was far preferable. An employer now may wish to formally assign the employee to work primarily from his home office, in which case travel to other destinations for business purposes would then be excluded from imputed income.

In summary, commuting flights refers to travel from a residence, when there for personal reasons, to a work location and results in income inclusion using the SIFL or charter rates. Furthermore, after 2017, as discussed in Section II.B.5, a deduction disallowance applies to the employer if the provision of commuting is not for the purpose of ensuring the safety of the employee.

(6) Important Factors to Support Business Travel

The most important consideration under the "ordinary and necessary business expense" test is whether the business conducted on the trip actually constitutes the *primary* purpose for the trip. However, there are several factors that are important in making this determination.

(i) Relative Time on Business and Personal Activities

In determining whether a trip is primarily for business or personal purposes, the relative amounts of time spent on business and personal activities is an important factor, although it is not determinative.[44] As an example, the Treasury Regulations state that when an individual travels to a destination to spend one week on business matters and five weeks on personal matters, the trip will be treated as primarily personal in nature, in the absence of a clear reason to the contrary. In one case, a trip to a vacation location was treated as primarily personal when the passenger's purported business purpose for the trip was that he had spoken to a few people about the idea of investing in a bank.[45] In another case, the court treated a trip to a trade-association meeting for three days as primarily personal when the rest of the time on the passenger's 15-day trip was for personal purposes.[46] In *Manning v. Commissioner*, T.C. Memo (RIA) 1993-127, the court considered the relative number of days of business and personal activities in holding that several trips were nondeductible (e.g., a two-day meeting during two-week trip or a three-hour meeting during one-week trip).

(ii) Existence of Agenda

In stating generally that travel to attend a convention should qualify as business travel, the IRS emphasizes the importance of an agenda as evidence that the convention is related to the employee's work.[47] Furthermore, an agenda that includes subjects designed to make those present more effective in their business activities and that indicates careful and extensive planning preceding each meeting is helpful in establishing business purpose.[48] In *Manning*, the court pointed to the absence of an agenda or syllabus as a reason for the disallowance of travel expenses with respect to meetings.

(iii) Location of Conference Site

The location of the purported business activity may be an important factor. The fact that a convention is held at a resort hotel is a consideration, but is not dispositive, in determining the primary purpose of a trip.[49]

(iv) Company's Characterization of Trip

Although not determinative, the company's characterization of a trip as a morale builder or as a vacation can negatively affect whether the trip is deemed primarily for business or primarily for pleasure.[50]

(v) Presence of a Spouse or Guest

In Ireland v. Commissioner, 89 T.C. 978 (1987), the presence of family members on trips to a vacation property was considered by the court in concluding that the trips were for entertainment purposes. In Cowing v. Commissioner, T.C. Memo (RIA) 1969-135, the presence of the doctor's wife was considered by the court in its determination that several trips were primarily for personal purposes. In other words, the presence of a spouse of personal guest is "suspect" that the primary purpose of the trip is personal and thus would result in imputed income for both the employee and the guest.

2. Directly Related or Associated with Active Conduct of Business

To be excluded from imputed income, there is some uncertainty whether all the IRC Section 274 requirements must be met or whether just Section 162, requiring a primary business purpose, is sufficient.

As noted previously, the working-condition-fringe regulations provide that "[g]ross income does not include the value of a working condition fringe. A *working condition fringe* is any property or service provided to an employee of an employer to the extent that, if the employee paid for the property or service, the amount paid would be allowable as a deduction under Section 162 or 167." The regulations go on to provide the following: "(ii) If, under Section 274 or any other section, certain substantiation requirements must be met in order for a deduction under Section 162 or 167 to

be allowable, then those substantiation requirements apply when determining whether a property or service is excludable as a working condition fringe." The working condition fringe exclusion does not specifically require that the "directly related or associated with" requirement which was part of IRC Section 274 prior to 2017, be met in order for the employee to avoid taxable income.

As illustrated under Business Entertainment "directly related or associated with", Section II.B.2, there are numerous cases on the issue of when those criteria are met. However, apparently in only one case, *Townsend Industries, Inc. v. United States*, 342 F.3d 890 (8th Cir. 2003), was the issue of income inclusion, rather than loss of deduction to the employer company, raised. In *Townsend*, a company's fishing vacation for employees met the "directly related" test because on the trip, the company had announced the launch of a new product and the employees had discussed the complexity and problems with customers, employees, salespeople, and products, as well as sales tactics and client-specific issues. The court concluded that the value of the trip need not be included in the employee attendees' Forms W-2 but that the employer company would have a deduction disallowance related to the entertainment expenditures. Numerous other cases addressing the "directly related or associated with" requirement only addressed the employer deduction and did not raise the possibility of income inclusion to the employee attendees.

Prior to the TCJA in 2017, Section 274(a) treated entertainment that was directly related or associated with the active conduct of business differently from other entertainment expenses. Now there is no such distinction. Business entertainment is defined with respect to entertainment that has a business purpose and that is directly related or associated with the active conduct of a trade or business. Because the working-condition-fringe rules do not pick up the "directly related or associated with" requirement, that definition is discussed in Section II, concerning the deduction disallowance. Although it may be possible to exclude from imputed income those flights that meet Section 162 only, it is highly recommended that when entertainment is involved, documentation occur to support "directly related or associated with" requirements to further support the exclusion of the flight from taxable income. For example, if executives are taking customers or clients golfing or hunting, an agenda to business discussions should be prepared in advance.

3. Spouse, Family, and Personal Guests

a. Classification of Flights by Spouse, Family, and Personal Guests

As a practical matter, an employee traveling for business purposes accompanied by spouse, family, and personal guests almost always has imputed income because the guest travel is categorized as primarily personal rather than as for ordinary and necessary business purposes under IRC Section 162. This is the case even where the employer requires or encourages the attendance of the personal guest at a business event.

The Treasury Regulations provide that a spouse and other family members traveling with an employee will only meet the "ordinary and necessary business expense" requirement if their presence serves a bona fide business purpose.[51] Performing some incidental service is not sufficient. The courts have held that meeting and socializing and serving as a host or hostess is not sufficient to meet this standard.[52]

Services by a spouse that did not constitute bona fide business purposes include:

- Attending business lunches and dinners
- Staffing a convention hospitality suite
- Hosting dances and receptions
- Typing notes[53]

The mere expectation alone that spouses are to attend a function requiring travel on the business aircraft does not necessarily meet the requirements to consider the spouse's travel an ordinary and necessary business expense. However, a spouse's presence has been found to constitute a bona fide business purpose in the following circumstances:

- Not only entertaining but also helping a spouse understand a foreign language
- Performing clerical functions, entertaining, and touring plants (but not sightseeing)
- In rare cases, attending and helping entertain at various events (luncheons, screenings, meetings) where other spouses are present and company policy requires employees to be accompanied by their spouses when traveling to project a family-friendly image
- Acting as business manager and road manager
- Acting as chaperone for minor contestants
- Attending business seminars directed to spouses of salespeople[54]

If an accompanying spouse's business-related activities are sufficient to support an "ordinary and necessary business expense" deduction under the above cases, it would still be necessary to determine whether the entertainment disallowance would apply. Accordingly, if the spouse's primary activity consists of engaging in entertainment activities (e.g., attending social functions), the "directly related or associated with" tests described below in Section II.B.2 ("Business Entertainment") would need to be considered.

b. Travel Deduction Limitation Under Section 274(m)(3) on Spouses, Dependents, and Personal Guests

IRC Section 274(m)(3) is intended to limit a company's deduction with respect to spouses, dependents, and personal guests accompanying employees on business travel. Treasury Regulations Section 1.132 5(t)(1) provides that the disallowance under Section 274(m)(3) does not affect the determination of whether the company must report imputed income with respect to the spouse, dependents, and personal guests. Accordingly, the classification of these individuals as business or personal travelers is made under the otherwise applicable rules discussed above. In other words, the fact that a spouse is not an employee of the company (as required under Section 274(m)(3)) is not relevant to the classification of the spouse's travel for income-inclusion purposes.

4. Recordkeeping

IRC Section 274(d) provides that no deduction is allowed for travel expenses, entertainment, or gifts or with respect to listed property, "unless the taxpayer substantiates by adequate records or by sufficient evidence corroborating the taxpayer's own statement" certain specified items. The specified items that must be documented include the amounts, dates, distance traveled, destinations, and business purpose.[55] In the case of Business Entertainment, the documentation also must include information regarding the individuals entertained.[56]

To maintain the required records, a company must maintain an account book, diary, log, statement of expense, trip sheets, or similar record and documentary evidence sufficient to establish each of these elements.[57] Typically, the company's cost-accounting system and the pilot's logs will provide all the required information, except for the business purpose. Sometimes it is necessary to make sure that the pilots are recording the names of all the passengers on each flight. It is important that someone (usually an individual in the company's flight department or accounting department) follow up with the passengers to prepare the business-purpose descriptions.

The business-purpose descriptions should be prepared at or near the time of the flight. This requirement is met if the description is prepared when the individual has full, present knowledge of the business purpose of the flight.[58] The degree of detail necessary to establish business purpose will vary depending on the facts and circumstances. If the business purpose is evident from the surrounding facts and circumstances, a written explanation of such business purpose is not required.[59] For example, no business-purpose description would be required for a salesman traveling on his established sales route or for a business meal when the relationship between the individuals is evident from the surrounding circumstances. Nevertheless, as a matter of practice, business-purpose descriptions should be prepared on a contemporaneous basis.

If the required business-purpose descriptions are not prepared on a contemporaneous basis, they can be prepared later. However, subsequently prepared records must be supported by other corroborative evidence.[60] In general, subsequently prepared records have a lower probative value than contemporaneous records.[61] In numerous cases, the courts have characterized taxpayers' testimony and other noncontemporaneous evidence of business purpose as unreliable, self-serving, contradictory, and vague.[62] Therefore, companies should prepare the business-purpose descriptions on a contemporaneous basis.

D. CHARTER RATE METHOD

The charter-rate method is the method required to calculate the amount of imputed income to an employee for a Personal flight when the SIFL method discussed below in Section II.E ("SIFL Rate Method") has not been properly elected.

In addition, the charter-rate method may be applicable to particular flights for which the SIFL rate method was elected but the SIFL amount was erroneously calculated, as discussed below in Section I.E.5 ("Penalties").

In most cases, the imputed income calculated under the SIFL method is lower than that under the charter-rate method with the exception related to flights with numerous personal passengers where the addition of the per passenger SIFL income inclusion is in excess of the charter rate for the flight. In addition, determining a comparable charter rate for a flight may be administratively difficult and uncertain. For both reasons, most companies choose to use the SIFL method.

1. Charter Rate Calculations – Employer-Provided Flights

Under the charter-rate method, the imputed income to an employee for an employer-provided Personal flight is the amount that an individual would have to pay in an arm's-length transaction to charter the same or a comparable piloted aircraft for that period for the same or a comparable flight.[63] In practice, this information is typically obtained by asking charter companies for the hourly rate that they would charge for a flight in a comparable aircraft. The hourly rate is then multiplied by the actual duration of the flight.

The definition of a *flight* under the charter-rate method is the same as that under the SIFL method. Therefore, no imputed income is required for a deadhead flight where no passengers are on board. In addition, when business is the primary purpose of a multi-leg trip to both business and personal destinations, only the additional travel attributable to the personal stop would be subject to the imputed-income calculation.

The charter-rate method provides that if an employee's flight is properly valued under the SIFL-rate method, no additional amount shall be imputed to that employee under the charter-rate method. This special rule seems likely to

be most relevant when some flights are not properly valued under the SIFL-rate method and the value is being redetermined on audit using the charter-rate method. For example, if the value of a flight were zero according to the 50%-seating-capacity rule under the SIFL method explained below in Section II.E.3.c ("50%-Seating-Capacity-Rule"), and zero were in fact imputed to that employee for that flight, then it would appear that because of this special rule, no additional amount would need to be imputed to that employee for that flight under the charter-rate method.

If there are multiple passengers on the flight, the fair-market charter rate is allocated among the passengers. Each employee would be imputed the share of the charter rate attributable to himself or herself and his or her guests. However, if there are one or more control employees, the fair-market charter rate is allocated proportionately among the control employees, unless there is a written agreement providing for a different allocation.

a. Definition of *Control Employee* (for Charter Rate Method Only)

For purposes of the charter rate method, *control employees* are defined as those employees who control the aircraft by determining the route, departure time and destination of the flight. Note that this definition of control employee differs from the definition of control employee for purposes of the SIFL method as discussed below in Section II.E.2.d (Control Employee Status).

b. Example of Charter Rate Method Calculation

The Treasury Regulations present the following example of the charter-rate method. [64]

Employee A wants to go from New York to Los Angeles for personal reasons. Employee B likewise wants to go from New York to Los Angeles for personal reasons but needs to stop in Chicago for business.

Chicago is an intermediate stop for Employee A and is not included in calculating A's imputed income. Therefore, the amount imputed to A is based on the charter value of a flight from New York directly to Los Angeles.

Chicago is a business destination for Employee B. Therefore, the trip from New York to Chicago is not to be included in calculating B's imputed income. The amount imputed to B is based on the charter value of a flight from Chicago to Los Angeles.

The values of the trips based on charter rates are as follows:

- Total charter value of the entire trip from New York to Chicago to Los Angeles is $1,200.
- The charter value of A's personal trip from New York to Los Angeles is $1,000.
- The charter value of B's personal trip from Chicago to Los Angeles is $600.

The combined charter value of A's and B's personal trips is $1,600 ($1,000 + $600), but the total charter value for the entire trip is only $1,200. Therefore, the total charter value of $1,200 for the entire flight is allocated between A and B in proportion to the relative values of their Personal flights.

Value of A's Flight:

Charter value of A's Flight	$ 1,000
Combined charter values of A's and B's flights	÷ 1,600
Charter value of entire flight	× 1,200
Imputed income to A	$ 750

Value of B's Flight:

Charter value of B's Flight	$ 600
Combined charter values of A's and B's flights	÷ 1,600
Charter value of entire flight	× 1,200
Imputed income to B	$ 450

There appears to be an inconsistency between the rule set forth in the regulation and the above example. The regulation states that the charter value is allocated among all employees on the flight, rather than among only the employees traveling for personal purposes. However, the above example seems to suggest that the charter value must be allocated among only the employees traveling for personal purposes. For example, if there is one passenger traveling for business and one passenger traveling for personal purposes on a flight with a charter value of $1,000, should the amount imputed to the one passenger traveling for personal purposes be $1,000 or $500? The regulation and the example therein appear to be ambiguous on this point.

2. Lease Value Method – Employer-Provided Aircraft Without Pilot

If an employer provides the use of an aircraft to an employee without a pilot, then the imputed income to the employee is the amount that an individual would have to pay to lease a comparable aircraft on the same terms for the same period in the same geographic location.[65] If the employer-provided aircraft benefits multiple employees, then the lease value is allocated among the employees according to the relevant facts and circumstances.

E. SIFL-RATE METHOD

The SIFL rates are determined using a formula prescribed in Treasury Regulations Section 1.61 21(g) and are applied on a cents-per-mile basis *for personal passengers while on the plane*. Thus, deadhead flights where there are no passengers on the plane are not included in the SIFL calculation. The rates are determined by the Department of Transportation and are updated every six months. The SIFL rates are intended to be approximately double the amount of first-class airfare for a control employee and equal to a standby coach fare for a non-control employee.

The SIFL rates may be utilized to value domestic and international flights of airplanes or helicopters as long as the travel was not sold on a per-seat basis.[66] Thus, the SIFL rates may be used in situations where the aircraft is owned, leased, or chartered by the employer.

The SIFL calculation can be performed using the NBAA Personal Use Calculator, which is available on the NBAA website at www.nbaa.org/taxes.

1. SIFL Calculation

a. Information Needed for SIFL Calculation

The following information is needed to calculate imputed income under the SIFL rate method:

- The point-to-point distance between the two airports on each leg of the trip.
- The SIFL rates and the terminal charge for the six-month period in which the flight occurred.
- Maximum certified takeoff weight ("MTOW") of the aircraft.
- The business or personal status of each employee and guest on the flight for each leg of the trip
- The control or non-control status of the employees on the flight.

b. Description of SIFL Calculation

The SIFL calculation for each leg of each employer-provided flight with passengers traveling for personal purposes is as follows under Treasury Regulations Section 1.61 21(g)(5):

- Step 1: Multiply the number of miles on the leg by the applicable SIFL rate for the six-month period in which the flight occurred to determine the base SIFL fare.
- Step 2: Multiply the base SIFL fare by the aircraft multiple, based on the MTOW of the aircraft and the employee's control or non-control status, to determine the adjusted SIFL fare.
- Step 3: To the adjusted SIFL fare, add the terminal charge for the six-month period during which the flight occurred to determine the SIFL fare per passenger.
- Step 4: Multiply the SIFL fare per passenger by the number of passengers traveling for personal purposes to determine the total SIFL fare.
- Step 5: Subtract any reimbursement received from the employee for the flight.

Each of these steps is explained in more detail below, followed by an explanation of the special rules for bona fide business-oriented security concerns, foreign travel, and the 50%-seating-capacity rule.

c. Example SIFL Calculation

Suppose the employer provides to a control employee an 874 mi. flight from Saint Louis to Orlando for personal purposes on January 10, 2022. The employee is accompanied by a spouse and two children, ages 5 and 10. Pursuant to a time-sharing agreement, the employee reimburses the employer $1,260 for the flight. The aircraft has a MTOW of 91,000 lbs.

The imputed income at SIFL rates that the employer would report to the employee would be calculated as follows:

Mileage Charge:

First 500 mi. at $0.1611/mi.	$ 80.55
Next 374 mi. at $0.1228/mi.	+ 45.93
Base SIFL fare	126.48
Aircraft multiple for control employee	× 400%
Adjusted SIFL fare	505.92
Terminal charge	+29.45
SIFL fare per passenger	535.37
Number of nonbusiness passengers	× 4
Total SIFL fare	2,141.48
Reimbursement from employee	(1,260)
Net taxable SIFL fare	$881.48

d. Tax Reporting

(1) Tax Forms

The proper reporting of the SIFL amounts to the employee depends on the parties' tax situations. In general, the reporting is generally as follows:

Employees – An employer would typically report the SIFL amount on a common-law employee's Form W-2.

Independent Contractors – An employer would typically report the SIFL amount for an independent contractor on a Form 1099. A person serving as a director, and not as an employee, would ordinarily be an independent contractor for tax purposes.

Partners or LLC Members – A partnership would report the imputed income to its partner as a guaranteed payment on Schedule K-1 of the partnership's tax return. This income would be subject to self-employment tax. Partnerships sometimes report such guaranteed payments on Form 1099, which appears to accomplish the reporting objectives, but may be technically incorrect. The same reporting would apply to an LLC treated as a partnership for tax purposes.

(2) Frequency of Imputed Income; Election to Defer November and December SIFL Reporting

It is permissible to report imputed income and withhold for flights provided to employees on a periodic basis as infrequently as once per year (e.g., as of December 31). It is also permissible to impute income only on flights through the end of October of the current year and report the SIFL value of the November and December flights in the subsequent year's compensation.[67] Presumably, the SIFL amount for the

entire calendar year would still be available to subtract from the entertainment disallowance for the calendar year in the calculation described below in Section II.B.4. addressing the entertainment deduction disallowance.

2. Components of SIFL Calculation

This Section explains in more detail the determination of the distance traveled, the SIFL rates and terminal charges, the aircraft multiples, and the control-employee status of the passengers.

a. Distance Traveled

(1) Statute Miles

The IRS defines a flight as the distance, in statute miles, between the place at which the individual boards the aircraft and the place at which the individual deplanes.[68] Under this definition, each leg of the trip requires a separate SIFL calculation. Consideration needs to be made that the calculation is point to point, while the leg-by-leg route may differ.

If the flight information is provided in nautical miles, it is necessary to multiply the number of nautical miles by 1.15 to convert to statute miles.

The number of miles for a particular leg of the trip is the distance between the two airports, rather than the number of miles that the aircraft actually flies.

(2) Multi-Leg Flights

(a) Primary Purpose of Trip

If an employee combines, in one trip, Personal and Business flights on an employer-provided aircraft, and the primary purpose of the trip is business, the SIFL amount is the excess of the SIFL amount calculated on the entire trip over the SIFL amount calculated on the flights that would have been taken if there had been no Personal flights. [69]

For example, suppose an executive travels on an employer-provided aircraft from Indianapolis to Tampa for a business meeting and returns from Tampa to Indianapolis, with a stopover at Pensacola for personal reasons. Assume that the primary purpose of the trip is the business meeting and the stopover in Pensacola for personal reasons was incidental. The SIFL amount for the trip would be calculated as follows:

- Calculate the SIFL amount for all three legs of the trip, as if the entire trip were for personal purposes.
- Calculate the SIFL amount for a hypothetical business trip from Indianapolis to Tampa and directly back to Indianapolis, without the stopover in Pensacola.
- The SIFL amount to impute to the employee would be the excess of the SIFL amount for the whole trip over the SIFL amount for the hypothetical business trip to Tampa and back.

In contrast, suppose the stopover in Pensacola was the primary purpose for the trip and the detour to Tampa for business was merely incidental. In that case, the amount of imputed income would be the SIFL amount calculated on a hypothetical trip from Indianapolis to Pensacola and directly back to Indianapolis, without a stop in Tampa.

(b) Intermediate Stop

The IRS defines an *intermediate stop* as a landing necessitated by weather conditions, an emergency, refueling, or any other purpose unrelated to the personal purposes of the employee whose flight is being valued.[70] An intermediate stop with respect to an employee would include a stop to accommodate another passenger for a purpose unrelated to the employee's purpose for traveling. The additional mileage attributable to an intermediate stop with respect to an employee is not considered when determining the distance of that employee's flight in the SIFL calculation.

For example, suppose an employer provides a flight from Washington, DC to Atlanta, then continuing on to Orlando. Control Employees A and B and their respective guests are traveling to Orlando for personal purposes and have no interest in stopping in Atlanta. Control Employee C and her guest's destination is Atlanta. The imputed income at SIFL rates for A and B is determined by the distance from Washington, DC directly to Orlando, since Atlanta represents an intermediate stop for them.

(3) Deadhead Flights

As previously stated, applying the SIFL rate method, a flight is the distance, in statute miles, between the place at which the individual boards the aircraft and the place at which the individual deplanes.[71] Based on this rule, no SIFL income needs to be imputed to anyone for flights with no passengers, such as deadhead or repositioning flights. In contrast, deadhead flights must be included in the entertainment-deduction-disallowance calculation, discussed below in Section II.B.4 addressing deadhead flights.

b. SIFL Rates

The SIFL rates are calculated and updated by the U.S. Department of Transportation every six months. The IRS publishes the SIFL rates and terminal charges for the six-month periods of January to June and July to December. These rates are available on the NBAA website at www.nbaa.org/taxes.

The SIFL rates are presented as one rate per mile for the first 500 miles, another rate for the next 1,000 miles, and a third rate for miles in excess of 1,500 miles. This schedule of rates is applied separately to each leg of a trip.

c. Aircraft Multiples

The aircraft multiple depends on the maximum take of weight, MTOW, of the aircraft and whether the income is to be imputed to a control or a non-control employee.

The aircraft multiples listed in Treasury Regulations Section 1.61.21(g)(7) are as follows and do not change from year to year:

MTOW of the Aircraft	Aircraft Multiple for a Control Employee	Aircraft Multiple for a Non-Control Employee
6,000 lbs. or less	62.5%	15.6%
6,001–10,000 lbs.	125%	23.4%
10,001–25,000 lbs.	300%	31.3%
25,000 lbs. or more	400%	31.3%

Since it is possible to have imputed income for both control and non-control employees on a single leg of a trip, it is possible that different aircraft multiples would be applied to the SIFL calculations for different employees on a single leg.

If there is a bona fide business-oriented security concern and certain other requirements are met, then the maximum aircraft multiple is capped at 200%.[72] This special rule is discussed below in more detail in Section I.3.a Business-Oriented Security Concerns

d. Control-Employee Status

To determine which aircraft multiple to use, it is necessary to determine the control- or non-control-employee status of the employee to whom the passenger's Personal flight is taxed. This Section of the Personal Use Handbook provides a general explanation of the definition of control employee. In many cases, only individuals who are obviously control employees have the right to use the aircraft for personal purposes. However, the definition of control employee is complex, and in some cases, it is necessary to consult the Treasury Regulations to determine whether the individual is a control employee.

(1) Definition of Control Employee

In general terms, a control employee is an officer, highly compensated employee, 5% owner, or director. More specifically, the IRS defines control employee in Treasury Regulations Section 1.61 21(g)(8)(i), for a nongovernment employer, as any employee that meets the following tests:

A. who is a board- or shareholder-appointed, -confirmed, or -elected officer of the employer, limited to the lesser of (i) 1% of all employees (increased to the next higher integer, if not an integer) or (ii) 10 employees;

B. who is among the top 1% most-highly-paid employees of the employer (increased to the next higher integer, if not an integer) and limited to a maximum of 50;

C. who owns a 5% or greater equity, capital, or profit interest in the employer; or

D. who is a director of the employer.

This control-employee relationship is determined with respect to the employee's employer, which is the entity to which the employee provides the services in return for which the fringe-benefit flight is provided.[73] The employer for this purpose need not be the same entity that actually provides the flight to the employee. See Section I.B.3.

An employee whose compensation is below $50,000 cannot be classified as a control employee under tests A or B above.[74] The $50,000 threshold is adjusted annually for inflation and the new amount is published by the IRS.

As explained above in Section 1.B.1 Personal Flights Provided to Service Providers – Referred to as 'Employees, the term "employee" for purposes of the SIFL-rate method generally refers to common-law employees, directors, partners, and independent contractors. However, for purposes of the highly-compensated-employee test (test B above), the term "employee" is modified to include only common-law employees, partners, and 1% or greater shareholders.[75]

(2) Former Employees

Former employees who are provided a flight on a former employer's aircraft for personal purposes will have imputed income, where the flight is provided in connection with their prior service to the employer. The regulations provide special rules for determining control-employee status of former employees.[76] Under these rules, an employee who was a control employee at any time after reaching age 55 or within three years of separation of service will be treated as a control employee. Former employees classified as control employees are not counted in determining the maximum number of employees who can be considered control employees under the definition of control employees.

(3) Personal Guests

As explained above in Section I.B.2 Guests of Employees, the SIFL value of a guest's flight is reported as income to the employee, rather than to the guest. Consistent with this principle, the control or non-control status of the guest is determined by the control or non-control status of the employee.[77] In other words, a flight provided to the personal guest of a control employee will be valued using the control-employee aircraft multiple.

(4) Family Members

A family member of a control employee is automatically a control employee.[78] For this purpose, family members include siblings, spouse, ancestors, and lineal descendants.[79]

(5) Aggregation Rules

To test the compensation of an employee for purposes of the highly-compensated-employee test (test B), it is necessary to treat as a single employer all companies that are subject to aggregation under certain compensation rules.[80] Those aggregation rules are set forth in IRC Section 414(b), (c), (m), and (o), and they generally include affiliated groups of corporations and other entities and affiliated service groups.

Under the 5%-owner test (test C) and the 1%-owner test (to determine employee status for purposes of test B), an individual's ownership of any entity is determined from direct- and indirect-ownership principles under IRC Section 318(a).[81] For purposes of these tests, if an individual is a 5% (or 1%) owner of an entity, that individual is considered to be a 5% (or 1%) owner of all entities subject to aggregation under IRC Section 414(b), (c), (m), and (o).

However, for purposes of the officer and director tests (tests A and D), officer and director status is determined on an entity-by-entity basis. In other words, being an officer or director of one corporation does not cause the individual to be treated as a control employee of another corporation.

3. Special Rules

a. Business-Oriented Security Concerns

A beneficial modification to the standard aircraft-multiple rates is found in the Bona Fide Business Oriented Security concern rules.

If a "bona fide business-oriented security concern" exists with respect to a particular employee, and the employer requires that the employee travel on employer-provided aircraft for personal trips, then the employer may exclude from the employee's gross income the excess value of the flight over the "safe-harbor airfare."[82] This rule results in the maximum aircraft multiple being capped at 200%.

To be eligible to apply this rule, the employee must qualify as an "employee" under Treasury Regulations Section 1.132 1(b)(2).[83] Under Treasury Regulations Section 1.132 1(b)(2), "employee" means (1) an individual currently employed by the employer; (2) a partner who performs services for the partnership/employer; (3) a director; and (4) an independent contractor. If a bona fide business-oriented security concern exists with respect to such an "employee," then the requisite security concern is also deemed to exist with respect to the employee's spouse and dependents who concurrently travel with the employee on Personal flights.[84] When the employee's spouse and dependents travel without the employee, the bona fide business-oriented security concern will exist for them only if the requirements discussed below are met for the spouse and dependents.

A bona fide business-oriented security concern exists only if the facts and circumstances establish a specific basis for concern regarding the safety of the employee.[85] A generalized concern for the safety of the employee is not sufficient.

In addition, the employer must either establish an "overall security program" for the employee or have an "independent security study" prepared for the employee.[86] An overall security program requires that security be provided to protect the employee on a 24-hour basis.[87] An independent security study must meet the following requirements: (1) it must be performed with respect to the employer and the employee by an independent security consultant; (2) it must be based on an objective assessment of all facts and circumstances; (3) the recommendation of the security study must be that an overall security program is not necessary and that the recommendation is reasonable under the circumstances; and (4) the employer must apply the specific security recommendations contained in the security study to the employee on a consistent basis. [88]

If the above criteria for a bona fide business-oriented security concern are met, then the employee's income is determined under the SIFL-rate method, except that the aircraft multiple is capped at 200%.[89] The same SIFL rate would apply to the employee's spouse and dependent children when traveling on the aircraft with the employee, and if a bona fide business-oriented security concern exists for them under the rules discussed above, the same lower rate applies even when the spouse and dependent children travel independently.

b. Foreign Travel

(1) Foreign Travel for More Than Seven Days

The foreign-travel-disallowance rule under IRC Section 274(c) applies to a trip outside the United States when both of the following conditions are met: (a) the trip outside the United States lasts for more than seven days and (b) at least 25% of the individual's time on the trip is devoted to nonbusiness activities. Under Treasury Regulations Section 1.274 4(d), the 25% threshold is measured on a day-by-day basis. If both conditions are met, then the disallowance rule applies to the costs of the foreign trip multiplied by the ratio of the number of nonbusiness days and divided by the total number of days.[90]

Rules for determining the number of business and nonbusiness days are provided in Treasury Regulations Section 1.274 4(d)(2). Under these rules, the travel days out of and into the U.S. are considered business days.[91] Any day that the taxpayer's presence is required for business purposes at the foreign location is considered a business day.[92] Intervening weekends are generally counted as business days.[93]

This foreign-travel-disallowance rule only applies to "individuals" as provided in Section 274(c). Treasury Regulations Section 1.274 4(a) makes it clear that this disallowance rule does not apply to an "employer." Accordingly, this provision cannot result in the disallowance of expenses for the employer.

Instead of causing the disallowance of the employer's deduction, the foreign-travel disallowance results in the inclusion in the employee's income of a portion of the SIFL amount that would otherwise apply if the trip were entirely nonbusiness.[94] The SIFL-income amount would be determined as follows:

1. Determine the number of personal days and the number of business days on the trip outside the U.S. Divide the personal days by the total days to determine the personal-days percentage. If the percentage exceeds 25% and the trip is outside the U.S. for more than seven days, then the foreign-travel-disallowance rule applies.

2. Calculate the SIFL amount for the trip as if the trip were entirely personal.

3. Multiply this SIFL amount by the personal-days percentage to calculate the SIFL-income inclusion.

Of course, this foreign-travel rule would not be relevant to a passenger whose primary purpose on the trip is personal, because the SIFL amount for the entire trip would be imputed to that individual.

In contrast, in the case of a sole proprietor, the foreign-travel rule would cause the disallowance of the personal-days percentage of the sole proprietor's costs of the flight.

The foreign-travel-disallowance rule in Section 274(c) applies for purposes of IRC Sections 162 and 212. There is no authority in the foreign-travel disallowance in Section 274(c), the entertainment disallowance in Section 274(a), or the Treasury Regulations under either of those sections to support applying the foreign-travel disallowance to the entertainment-disallowance rules discussed below in Section II Entertainment Deduction Disallowance.

(2) Travel to Conventions or Seminars Outside North America

With respect to attendance at conventions, seminars, or similar meetings held outside the North American area, no deduction shall be allowed under Section 162 for expenses allocable to such meetings unless the taxpayer establishes that the meeting is directly related to the active conduct of his trade or business and that taking into account:

- the purpose of such meeting and the activities taking place at such meeting;
- the purposes and activities of the sponsoring organizations or groups;
- the residences of the active members of the sponsoring organization and the places at which other meetings of the sponsoring organization or groups have been held or will be held; and
- such other relevant factors as the taxpayer may present that make it as reasonable for the meeting to be held outside the North American area as within the North American area.[95] This criterion may be met, for example, if the selected location outside the North American area is a central location for a multinational company.

c. 50%-Seating-Capacity Rule

This beneficial rule can be utilized when 50% or more of the regular seating capacity of an aircraft occupied by individuals whose flights are primarily for the employer's business. The value of a flight on that aircraft by any employee, employee's spouse, or dependent who is not flying primarily for the employer's business is deemed to be zero.

(1) Benefits of the 50%-Seating-Capacity Rule

If the 50%-seating-capacity test is met for a flight, no SIFL income needs to be imputed for a common-law employee, a partner, or his or her accompanying spouse and dependent children traveling for personal purposes on that flight.[96] In addition, if the 50% seating capacity rule is met, guests of common-law employees and partners, other than an accompanying spouse and dependent children, independent contractors, directors, and their guests traveling for personal purposes are subject to imputed income at the non-control-employee SIFL rate, even if they are control employees.

For example, if the 50%-seating-capacity test is met, there is no imputed income for the accompanying spouse of a common-law employee traveling for personal purposes, but SIFL income would be calculated at non-control-employee rates for a cousin of a common-law employee traveling for personal purposes.

(2) Meeting the 50%-Seating-Capacity Test

The 50%-seating-capacity rule applies if 50% or more of the regular passenger seating capacity of an aircraft as used by the employer is occupied by individuals whose flights are primarily for the employer's business and whose flights are excludable from income under IRC Section 132(d).[97] As the term "individual" is not restricted, it presumably includes employees, partners, independent contractors, directors, and other individuals such as customers whose flights are provided primarily for the employer's business.

In the calculation of whether business passengers fill 50% of the aircraft's "regular seating capacity," the regular seating capacity includes all seats that are belted and approved for takeoff and landing less any required crewmember seats.[98] The regular seating capacity of the aircraft is the maximum number of seats on the aircraft during a 24-month period, unless the seats were permanently removed and not reinstalled in the 24-month period.[99] If a seat is reinstalled, even for one flight, it is included in the count for the entire period, including previous flights in the 24-month period. "Seats" include jump seats and removable seats used solely for the purposes of flight-crew training.

Seats occupied by the flight crew are not included in the regular seating capacity, and such members of the flight crew are not counted in reaching the 50% threshold.[100] It is not clear whether "flight crew" is limited to those individuals required by the Federal Aviation Regulations and the original equipment manufacturer's specifications to operate the aircraft or whether it has a more general meaning, such as those individuals primarily on the aircraft to provide flight service rather than to travel to the destination. The example in Treasury Regulations Section 1.61 21(g)(12)(v) might be read to support the latter interpretation.

4. Consistency Rules

The charter-rate method is the default method, and the SIFL-rate method is a special valuation method that the employer can elect if it complies with the requirements of the SIFL-rate method. One of the requirements is the consistency requirement, which provides that if the employer elects to use the SIFL-rate method in any particular year, it must use that method for all of its employees during that year.[101] An exception to this consistency rule provides that the charter-rate method may be used for entertainment flights for all specified employees, while the SIFL-rate method is used for all other flights.[102]

5. Penalties

It is important that the SIFL rules be applied correctly. If it is subsequently determined that the SIFL rules were not applied correctly to an employee on a flight, then the rules will not be available for that employee on that flight and the imputed income for that employee on that flight would have to be recalculated using the charter-rate method.[103] The Regulations provide the following nonexclusive list of errors that will trigger this penalty:

- treating a control employee as a non-control employee;
- classifying the aircraft in too low a weight classification for purposes of determining the aircraft multiple;
- applying the 50%-seating-capacity rule to a passenger who did not qualify for it; or
- classifying a passenger traveling for personal purposes as business.

In addition, failure to properly report the SIFL amount on information returns (e.g., Form W-2, Form 1099, Schedule K-1) can result in information-return-reporting penalties specific to those returns.

In the case of Personal nonentertainment flights (discussed below in Section II.B.4, the failure to report imputed income may prompt the IRS to seek to deny the employer's deduction for the cost of the flights.[104] However, after the October 23, 2004 effective date of the American Jobs Creation Act of 2004, the requirement in IRC Section 274(e)(2) that the fringe benefit be reported to the employee as a prerequisite to claiming the compensation exception to the entertainment disallowance would seem irrelevant with respect to a flight provided to a specified individual. The 2004 amendment to Section 274(e)(2) disallows the employer's deduction (in excess of the imputed income reported to, or reimbursement received from, the employee) of entertainment flights provided to specified individuals, irrespective of whether the imputed income was reported to the employee.

F. REIMBURSEMENTS

1. Reimbursements Permitted by Tax Laws but Not by the FAA [see *also* Section III]

Reimbursements by an employee reduce the amounts of the employee's imputed income and the employer's entertainment disallowance as well as the amount reported as a perk for public-company-reporting purposes. Therefore, it is not unusual for the company or the employee to want to reimburse for all or a portion of a Personal flight.

However, if the flight is provided under Part 91, the employer and employee may want to enter into a time-sharing agreement or Nichols opinion arrangement to enable the employee to make reimbursements without running afoul of the FAA rules. Refer to Section III for a more detailed FAA overview.

G. FREQUENTLY ASKED QUESTIONS (FAQ) ABOUT PERSONAL USE

Q: Can the SIFL rules still be used for reporting the value of Personal flights provided by an employer?

A: Yes. The SIFL rules [Treas. Reg. Sec. 1.61 21(g)] may be used for reporting the value of Personal flights provided by an employer. Note that subsequent to 2004, the amount deductible on the employer's tax return may be decreased for certain entertainment flights by specified employees and for certain commuting travel.

Q: Can the SIFL valuation formula in the regulations be used for international flights?

A: [Treas. Reg. Sec. 1.61-21(g)(2).] Yes. The valuation rule may be used to value international, as well as domestic, flights.

Q: Can the SIFL valuation formula in the regulations be used for flights provided by the employer through a charter operator?

A: [Treas. Reg. Sec. 1.61-21(g)(2).] The valuation rule may be used to value charter flights and all flights provided by an employer other than those where seats are sold on an individual basis to the public.

Q: Does this valuation formula apply to helicopters as well?

A: [Treas. Reg. Sec. 1.61-21(g)(2).] Yes. The valuation rule of this paragraph may be used to value flights on all employer-provided aircraft, including helicopters.

Q: What do we do if the individual flying on the aircraft is not an employee or personal guest of any employee of the company?

A: [Treas. Reg. Sec. 1.61-21(g)(4)(v).] If the individual flying on the aircraft is not an employee or personal guest of any employee of the company, the flight by the individual is not taxable to any employee of the employer providing the flight. The rule in the preceding sentence applies only where the individual is provided the flight by the employer for noncompensatory business reasons of the employer. However, it can also be determined on a facts-and-circumstances basis.

Q: What information do I need to calculate personal use under the SIFL method?
A: The mileage of the personal component of the employer-provided flight, the status of the employee as control or non-control, and the weight of the aircraft. If a security study is in place, the SIFL amount may be decreased, and if the 50%-seating-capacity rule is met, the amount included may be reduced or eliminated.

Q: Can you provide an example of the computation for control and non-control employees?
For purposes of this example, assume a simple flight of one control and one non-control employee, each flying with his or her spouse. They are flying from A to B and back to A, with no stops in between. The distance from A to B is 1,700 mi. And the MTOW of the aircraft is over 25,000 lbs.

Here is an example calculation:

For the Control Employee
First, apply the SIFL rates to the miles of the flight. Note: SIFL rates change every six months. The rates used below are for demonstration only. For the latest SIFL rates, visit the NBAA website at www.nbaa.org/taxes.

0–500 mi. = $0.1684 (500 × 0.1684 = $84.20)

501–1,500 mi. = $0.1284 (1,000 × 0.1284 = $128.40)

Over 1,500 mi. = $0.1235 (200 × 0.1235 = $24.70)

$84.20 + $128.40 + $24.70 = $237.30

Next, multiply the result ($237.30) by the appropriate aircraft multiple (400%):

$237.30 × 400% = $949.20

Next, add in the terminal charge ($30.79):

$949.20 + $30.79 = $979.99

Next, multiply by the number of flights, which in this case is two (2), because it was a round trip:

$979.99 × 2 = $1,959.98

Next, multiply by the number of individuals, which in this case is two (2), control employee and spouse:

$1,959.98 × 2 = $3,919.96

This amount ($3,919.96) is the amount includible in the control employee's income.

For the Non-control Employee
First, apply the appropriate SIFL rate to the flight miles (same as above). Note: SIFL rates change every six months. The rates used below are for demonstration only. For the latest SIFL rates, visit the NBAA website at www.nbaa.org/taxes.

0–500 mi. = $0.1684 (500 × 0.1684 = $84.20)

501–1,500 mi. = $0.1284 (1,000 × 0.1284 = $128.40)

Over 1,500 mi. = $0.1235 (200 × 0.1235 = $24.70)

$84.20 + $128.40 + $24.70 = $237.30

Multiply the result ($237.30) by the appropriate aircraft multiple, which in this case is 31.3%, because this employee is not a control employee:

$237.30 × 31.3% = $74.27

Next, add in the terminal charge ($30.79):

$74.27 + $30.79 = $105.06

Next, multiply by the number of flights, which in this case is two (2), because it was round trip:

$105.06 × 2 = $210.12

Next, multiply by the number of individuals, which in this case is two (2), employee and spouse:

$210.12 × 2 = $420.24

This amount ($420.24) is the amount includible in the employee's income.

Q: How do you determine the seating capacity of an aircraft?
A: [Treas. Reg. Secs. 1.61-21(g)(12)(iii)–(v).] Except as otherwise provided, the regular passenger seating capacity of an aircraft is the maximum number of seats that have at any time on or prior to the date of the flight been on the aircraft while owned or leased by the employer.

Special rules: A company can permanently reduce the seating capacity of an aircraft. However, if the company then restores some seats within 24 months, the IRS will ignore the reduction in seating capacity.

Seating capacity includes only seats that may legally be used during takeoff, provided that the seats that cannot be legally used are, in fact, not used.

Q: When is a flight taxable?
A: Any time an individual travels aboard a company's aircraft for reasons not related to the company's business, the flight is potentially taxable to an employee.

Q: Can an employee pay for the fringe benefit?
A: : [Treas. Reg. Section 1.61-21(b).] Yes. However, the FAA does not allow for reimbursement of personal use of the corporate aircraft (FAA Counsel Opinion 8/8/93), except in limited and narrowly defined circumstances such as when a timeshare agreement is in place. Refer to Section III for more details.

Q: Do SIFL rates change? If so, how often, and how will we know when they have?
A: The SIFL rates change every six months (January 1 through June 30 and July 1 through December 31). Once the revised rates are available, they will be posted on the NBAA website and members will be notified through *NBAA Insider Daily*.

Q: Do we charge a terminal charge for each person or just once for the aircraft? How often do I charge this?
A: The terminal charge is charged for each person flying on the aircraft. In addition, this charge is used for each leg of the trip (both going and returning).

Q: Do I use statute or nautical miles?
A: [Treas. Reg. Sec. 1.61-21(g)(3)(i).] A flight is the distance in statute miles between the place at which the individual boards the aircraft and the place at which the individual deplanes.

Q: Do I have to use SIFL rates? If not, what other method is there?
A: [Treas. Reg. Secs. 1.61-21(b)(6), (7).] The value of a flight deemed taxable can be computed two ways. The first is by how much it would cost a hypothetical person to charter the same or comparable aircraft for the same or comparable flight for flights provided with a crew. The second is by the noncommercial-flight special valuation rule (using SIFL rates). However, the charter-rate method will, in most cases, result in the higher of the two valuation methods allowed. The consistency rules in Treasury Regulations Sections 1.61-21(g)(14)(i), (ii) provide that if the SIFL rules are used for one employee's flight, they must be used for all flights, with the exception of entertainment flights for specified employees.

Q: How do you value a flight?
A: [Treas. Reg. Section 1.61-21(g)(3)(ii).] Under the valuation rule of this paragraph, value is determined separately for each flight. Thus, a round trip comprises at least two flights.

Q: What if there is an intermediate stop?
A: [Treas. Reg. Section 1.61-21(g)(3)(iii).] Additional mileage attributable to an intermediate stop not related to the employee is not considered when determining the distance of an employee's flight. Examples are stops to refuel, to clear customs, or to drop off a passenger who is neither the employee nor the employee's guest.

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II. DEDUCTION DISALLOWANCE

This Section explains the different deduction disallowances that may apply with respect to employer provided flights. These deduction disallowances apply only after the flight first would have been deductible either as a compensatory fringe benefit provided to employees or as a noncompensatory Business flight. For the deduction rules related to sole-proprietor flights, see Section V.

A. ENTERTAINMENT DEFINITION FOR BOTH BUSINESS AND PERSONAL ENTERTAINMENT DEDUCTION DISALLOWANCES

The Personal Entertainment disallowance rules were revised following the issuance of final regulations on August 1, 2012,[105] providing clarity on the rules of the Personal Entertainment deduction disallowance. Since then, new proposed[106] and then final regulations[107] have been issued in response to Business Entertainment changes of the TCJA as enacted in 2017. The final Regulations Sections 1.274 11 and 1.274 12 do not officially revise Regulations Section 1.274 2, which addresses limitations on entertainment deductions and provides a general definition of *entertainment*. Instead, the new Business Entertainment regulations reflect the removal of entertainment as a deductible expense, even where directly related to or associated with business. The existing definition of entertainment in 1.274 2(b)(1), with minor modifications to remove outdated language, is incorporated into the final regulations.[108] Below is a discussion of the most recent final Business Entertainment regulations, including compatible portions of Section 1.274-2 regarding the definition of entertainment and the role of meals in calculating deductible expenses.

1. Basic Definition of Entertainment

Entertainment is generally defined as "any activity which is of a type generally considered to constitute entertainment, amusement, or recreation."[109] It is further defined by the examples of "entertaining at bars, theaters, country clubs, golf and athletic clubs, sporting events, and on hunting, fishing, vacation and similar trips, including such activity relating solely to the taxpayer or the taxpayer's family."[110] Activities identified as entertainment by the courts include sailing, sightseeing, parties and luncheons at the Kentucky Derby, attending the Super Bowl, staying at beachfront property, and parties at the taxpayer's home. [111]

Entertainment may also include "an activity, the cost of which otherwise is a business expense of the taxpayer, which satisfies the personal, living, or family needs of any individual, such as a hotel suite or an automobile to a business customer or the customer's family."[112] Despite this, activities that satisfy personal, living, or family needs are not considered entertainment if the activities are "clearly not regarded as constituting entertainment."[113] The IRS cites hotel suites maintained by employers for employees while in business travel and automobiles used in active conduct of trade or business as examples.

Entertainment is determined on an objective basis.[114] An activity generally considered to be entertainment will be treated as entertainment for tax purposes, irrespective of whether the taxpayer actually enjoyed the activity.[115] For example, in *Walliser,* the taxpayer's sightseeing tour with customers constituted entertainment, even though it was so strenuous for the taxpayers that they did not enjoy it.[116] In determining whether an activity is entertainment, the taxpayer's trade or business is taken into consideration.[117] For example, a trip to the theater would not be classified as entertainment for a theater critic attending the show in that capacity, and a fashion show would not be classified as entertainment for a clothing manufacturer showing clothing to store buyers. [118]

2. Meals

The final regulations provide that for purposes of Section 1.274, the term *entertainment* does not include food or beverages, unless the food or beverages are provided at or during an entertainment activity and the associated costs are not stated separately from the entertainment costs.[119] The price(s) of the separate food and beverage items must also reflect the "usual selling cost for those items if they were to be purchased separately from the entertainment."[120] In the event that this is not possible, the taxpayer must approximate reasonable value.[121]

Additionally, the charges for food and beverages must be reasonable, the taxpayer or an employee of the taxpayer must be present at the presentation of the food or beverages, and the food or beverages must be provided to a business associate in order for the expenses to be deductible.[122] For the purpose of these proposed regulations, *business associate* refers to "a person with whom the taxpayer could reasonably expect to engage or deal in the active conduct of the taxpayer's trade or business such as the taxpayer's customer, client, supplier, employee, agent, partner, or professional advisor, whether established or prospective."[123] These generous regulations establish that where the purpose of a flight is to have a meal or meals with business colleagues at the destination, the flights will not be classified as entertainment and thus not subject to the special disallowance rules for either Personal or Business Entertainment.

B. FOUR BASIC CLASSIFICATIONS OF FLIGHTS

The American Jobs Creation Act of 2004 (the "Jobs Act"), effective in 2005, provides that the compensation exception to the entertainment disallowance is not available for flights provided to specified individuals. Thus employers cannot deduct the costs of flights provided as *compensation* to specified individuals for entertainment purposes. After 2017 and passage of the TCJA, there is now a disallowance of deductions for Business Entertainment flights. Therefore, employers generally must divide flights into four categories: "Business" flights (nonentertainment), "Business Entertainment" flights, "Personal Nonentertainment" flights, and "Personal Entertainment" flights. (In this handbook, the term "Business" flight refers to nonentertainment Business flights.)

In addition to these four basic categories, there are other exceptions to the entertainment classification that can prevent the entertainment disallowance from applying to certain flights discussed in Section II.C below. Furthermore, there are other tax disallowance rules that can that can result in the disallowance of expenses of certain flights discussed in Section II.D below. Among these additional rules is the disallowance of costs of Commuting flights (when not provided to ensure the safety of the employee) pursuant to the TCJA. If these exceptions or disallowance rules apply, they may need to be treated as additional flight classifications in the taxpayer's flight accounting records.

1. Business Flights

Where no entertainment activities occur, the costs of employer-provided flights primarily for the employer's business purposes are generally deductible by the employer and should not result in a taxable fringe benefit to the employee. The distinction between Personal flights and Business flights is discussed in Section I(C) when determining which flights should be included in personal income and which should not be included in income.

As discussed under the income-inclusion rules, Business flights include only flights that are ordinary and necessary to the employer company's business. Furthermore, the primary purpose of the flight for each passenger is analyzed to determine whether that passenger's flight was for a business purpose. Factors examined include the existence of an agenda, time spent on business activities, nature of the locations, and presence of personal guests.

Examples of Business flights are travel to meet with customers or clients, to attend business conferences, to meet with suppliers, to attend board meetings, and for any purpose related to meeting the business goals of the employer company.

As discussed under the imputed-income rules, spouses and personal guests are almost never considered business, as their presence is not an ordinary and necessary business expense.

Where entertainment activities occur during business travel, the analysis becomes more complicated.

2. Business Entertainment Flights

a. General Description of Business Entertainment

The Business Entertainment classification consists of flights that (a) meet the Section 162 trade or business requirement, but (b) are nevertheless travel for entertainment activities. The distinction between business and personal activities is discussed in Section I.C above. As explained above, such flights for business purposes would ordinarily be working condition fringe benefits,[124] and therefore imputed income (SIFL) would not need to be reported for such flights. However, because Business Entertainment flights are for travel to entertainment activities, the costs of such flights are disallowed.

Prior to the TCJA amendment to Section 274(a), entertainment flights that met the "directly related" or "associated with" business tests (explained in more detail in Section II.B.2.c below) could be deducted as business flights. Confusingly, such flights were defined in the entertainment regulations as "Business Entertainment."[125] However, entertainment flights that met the Section 162 trade or business test but failed to meet the more strict "directly related" or "associated with" business tests were disallowed as entertainment travel that did not meet the pre-TCJA Business Entertainment definition. These flights were not defined in the regulations, and they could be referred to as nondeductible business entertainment flights. Post-TCJA, the term Business Entertainment includes both the flights classified under pre-TCJA law as Business Entertainment flights and the flights classified under pre-TCJA law as nondeductible business entertainment.

While pre-TCJA Business Entertainment flights and nondeductible business entertainment flights were treated differently prior to the TCJA, they are now treated the same (nondeductible) with the elimination of the Business Entertainment exception. Post-2017, there is no reason to distinguish between flights that meet the "directly related" or "associated with" tests (formerly Business Entertainment) and nondeductible business entertainment. Both are nondeductible. Therefore, both are now collectively referred to as Business Entertainment.

As previously described, the first task in determining the tax treatment for travel on an employer aircraft is to determine whether the trip is primarily business or primarily personal on a passenger-by-passenger basis.[126] If the trip is primarily personal, then the value will ordinarily be taxable to the passenger (at SIFL rates). It would then be necessary to determine whether the flight is for an entertainment purpose to classify the flight as Personal Entertainment or Personal Nonentertainment. If the flight is primarily for entertainment purposes,[127] then Section 274(e)(2) and Treasury Regulation Section 1.274 10(e) provide rules as to the permissible methods for calculating the deduction disallowance.

However, if the passenger is traveling primarily for a business purpose, and the trip is primarily to engage in an entertainment activity (e.g., playing golf while discussing business with a customer), then it would be a Business Entertainment flight. In that case, it would not be necessary to report the flight as taxable income (SIFL) to the passenger, but the costs of the flight would be nondeductible due to the entertainment disallowance.

b. Cost Allocation Issues

Section II.d below describes the cost allocation regulations for employer-provided flights. These cost allocation rules apply to flights provided as compensation to Specified Individuals.[128] Accordingly, under the regulations, these allocation rules would not apply to Business Entertainment flights. As a practical matter for the sake of internal consistency, most employers will likely use the same cost allocation rules to allocate costs to both Personal Entertainment flights and Business Entertainment flights. Nevertheless, the following describes several issues that may arise from the limitation on the applicability of the cost allocation rules under the regulations.

The new Business Entertainment disallowance may or may not use the "primary purpose of the trip" criterion in judging which expenses of the flight are subject to the disallowance. For example, if the purpose of the trip is five days of business meetings and one day of golf, then if the "primary purpose" method is used, the entire trip would be deductible, as it is primarily for business, but if not used, perhaps only 5/6 of the costs would be deductible. The same unknown applies to how to treat multiple passengers with different purposes on the same flights.

Another unknown is how to calculate the Business Entertainment deduction disallowance and which costs are subject to the new Business Entertainment disallowance. Prior to the issuance of the Section 274(e)(2) guidance regarding Personal Entertainment flights for specified employees, there was the possibility that only the additional expenses related to the flights were subject to the disallowance, but guidance later issued clearly required an allocation of *all costs*, not just the incremental costs, as nondeductible expenses.

c. Pre-TCJA Business Entertainment

The following discussion is relevant for flights occurring prior to 2018, before the TCJA eliminated the exception in Section 274(a) for Business Entertainment flights that met the "directly related" or "associated with" tests.

Under Pre-TCJA law, Business Entertainment travel referred to travel to engage in an entertainment activity if either (i) the entertainment activity is "directly related" to business or (ii) the entertainment activity is "associated with" business and occurs immediately preceding or following a substantial business discussion. Business Entertainment flights were previously fully excluded from taxable income to the passenger and were fully deductible to the taxpayer.

(1) "Directly Related to Business" Requirement

Under the "directly related" test, there must be substantial business discussions at the entertainment event. Considering all the facts and circumstances, the "principal character" of the combined business and entertainment must be the active conduct of the taxpayer's business.[129] If the purpose of the entertainment is to create goodwill with only a general expectation of deriving income or other business benefit in the future, the "directly related" test is not met. Stated otherwise, the "directly related" test is not met if the entertainment is only vaguely or remotely connected with business.[130]

In Churchill Downs, Inc. v. Commissioner, 307 F.3d 423 (6th Cir. 2002), the IRS agreed that a gala, brunch, hospitality tent, and parties were entertainment that was directly related to Churchill Downs' business of operating a horse race. In *United Title Insurance Co. v. Commissioner*, T.C. Memo (RIA) 1988 38, the company's out-of-town meetings with real-estate professionals met the "directly related" test because the meetings were formal, prearranged business meetings in which the company discussed substantive business matters with the real-estate professionals and obtained input from the professionals on a variety of topics. In *Custis v. Commissioner*, T.C. Memo (RIA) 1982 296, the court found that an insurance salesman had met the "directly related" test when he brought potential customers to his hunting lodge for the weekend, because of his discussion of insurance products with the potential customers.

However, in numerous other cases, the courts found that taxpayers had not met the "directly related" test, because the evidence presented did not establish that their business discussions had risen above the level of merely promoting goodwill.[131] In several cases, the entertainment activity enhanced goodwill, thereby meeting the "ordinary and necessary business expense" test under Section 162, but failed to constitute the active conduct of business, thereby failing to meet the "directly related to business" standard.

Entertainment occurring in a "clear business setting" is deemed to meet the "directly related to business" requirement.[132] A clear business setting is one in which the recipient of the entertainment would have reasonably known that the company had no significant motive in incurring the expenditure other than directly furthering its business. An example includes a hospitality room at a convention. In addition, entertainment in a clear business setting may occur when there is no "meaningful personal or social relationship" between the taxpayer and the recipients of the entertainment. For example, the opening of a new hotel or theatrical production where the purpose is to obtain business publicity, rather than to maintain or create the goodwill of the recipients of the entertainment.

In contrast, it is presumed that entertainment will not be directly related to business when it occurs on hunting or fishing trips or on pleasure boats.[133] Also, it is presumed that the "directly related to business" standard is not met when the entertainment occurs in circumstances in which there is little or no possibility of engaging in the active conduct of business.[134] Examples include nightclubs, theaters, sporting events, and parties. They can also include meeting with persons other than business associates at cocktail lounges, country clubs, golf and athletic clubs, or vacation resorts. Both of the presumptions may be rebutted by a clear showing that the taxpayer in fact engaged in the active conduct of business.

For example, in *Townsend*, the court found that the evidence presented by the company regarding the extent of the business discussed at the fishing resort was sufficient to overcome the presumption. However, in *Danville Plywood*, the court noted the distracting atmosphere at the Super Bowl and decided that the taxpayer had not presented sufficient evidence of business discussions to overcome the presumption.

(2) "Associated With Business" Alternative

As an alternative to the "directly related to business" test, a company can qualify its entertainment activity by meeting the "associated with business" test. Under this test, the entertainment activity must be "associated with" the active conduct of business and must occur directly preceding or following a "substantial and bona fide business discussion."[135] Associated entertainment must have a clear business purpose, such as obtaining new business or encouraging continuation of existing business. In general, promoting goodwill with business associates appears to satisfy this "associated with" standard.

A "substantial and bona fide business discussion" is one where there is a substantial business meeting, negotiation, discussion, or other bona fide transaction for the purpose of obtaining income or other specific business benefit. This requires that the principal character of a combined business and entertainment activity be the active conduct of business. A scheduled program at a convention generally will be considered a substantial business meeting if it meets the "ordinary and necessary business expense" requirement under Section 162 and the scheduled program of meetings and presentations is the principal activity of the convention.

Presumably, the "associated with business" test would be met by the conventions in *Peoples Life* and *Acacia* cases, discussed previously in Section I.C.3.a ("Classification of Flights by Spouse, Family, and Personal Guests") and in Section I.C.1.a.(3) ("Examples of Business Travel").

To meet the requirement that the associated entertainment occur directly preceding or following the substantial business discussion, the entertainment generally must occur on the same day as the business discussion.[137] However, the regulations also would include entertainment occurring in the evening before a substantial business discussion. For example, taking a business associate from out of town to dinner and a show on the evening of his or her arrival, prior to meetings the next day, would satisfy the "directly preceding" requirement.

3. Personal Nonentertainment Flights

The Jobs Act amended the entertainment-disallowance rules, denying deductions for entertainment flights by specified employees, but the change did not affect the employer's ability to deduct the costs of *nonentertainment* Personal flights provided to an employee as compensation.[138] The value of such flights would be reported to the employee as a taxable fringe benefit, ordinarily at SIFL rates. This category of flights includes flights provided as compensation to specified individuals for nonentertainment personal purposes.

Personal nonentertainment flights are flights that do not qualify as Business flights but are not for an entertainment purpose. The distinction between Business and Personal flights is discussed above in Section I ("Ordinary and Necessary Business Expenses").

As stated in Section II.A.1, entertainment activities are those ordinarily considered to constitute entertainment, amusement, or recreation. Examples from the Treasury Regulations include entertaining at nightclubs, cocktail lounges, theaters, country clubs, golf and athletic clubs, and sporting events and on hunting, fishing, vacation, and similar trips. Examples from court decisions include sailing, sightseeing, parties and luncheons at the Kentucky Derby, attending the Super Bowl, staying at beachfront property, and parties at the taxpayer's home. The determination should be made according to the principal character of the trip, using an objective standard and taking into consideration the business of the taxpayer.

Treasury Regulations Section 1.274 2(b)(1) provides some guidance in distinguishing between personal nonentertainment activities and personal entertainment activities by pointing out that "routine personal activities" are not entertainment activities. The regulation provides the example of commuting to and from work. The preamble to the proposed regulations provides as additional examples of personal nonentertainment activities "attending to business other than that of the employer, medical purposes, attending funerals and participating in charitable activities."[139] The IRS has also provided visiting sick relatives and going to the grocery store as examples of nonentertainment activities.[140]

Based on the above guidance, several other activities that ordinarily appear to be nonentertainment activities include personal investment activities, meetings with legal or accounting advisors, and the taking of a child to boarding school or college. Travel between a taxpayer's residences generally appears to be nonentertainment travel for the same reasons that commuting is nonentertainment, unless the trip is to a second residence specifically to engage in a particular entertainment activity. Whether travel to visit relatives who are not sick is entertainment may depend on the activities undertaken on the trip. Visiting relatives to play golf probably is entertainment, but discussing a particular family issue does not appear to be entertainment.

To distinguish between business and entertainment, an objective test is applied taking into consideration the taxpayer's occupation. To distinguish between personal entertainment and personal nonentertainment, it seems reasonable to consider other objective factors regarding what a person ordinarily considers to be entertainment, amusement, or recreation.

For example, visiting with relatives in their home may be a routine personal activity, while visiting with them in a beachfront rental property may be an entertainment activity. In both cases, the determination based on the circumstances seems to be more appropriate as a presumption than as a final conclusion.

4. Personal Entertainment Flights

This Section addresses the deduction rules for Personal flights that are characterized as for entertainment purposes. The TCJA expanded and changed the deduction rules applicable to Business flights characterized as entertainment for taxable years beginning after 2017, as discussed in Section II.B.2 ("Business Entertainment").

As explained in Section II ("Imputed Income for Personal Flights"), when an employer provides a flight to an employee as a fringe benefit for services, the value of the flight must be reported to the employee as a taxable fringe benefit. Most employers report the value using SIFL rates rather than the charter-rate method because SIFL rates generally result in less imputed income.

Prior to the Jobs Act, the case of *Sutherland Lumber-Southwest, Inc. v. Commissioner*, 255 F.3d 495 (8th Cir. 2001), acq. 2002 1 C.B. xvii, held that the entertainment disallowance under IRC Section 274(a) did not prevent the deduction of any costs of Personal flights provided to employees, because they fell within the exception in Section 274(e)(2) for costs incurred to provide compensation.

The Jobs Act modified the compensation exception in Sections 274(e)(2) and (9) to the entertainment disallowance rules to provide that the exception is not available to "specified individuals" except to the extent of the amount of the taxable fringe benefit reported to the specified individual.

For example, suppose a flight is provided to a specified individual to go on vacation and the employer reports a value of $1,000, under the SIFL-rate method, to the specified individual as a taxable fringe benefit on Form W 2. Suppose further that the employer's cost of providing the flight is $5,000. The entertainment disallowance would require the employer, on its federal income tax, to reduce its otherwise allowable deductions for the operation of the aircraft by the $4,000 difference between the two amounts. In contrast, if the Personal flight was not for entertainment (or commuting) purposes or if it was provided to a nonspecified individual, then the full $5,000 would be deductible.

The following sections discuss the Personal Entertainment disallowance and the mechanics of allocating costs between deductible and nondeductible flights under rules in the final Treasury Regulations, applicable to taxable years beginning after August 1, 2012.[141]

Costs of flights constituting dividends or excessive compensation would be nondeductible, without regard to the entertainment disallowance or the specified individual status of the passengers.[142] Therefore, such flights do not appear to be subject to the passenger-by-passenger cost-allocation rules that appeared in the proposed regulations.

a. Specified Individuals

The term "specified individual" is defined as any individual who is subject to Section 16(a) of the Securities Exchange Act of 1934 with respect to the company, or any individual who would be subject to it if the company were an issuer of equity securities subject to the Securities Act. [IRC Section 274(e)(2)(B); Prop. Treas. Reg. Sec. 1.274-9(b).] Under these rules, specified individuals generally include officers, directors, and 10% owners.[143] Officers are defined by reference to securities laws and include the principal financial officer, principal accounting officer or controller, vice presidents in charge of a principal business unit, division, or function, and any other officer who performs a similar policymaking function.[144]

b. Spouse, Family, and Personal Guests

A flight provided to a guest or family member of a specified individual is considered provided to the specified individual for purposes of the entertainment disallowance because of that person's relationship to the specified individual.[145]

As discussed in Section I.C.3.a ("Classification of Flights by Spouse, Family, and Personal Guests"), travel by the spouse of an employee is generally not deductible as a business expense when the spouse's only business function is to greet and socialize. Therefore, it is usually necessary to report a taxable fringe benefit to the employee with respect to a nonemployee spouse. However, in rare instances where there is a bona fide business purpose for the spouse's presence, the value of the spouse's travel as a fringe benefit does not need to be reported.

If the spouse's travel does not meet the "bona fide business expense" standard and therefore the value of the flight is reported to the employee, the employer must consider whether the spouse is traveling for entertainment or nonentertainment purposes. If the spouse does not engage primarily in activities that ordinarily constitute entertainment, amusement, or recreation, it should be appropriate to classify the spouse's flight as personal nonentertainment travel.

As explained in Section I.C.3.b ("Travel Deduction Limitation Under Section 274(m)(3)"), the employer's deduction typically will not be affected by the deduction limitation in IRC Section 274(m)(3) on travel by spouses, dependents, and personal guests.

c. Security Concerns

As noted in Section I.E.3.a ("Business-Oriented Security Concerns"), when there is a bona fide business-oriented security concern and certain other requirements are met, the amount of the taxable fringe benefit to the employee for Personal flights is calculated with a 200% cap on the aircraft multiple. There is no similar rule to reduce the entertainment disallowance for an aircraft.[146] Accordingly, it would likely be difficult to convince the IRS to permit the deduction of otherwise disallowed costs of entertainment travel on the grounds that the additional expenses attributable to the private aircraft are for security reasons.

d. Allocation of Costs

(1) Allocation Methods

In the past, costs were allocated among flights in proportion to the number of miles or hours of the flight according to the primary purpose of each flight, without allocating costs of a flight among the passengers who may be traveling for different purposes.[147] As noted below in Section V.B ("Allocation of Costs – 'Primary Purpose' Method"), the "primary purpose" method appears to remain applicable to sole proprietors. While the "primary purpose" method remains generally applicable to a company's flights, the IRS issued final regulations explaining that to allocate costs to determine the entertainment disallowance, companies must use either the "occupied seat method" or the "flight by flight" method.[148] Both of these methods allocate costs based on each passenger's purpose for traveling.

Before issuance of the final regulations, a company could argue that the "primary purpose" test applied to entertainment flights provided as compensation to specified individuals according to existing case law, since the passenger-by-passenger allocation methods were only discussed in proposed regulations and an IRS Notice.[149] However, with the issuance of the final regulations in 2012, companies are now required to use the passenger-by-passenger allocation methods.

These passenger-by-passenger allocation methods apply only to flights for which the compensation deduction is limited under the exception to the entertainment disallowance in the Jobs Act amendment. IRC Sections 274(e)(2) and (9), as amended by the Jobs Act, provide that the compensation exception is only available to specified individuals to the extent of the amount reported as income to them or received from them as reimbursements. This means that the passenger-by-passenger allocation methods apply to flights provided as compensation to specified individuals traveling for entertainment.

The "primary purpose" method would continue to apply in determining the entertainment disallowance for entertainment flights not provided as compensation, irrespective of whether the recipient of the flight is a specified individual. For example, a company could not deduct the costs allocated under the "primary purpose" method to a flight solely to transport customers to an entertainment event.

The two passenger-by-passenger allocation methods are described below. Appendix 1 provides an example of these calculation methods from the proposed regulations, with step-by-step instructions. Under both methods, the calculation may be performed in either hours or miles. For convenience only, the below explanations of the methods refer only to hours. In addition, in the explanations, the references to specified individuals include their family and personal guests traveling on the flight.

Each year, the company may select either method and use either miles or hours. As a result, companies typically

perform the calculation four different ways – under both methods and both miles and hours – and use the result that produces the lowest entertainment-disallowance amount.

Companies typically perform this calculation using a spreadsheet or other software. They often rearrange the order of the steps in these calculations to determine the entertainment-use percentages under the four methods. The lowest entertainment-use percentage can then be multiplied by total costs, and the SIFL amount for entertainment flights of specified individuals and their guests can then be subtracted from the result to determine the net disallowed entertainment expense.

(i) Occupied-Seat Method

Under the occupied-seat method, the company must determine the total number of occupied-seat hours (or miles) flown for the year. The occupied-seat hours for any particular flight are the number of hours for the flight multiplied by the number of passengers on the flight. The cost per occupied-seat hour is calculated by dividing the total annual operating costs by the total number of occupied-seat hours for the year. For each specified individual on each flight, the cost per occupied-seat hour is multiplied by the number of hours flown by the specified individual and his or her guests for entertainment. This entertainment cost for each specified individual for each flight is then reduced by any amounts reported as taxable fringe benefits or received as payment for the flight (e.g., time-sharing payments) to determine the net entertainment cost for the specified individual for the flight. These net entertainment costs for each specified individual on each flight are then added together to determine the total entertainment disallowance for the year.

(ii) Flight-by-Flight Method

In general, under the flight-by-flight method, the company must determine the total number of hours (or miles) flown for the year. The cost for each flight is calculated by multiplying the total annual operating costs for the year by the ratio of hours for the flight over total hours flown during the year. For each flight with a specified individual or his or her guest traveling for entertainment, the cost of the flight is divided by the total number of passengers, and the result is multiplied by the number of specified individuals and their guests traveling for entertainment purposes.

This amount is then reduced by any amounts reported as taxable fringe benefits or received as reimbursement with respect to the specified individual or guest for the flight (e.g., time-sharing payments) to determine the net entertainment cost subject to the entertainment-expense disallowance for the flight. These net entertainment costs for each specified individual on each flight are then added together to determine the total entertainment disallowance for the year.

(iii) Multi-leg Flights

When a trip consists of multiple segments and not all of them are for entertainment purposes, only the marginal hours (or miles) attributable to the entertainment travel are counted as entertainment.[150] For example, suppose an individual travels from City A to City B for business and from City B to City C for entertainment and returns to City A. In that case, the flight from City A to City B would be treated as Business. In addition, an equal number of miles (or hours) would be treated as business miles for a hypothetical return trip from City B directly back to City A. The entertainment hours (or miles) would be the excess of the actual hours (or miles) flown from City B to City C and from City C to City A over the number of hours (or miles) in the hypothetical Business flight from City B back to City A.

This special rule for multi-leg flights is generally favorable to the company since it tends to minimize the number of hours (or miles) treated as entertainment.

This rule is similar to the multi-leg rule for SIFL flights discussed in Section I.E.2. ("Multi-leg Flights"), except that rule requires a determination that the primary purpose of the multi-leg flight is business or personal. In contrast, the multi-leg-flight rule, for purposes of the entertainment disallowance, effectively assumes that the trip is primarily for business and only treats the marginal hours (or miles) as entertainment incurred to travel to the entertainment destination.

(iv) Deadhead Flights

- **Deadhead-flight calculation indicated by examples in final regulations issued in 2012**

A deadhead flight is a repositioning flight with no passengers after dropping off passengers or to pick up passengers. For example, a return flight from transporting an executive and spouse to a vacation destination with only the crew on-board. For the entertainment-disallowance rules, a deadhead flight is treated as having the same number of passengers traveling for the same purposes as the occupied flight to which the deadhead flight relates.[151] Therefore, when there is one occupied flight from the aircraft's base to another location and a second deadhead return flight, the deadhead return flight ordinarily will be treated as having the same number of passengers traveling for the same purposes as the first flight. This treatment contrasts with the SIFL rules, which provide that no SIFL income inclusion is required for a deadhead flight, as explained in Section I.E.

Identifying the occupied flight to which a deadhead flight relates is more difficult in the case of a multi-leg trip with one or more deadhead segments. The regulations state that the character of the deadhead flight should be "based on" the two occupied flights. The preamble to the final regulations explains that this does not mean that taxpayers can use any reasonable method to determine the disallowance for a deadhead flight.[152] However, the regulations do not specify a particular method for making the allocation. Instead, the final regulations provide two example calculations, both of

which suggest that taxpayers should use a weighted-average calculation to determine the deemed number and purpose of passengers on a deadhead flight related to two occupied flights.[153] Unfortunately, both examples appear to contain errors, which complicates taxpayers' burden of complying with the regulations.[154]

- **Alternative to deadhead-flight calculation indicated by multi-leg-flight rule**

The disallowance calculations for deadhead flights on multi-leg trips is further complicated by the fact that these flights are also covered by the multi-leg-flight rule discussed in Section I.E. ("Multi-leg Flights"). The multi-leg-flight rule differs from the deadhead-flight calculation indicated by the examples above. When there is a Business flight, an entertainment flight, and a deadhead flight, the multi-leg-flight rule calls for the entertainment flight and the deadhead flight to be analyzed together as a hypothetical Business flight returning from the actual Business flight with a detour for entertainment purposes.

Under the multi-leg rule, the total number of miles (or hours) on the deadhead and entertainment flights combined would be classified as business miles (or hours) to the extent of the number of miles (or hours) on the Business leg, with the remaining miles (or hours) classified as entertainment. The hypothetical Business flight would have the same number of passengers traveling for the same purposes as on the actual Business flight. The excess miles (or hours) classified as entertainment would have the same number of passengers traveling for the same purposes as the actual entertainment flight.

(2) Aggregation of Aircraft

The cost-allocation methods can be applied to each aircraft separately or to the aggregate miles (or hours) of a group of aircraft having "similar cost profiles."[155] Aggregating the cost allocations for multiple aircraft may be beneficial, particularly if the specified individuals and their guests use the newest aircraft with the greatest depreciation deductions for entertainment flights. When aircraft are not aggregated, it is necessary to allocate the costs of operating the aircraft among all aircraft to apply the cost-allocation rules separately to each aircraft.

Aircraft have similar cost profiles when their operating costs per hour or per mile are comparable. To be aggregated, the aircraft must have the same engine type (jet or propeller) and have the same number of engines. Other factors to be considered include payload, passenger capacity, fuel-consumption rate, age, maintenance costs, and depreciable basis.

e. Recordkeeping

Adequate documentation with respect to each Business and Personal nonentertainment flight is critical to support the company's ability to deduct the costs of the flights. The importance of maintaining adequate documentation on a contemporaneous basis with respect to Business flights is crucial and required by IRC 274(d)(4). These substantiation rules presumably require the same level of documentation regarding the nonentertainment character of the passengers' activities on Personal nonentertainment flights. Since the entertainment-disallowance rules apply on a passenger-by-passenger basis, it is important to record this information with respect to each passenger.

It is often difficult for company staff to obtain detailed information from passengers regarding the nature of their personal nonentertainment activities. Nevertheless, the accounting records should include as much detail as possible regarding the passengers' nonentertainment activities for any flights classified as Personal nonentertainment travel. It may also be helpful for the records to affirmatively state that the passengers did not engage in entertainment activities like hunting, fishing, or attending sporting events.

f. Leasing and Chartering Aircraft

Private aircraft are owned and operated in a variety of arrangements. An aircraft could be leased or chartered from an owner entity to a commonly owned operating company that provides the use of the aircraft to employees. The aircraft could be leased by a company to its individual owner, who separately hires the crew to fly the aircraft. An operating company could provide the use of its aircraft to its employees under a charter arrangement or a time-sharing agreement. Alternatively, the company could place its aircraft with a charter operator to provide charter service to employees of the company and to third parties. In each of these cases, the company may need to address the question of whether and how to apply the entertainment disallowance to an aircraft that is leased or chartered to another party.

When an aircraft is leased or chartered to third parties, it may be difficult to obtain information regarding the number of passengers on each flight or their purposes for traveling. In recognition of this difficulty, the regulations provide that when an aircraft is leased or chartered to unrelated third parties for adequate and full consideration, expenses allocable to the lease or charter are excluded from the entertainment-disallowance calculation.[156] Presumably, the miles and hours involved in the lease or charter are also excluded from those calculations.

Since the preamble to the proposed regulations makes it clear that the proposed regulations do not address the "adequate and full consideration" exception, this should not be interpreted to mean that the "adequate and full consideration" exception only applies to leases or charters to unrelated third parties.[157]

g. Costs Subject to Personal Entertainment Disallowance

The costs subject to the entertainment-disallowance calculation include all out-of-pocket expenses of the flights and all costs with respect to the aircraft. These include all fixed and variable costs of operating the aircraft.[158] The regulations list examples of expenses subject to the disallowance: salaries for pilots, maintenance personnel, and other personnel assigned to the aircraft; meal and lodging expenses

for the flight personnel; takeoff and landing fees; costs for maintenance flights; costs of onboard refreshments, amenities, and gifts; hangar fees (at home or away); management fees; costs of fuel, tires, maintenance, insurance, registration, certification of title, inspection, and depreciation; interest; and all costs paid or incurred for aircraft leased or chartered to or by the taxpayer.

(1) Overhead and Tax Preparation

It is important to note that all of these costs subject to the entertainment-disallowance calculation relate directly to the aircraft. The list of examples from the regulations as well as guidance from existing regulations do not appear to contemplate the allocation of corporate overhead or other indirect costs to an aircraft operation.[159] For example, it would not appear appropriate to include a percentage of the costs of the company's human-resources and payroll departments allocable to hiring and paying the pilots. Furthermore, costs relating to tax-return preparation, such as the costs of calculating the entertainment disallowance, should not be subject to the disallowance. However, it would seem appropriate to include specifically identifiable costs, such as legal fees or consulting fees related to the aircraft.

(2) Maintenance Flights

Costs subject to the disallowance include the cost of maintenance flights. This is consistent with the occupied-seat method, which only considers flights with occupied seats and related deadhead flights. Since a maintenance flight is not included in either the numerator or the denominator of the occupied-seat-method calculation, the cost of the maintenance flight is effectively included in the costs allocated between entertainment and nonentertainment flights under the occupied-seat method. In fact, under the occupied-seat method, the costs of training flights and any other flights for purposes other than transporting passengers are effectively allocated between entertainment and nonentertainment flights.

The treatment of maintenance and training flights is less clear under the flight-by-flight method. The denominator under the flight-by-flight method is the total hours (or miles) flown for the year.[160] Therefore, it can be argued that maintenance and training flights are included in the denominator in the allocation of expenses, thus reducing the amount subject to the disallowance. Courts interpreting similar flight-allocation ratios have reached different results on this issue, suggesting that it is an open question whether the denominator of the allocation ratios under the flight-by-flight method should include the hours (or miles) flown for maintenance and training flights.[161]

(3) Straight-Line Election for Depreciation

Accelerated depreciation and bonus depreciation were enacted to encourage investment in capital equipment, and those goals may be thwarted by the entertainment-disallowance rules, which would disallow a portion of enhanced-depreciation deductions. In response to this concern, the regulations permit companies to elect to calculate the entertainment disallowance using a depreciation amount calculated under the straight-line method over the alternative-depreciation life of the aircraft.[162] If a company elects this method, only the straight-line depreciation amount will be included in the disallowance calculation, and all the depreciation in excess of the straight-line amount will be fully deductible.

This straight-line-depreciation election can produce a significant benefit, but companies must consider the implications. Once the depreciation election is made, it can only be revoked with IRS permission pursuant to a private-letter ruling as long as the company provides the use of aircraft to its employees. In addition, the transition rule provides that the straight-line depreciation amount for the year of the election is determined as if straight-line depreciation had been used in all prior years for the aircraft.[163] By failing to make this adjustment prospectively, the transition rule causes more than 100% of the adjusted basis of the aircraft to be subject to the entertainment-disallowance calculation.

The final regulations limit the disallowance of depreciation calculated under the straight-line election in any year to the total amount of depreciation on the aircraft in that year.[164] This limitation can have a beneficial effect for taxpayers deducting 100% bonus depreciation and making the straight-line election. For example, if a company deducts 100% bonus depreciation in the year of aircraft acquisition and makes the straight-line election, the entertainment disallowance will be calculated on the relatively small straight-line depreciation amount in the first year. In subsequent years, since there would be no depreciation (because 100% was deducted in the first year), the limitation added by the final regulations means that there would be no disallowance of depreciation in such subsequent years.[165]

(4) Interest Expense

Interest expense is listed in the final regulations as an example of expenses to include in the cost-disallowance calculation.[166] Following the effective date of the final regulations, it must be included in the expenses subject to the entertainment disallowance.

Under the final regulations, there is a broad rule for identifying interest expense subject to the disallowance, meaning that costs subject to the disallowance include interest on debt that is "secured by" or "properly allocated (within the meaning of Section 1.163 8T) to" the aircraft. These broad tests can lead to unexpected results. For example, if a company has a large loan secured by all of its assets, including its aircraft, then (reading the rule literally) all the interest expense on the loan would be subject to the disallowance. As another example, if a company has a large loan and the proceeds are placed in its bank account, then cash drawn from the bank account to acquire the aircraft may cause a portion of the loan to be subject to the disallowance under the interest-tracing rules in Treasury Regulations Section 1.163 8T. Under these interest-tracing rules, loan proceeds

deposited into a cash account may be treated by the company as traced to any expenditure from any cash account within 30 days before or after the deposit. [167]

The proposed regulations did not mention interest expense, so companies may have a reasonable argument that it should not be included in costs subject to disallowance prior to the effective date of the final regulations.[168] Interest was also omitted from the list of costs subject to disallowance in IRS Notice 2005 45, 2005 1 C.B. 1228, Section B(4), which predated the proposed regulations, and, it was also omitted from regulations regarding the entertainment-facility disallowance.[169] Furthermore, IRS rulings omit any reference to interest as subject to the entertainment disallowance.[170] However, the tax court in Helwig v. Commissioner, T.C. Memo (RIA) 1999 386, apparently accepted the parties' consensus that interest expense is subject to the entertainment disallowance.

C. EXCEPTIONS TO PERSONAL AND BUSINESS ENTERTAINMENT DISALLOWANCES

The following specific exceptions are cited as excludable for purposes of calculating the entertainment-cost disallowance. Thus, a flight that is otherwise not deductible as a Business Entertainment flight could nevertheless be deductible if one of these exceptions applies.

1. Recreational, etc. Expenses for Employees

Section 274(e)(4) provides,

Expenses for recreational, social, or similar activities (including facilities therefor) primarily for the benefit of employees (other than employees who are highly compensated employees (within the meaning of section 414(q) which is $130,000 of annual compensation in 2020, indexed yearly)). For purposes of this paragraph, an individual owning less than a 10-percent interest in the taxpayer's trade or business shall not be considered a shareholder or other owner, and for such purposes an individual shall be treated as owning any interest owned by a member of his family (within the meaning of Section 267(c)(4)). This paragraph shall not apply for purposes of subsection (a)(3).

There have been few cases interpreting this exception. The favorable case of *American Business Service Corp. v. Commissioner*, 93 TC 449, Code Secs. 162, 274 (Oct. 3, 1989), allowed for the expense deduction for fees to charter boats for cruises supplied to permanent, but not the numerous temporary, employees. Although the court rejected the taxpayer's argument that temporary workers were not employees, the deduction was allowed for expenses primarily for the permanent employees' benefit. The court noted that the deduction under the statute does not require that all employees have access to recreational facilities, as long as access is based on a nondiscriminatory, reasonable, and realistic method of selecting participants. Also, of interest in this favorable case was that the majority of employees were not aware of the boat.

In an unfavorable case, *Harry L. Snyder, et al.*, TC Memo 1983-692, Code Secs. 79, 105, 162, 164, 212, 267, 269, 274, 301, 1012, 6653(a), 7442 (Nov. 23, 1983), the court disallowed certain entertainment, gift, and travel expenses and the cost of entertainment facilities. The taxpayer corporation was denied deduction for the maintenance of riding horses, and the expenditures were a constructive dividend to the shareholder whose family used horses. The taxpayer had not shown use of horses by employees other than the shareholder's children.[171]

Because of the 100% Business Entertainment disallowance, there will be increased focus on when this exception might apply. However, for private air travel, the exception will not often apply, because an executive is not typically flying to a destination for the purpose of attending a nondiscriminatory entertainment event for employees. However, an example of a fully deductible entertainment flight would be a CEO flying from his office to a resort for a company-wide entertainment event for all employees or to a holiday party in another city.

2. Employee, Stockholder, etc. Business Meetings

Section 274(e)(5)[172] provides an exception from the entertainment disallowance for

[e]xpenses incurred by a taxpayer which are directly related to business meetings of his employees, stockholders, agents, or directors.

The regulations also include partners in a partnership.[173] The exemption applies only if the meeting is held principally for trade or business purposes. Examples are board of directors' meetings or annual company leadership conferences. The exemption would *not* apply to (1) primarily social or nonbusiness meetings where there is little or no possibility of engaging in active business activities or (2) meetings or conventions for the principal purpose of rewarding employees, agents, directors, partners, etc. for their services.[174]

In an unfavorable case addressing this exception, *Superior Container, Inc.* TC Memo 1980 434 (Sept. 29, 1980), the court stated that there was insufficient substantiation under Section 274(d) to support the "business meetings" exception where a condominium in Naples, Florida, appeared to be used for vacation purposes and evidence to the contrary was not presented.

3. Meetings of Business Leagues, etc.

Section 274(e)(6) provides,

Expenses directly related and necessary to attendance at a business meeting or convention of any organization described in Section 501(c)(6) (relating to business leagues, chambers of commerce, real estate boards, and boards of trade) and exempt from taxation under Section 501(a).

Thus, travel to attend such meetings would not be disallowed under the Business Entertainment disallowance.

4. Items Available to Public

Section 274(e)(7) provides,

Expenses for goods, services, and facilities made available by the taxpayer to the general public.

Thus, expenses related to the aircraft that is made available to the general public would remain deductible even when used for entertainment.

5. Entertainment Sold to Customers

Section 274(e)(8) provides the most significant exception to the deduction-disallowance rules and should be explored where there is a payment for the aircraft, both dry-leased or with a crew.

Section 274(e)(8) provides,

Expenses for goods or services (including the use of facilities) which are sold by the taxpayer in a bona fide transaction for an adequate and full consideration in money or money's worth.

Section 274(e)(8) provides an exception from the entertainment-deduction disallowances for both Business and Personal where a payment or reimbursement is made. This exception simply states that: where a taxpayer is selling an item or providing a service used by the purchaser for an entertainment purpose, the seller is not *providing* entertainment – it is *selling* entertainment.

For example, Personal Entertainment expenses related to a vacation by a CEO and spouse are $100,000. The CEO reimburses for the flight under the Nichols opinion, or pays a charter company for use of the aircraft, in an amount equal to a full arm's-length charter rate of $20,000. Using the exception of Section 274(e)(8), the employer would deduct the full $100,000.

When the aircraft is leased or chartered to *unrelated third parties*, ordinarily the rate charged is respected as a fair-market charter rate and the "adequate and full consideration" exception would apply to the lessor, or charter company.[175]

For leases or charters to *related parties*, if a flight is paid for by the executive, at arm's-length rates and terms, then the "adequate and full consideration" exception ordinarily should apply to prevent the entertainment disallowance from applying to the lessor, or charter company.[176] However, the IRS is likely to scrutinize such transactions carefully. Also, the discussion of the "adequate and full consideration" exception in the preamble to the proposed regulations suggests that the IRS intends to interpret the "adequate and full consideration" exception narrowly.[177] Whether time-sharing arrangements will fall within this exception is unclear because time-sharing rates are typically below fair-market charter rates, it seems unlikely they would be sufficient to invoke the "adequate and full consideration" exception. However, some taxpayers argue that the time-sharing lessor is charging the maximum rate allowed by law and thus should be covered by the exception.

Favorably, Proposed Regulations Section 1.274 13(e)(2)(iii), addressing qualified transportation disallowance, provides that for purposes of the Section 274(e)(8) exception, the term "customer" includes an employee of the taxpayer who purchases the transportation in a commuter highway vehicle, a transit pass, or parking in a bona fide transaction for an adequate and full consideration in money or money's worth. Thus, since Section 274(e)(8) applies to purchases by employees for other types of transportation, it is reasonable that it should apply to reimbursements by executives for air transportation.

Section 1.274-2(f)(ix), following legislative history,[178] provides,

Any expenditure by a taxpayer for entertainment (or for use of a facility in connection therewith) to the extent the entertainment is sold to customers in a bona fide transaction for an adequate and full consideration in money or money's worth, is not subject to the limitations on allowability of deductions provided for in paragraphs (a) through (e) of this section. Thus, the cost of producing night club entertainment (such as salaries paid to employees of night clubs and amounts paid to performers) for sale to customers or the cost of operating a pleasure cruise ship as a business will come within this exception.

The IRS ruled that related parties commonly owned by the shareholder are treated separately for purposes of the entertainment disallowance. In Technical Advice Memorandum 200214007 (Apr. 5, 2002), a husband and wife owned almost all the stock of two S corporations. Taxpayer, which is one of the S corporations, was incorporated for the sole purpose of developing and operating an entertainment facility. The facility was primarily used by B, the second S corporation. The facility was used for charity events and tournaments and by the employees and clients of B, for a fee. Taxpayer argued that it did not operate the facility for its own recreation or entertainment and thus, Section 274(a)(1)(A) did not apply to it. The IRS allowed Taxpayer to take a deduction under IRC Section 274(e)(8) for expenses incurred in operating the facility. It noted that tax law generally recognizes the existence of separate entities and that the corporate form may only be disregarded where it is a sham or unreal. Taxpayer received revenue from its operation, but despite common ownership of Taxpayer and B, the absence of facts indicating that Taxpayer was a sham entity meant the IRS could not disregard the separate corporate existences of related entities.

In summary, where an executive dry-leases an employer aircraft for an arm's-length price, the transaction may not be considered entertainment at all, as the employer would not have knowledge of the end use as entertainment. In the case of a purchase of a flight complete with crew, if the executive pays a full arm's-length price for the charter, it is also sustainable that the exception of Section 274(e)(8) applies.

D. OTHER DEDUCTION-DISALLOWANCE RULES

In addition to the four basic classifications of flights arising from the business/personal and entertainment/nonentertainment classification (discussed in Section II.B above), there are additional rules that can result in the disallowance of deductions for flights. To the extent that these rules apply, it may be necessary for a company operating an aircraft to establish additional flight classifications for purposes of its flight tax accounting.

1. Travel-Deduction Limitation Under Section 274(m)(3) on Spouses, Dependents, and Personal Guests

IRC Section 274(m)(3) limits a company's deduction with respect to spouses, dependents, and personal guests accompanying employees on business travel. As discussed under the imputed-income rules, Treasury Regulations Section 1.132 5(t)(1) provides that the disallowance under Section 274(m)(3) does not affect the determination of whether the company must report imputed income with respect to the spouse, dependents, and personal guests.

However, restrictions on the application of this rule means it has little effect on most companies. Section 274(m)(3) provides that no deduction is allowed for travel expenses of a spouse, dependent, or other individual accompanying the taxpayer (or an officer or employee of the taxpayer) on business travel, unless *all* the following criteria are met: (1) the accompanying person is an *employee* of the taxpayer; (2) the accompanying person's travel is for a bona fide business purpose; and (3) the travel expenses would otherwise be deductible by the accompanying person. For this purpose, the reference to individuals accompanying the taxpayer does not include business associates.[179] Business associates are persons with whom a taxpayer would reasonably expect to engage or deal in the active conduct of the taxpayer's business.[180]

With respect to the employer's deductions, Treasury Regulations Section 1.132 5(t)(1) provides that Section 274(m)(3) does not apply if the fringe benefit is reported for the travel by the accompanying spouse, dependent, or personal guest. Accordingly, reporting the SIFL value of these individuals' personal flights is important to retain the deduction of any incremental costs, but also to avoid failure to report income (with the related penalties and interest) for failure to withhold employment taxes where the host passenger is an employee.

If an accompanying spouse, dependent, or personal guest is found to be traveling for business purposes under the "ordinary and necessary business expense" standards described above, and the travel is not disallowed under the entertainment-disallowance rules, then Section 274(m)(3) applies, to limit the employer's deduction with respect to that accompanying individual. In that situation, Section 274(m)(3) typically applies because the accompanying individual is usually not an employee. However, the amount of the disallowance ordinarily is equal to only the marginal costs of the accompanying individual's travel, which are typically negligible (e.g., additional catering charges). The marginal-cost approach appears to apply because (1) the passenger-by-passenger allocation of costs discussed in Section II.B.4.d ("Allocation of Costs") only applies with respect to the entertainment disallowance under IRC Section 274(e)(2) and (2) the deduction disallowance for accompanying nonbusiness passengers is generally limited to marginal costs.[181]

2. Publicly Held Corporations

Publicly held corporations are subject to an expense-disallowance rule under IRC Section 162(m), which precludes compensation deductions in excess of $1 million for the CEO and the other four highest-paid employees, known as covered employees. There are exceptions, such as for commission-based or performance-based compensation. When a covered employee's compensation exceeds the $1 million cap, the employer cannot deduct the cost of non-Business flights provided to the covered employee.

In the case of a covered employee's entertainment flights, the company would otherwise be able to deduct only the amount it reported to the employee as a taxable fringe benefit, ordinarily at SIFL rates. The application of the Section 162(m) limitation takes away the company's ability to deduct the costs in the amount of this fringe benefit.[182]

In the case of a covered employee's Personal nonentertainment flights, the company is otherwise able to deduct the full amount of the cost of the flight. Since Section 162(m) applies to the deduction of compensation, it appears that the Section 162(m) disallowance prevents the company from deducting the cost of the flight in the amount of the reported fringe benefit. However, the costs of the flight in excess of this amount may still be deductible by the company.

3. Foreign Travel

As explained in Section I.E.3.b ("Foreign Travel"), the foreign-travel-disallowance rule in IRC Section 274(c) should not affect an employer's ability to deduct costs with respect to a foreign trip. It could only require the reporting of imputed income to an employee who engages primarily in personal activities on at least 25% of the days on a foreign trip lasting more than one week. However, this rule could result in the disallowance of deductions for sole proprietors, who should refer to I.E.3.b ("Foreign Travel") for more information. Nothing in the foreign-travel rules or the entertainment-disallowance rules suggests that the foreign-travel rules trigger the disallowance of expenses under the entertainment disallowance.

4. 50% Entertainment Disallowance and Overlap of Disallowances

Prior to the TCJA, IRC Section 274(n)(1) imposed a 50% disallowance on the deduction of both meals and entertainment expenses. The 100% disallowance in Section 274(a)

previously did not apply to entertainment activities meeting the "directly related" or "associated with" tests; the 50% disallowance in Section 274(n)(1) did apply to such expenses, but generally not for the transportation related to the entertainment.[183] Entertainment is no longer subject to the 50% disallowance, whether or not directly related or associated with the active conduct of business.

The 50% disallowance still applies to meals. To avoid misapplication of the deduction disallowances to the detriment of the taxpayer, it is important that meal expenses subject to the 50% disallowance not also be subject to the 100% entertainment disallowance, or vice versa. This can occur when a reconciliation from the taxpayer's books to taxes is being made.

For example, fifty percent of all flights are deemed entertainment flights. Expenses of $10 million for depreciation, fuel, and fees related to all flights and $100,000 for pilot meals, $5,000 for pilot entertainment, and $200,000 for passenger catering are related to the entertainment flights only. The total aircraft expense deductions should be $5 million ($10 million × 50%). The meal and entertainment disallowance of Sections 274(a) and 274(n) related to the entertainment flights would be $155,000 ($300,000 × 50% + $5,000 × 100%). The employer may take a total deduction of $5 million rather than $4,845, which would be the result by incorrectly applying the Section 274 meals and entertainment disallowances to amounts already disallowed.

In summary, it is important to apply the 100% and 50% disallowances only once to the same amounts. In other words, amounts already disallowed pursuant to Section 274(a) should not again be disallowed under Sections 274(a) and 274(n).

5. Commuting Flights

For taxable years beginning after 2017, the TCJA disallows the costs of commuting, unless to ensure the safety of the employee. Like Business Entertainment, the TCJA's new deduction disallowance for "commuting" expenses has many undefined terms. The new Section 274(l) provides, "Transportation and commuting benefits. (1) In general. No deduction shall be allowed under this chapter for any expense incurred for providing any transportation, or any payment or reimbursement, to an employee of the taxpayer in connection with travel between the employees' residence and place of employment, except as necessary for ensuring the safety of the employee."

Thus, for expenses paid or incurred after December 31, 2017, if not to ensure the safety of the employee, any transportation, or any payment or reimbursement, to an employee in connection with personal travel between the employee's residence and place of employment is not deductible.

Proposed regulations providing some guidance were finalized in 2020 with the addition of more favorable clarifying interpretations. The final commuting regulations are effective for taxable years beginning after December 16, 2020.

a. Commuting: Ensuring the Safety of the Employee

Commuting expenses to "ensure the safety of the employee" will allow for continued deductions as Personal Nonentertainment travel. Final regulations amended the definition of "ensuring the safety of the employee" by expanding the proposed definition from the "bona fide security concern" in Regulations Section 1.132 5(m), which provides,

(2) Demonstration of bona fide business-oriented security concerns -
(i) In general. For purposes of this paragraph (m), a bona fide business-oriented security concern exists only if the facts and circumstances establish a specific basis for concern regarding the safety of the employee. A generalized concern for an employee's safety is not a bona fide business-oriented security concern. Once a bona fide business-oriented security concern is determined to exist with respect to a particular employee, the employer must periodically evaluate the situation for purposes of determining whether the bona fide business-oriented security concern still exists. Example of factors indicating a specific basis for concern regarding the safety of an employee are -

(A) A threat of death or kidnapping of, or serious bodily harm to, the employee or a similarly situated employee because of either employee's status as an employee of the employer; or

(B) A recent history of violent terrorist activity (such as bombings) in the geographic area in which the transportation is provided, unless that activity is focused on a group of individuals which does not include the employee (or a similarly situated employee of an employer), or occurs to a significant degree only in a location within the geographic area where the employee does not travel.

The final commuting regulations expand the definition to refer to Treasury Regulation Section 1.61 21(k)(5),[184] which provides that unsafe conditions exist if a reasonable person would, under the facts and circumstances, consider it unsafe for the employee to walk to or from home, or to walk to or use public transportation at the time of day the employee must commute. Compared to the early definition set forth in Section 1.132 5(m), this is a more liberal standard of "ensuring the safety of the employee."

For example, suppose a CEO has a compromised immune system during the coronavirus pandemic. In addition, the CEO's employer has taken unfavorable measures with release of the vaccine, which is available only to individuals living in certain geographic areas, and due to this, there have been threats on the CEO's life. The CEO and spouse are also covered by an independent security study that provides for travel in the employer aircraft for all domestic and foreign travel. In addition, the CEO and spouse fly on a weekly basis from their home in Boca Raton, Florida, to

New York, New York, the CEO's primary place of work. Under this example, no expenses would be disallowed under the Section 274(l) provisions, because the travel in the employer-provided aircraft is to ensure the CEO's safety. The commuting would also be deductible under these circumstances even if an independent security study was not obtained.

b. Definition of Commuting

The new statutory language does not specify whether it is directed at travel between any residence and any place of employment[185] or just between the primary residence and primary place of employment. The proposed regulations provided that the definition of *residence* is by reference to Regulations Section 1.121 1(b)(1), which includes any residence, not just the primary residence, and that the term is based on all the facts and circumstances, including a houseboat, a house trailer, or the house or apartment that the taxpayer is entitled to occupy as a tenant-stockholder in a cooperative-housing corporation. Thus, from the proposed regulations, travel from any residence, including second or third homes, to a place of employment could be considered commuting and subject to disallowance, unless for the purpose of ensuring the safety of the employee. The final regulations retained the proposed definition including any residence, not just the primary residence. However, the final regulations clarify that *place of employment* encompasses the employee's regular or principal (if more than one regular) place of business and that an employee's place of employment does not include temporary or occasional places of employment.[186] The employee must have at least one regular or principal place of business.[187]

The final regulations clarify that where the transportation is excluded from income as a business expense because the transportation was for business purposes, such travel is not subject to the Section 274(l) disallowance.[188] Therefore, where an executive primarily lives and works in City A and primarily travels to City B for business purposes, the costs would *not* be treated as commuting costs, despite the fact that the travel is literally from the residence to a place of employment. In contrast, where an executive primarily works in City A and has a primary residence in City C and from time to time travels from City A to City C to be at the residence for personal purposes, the travel is considered commuting and subject to the disallowance unless to ensure the safety of the employee.

For example, a CEO's primary residence and primary office are in New York. The CEO's flight from New York to a second employer office in Chicago for business purposes is not Commuting, because that flight is a business trip, not taxable to the employee under the working-condition fringe rules of Section 132. The flight should be fully deductible to the employer as a business trip and therefore not Commuting. However, if the CEO's primary office is in New York and primary residence is in West Palm Beach, Florida, then absent a concern for the safety of the employee, travel from Florida when there for nonbusiness purposes to New York to work at the primary office is commuting, is taxable income to the CEO reported on Form W-2, and is not deductible to the employer company pursuant to Section 274*(l)*.

c. Definition of Employee

Section 274(l) applies to commuting benefits provided to "employees" but it does not define the term "employee." Self-employed individuals such as partners, directors, and independent contractors are typically not considered employees for tax purposes, unless a specific statutory or regulatory provision affirmatively states so. The final regulations[189] define employee by reference to Sections 3121(d)(1) and (2): "that is, officers of a corporate taxpayer and employees of the taxpayer under the common law rules." This definition generally references individuals subject to FICA tax rather than self-employment tax and includes 2% S corporation shareholders, but not sole proprietors, directors, partners, or other types of self-employed individuals.

However, for purposes of distinguishing between employees subject to Section 274(e)(2) and non-employees subject to Section 274(e)(9), the IRS has ruled that 2% shareholders of S corporations are not employees with respect to benefits from the S corporation for income tax purposes due to I.R.C. Section 1372. This line of reasoning was not addressed in the final regulations.

d. Calculation of Commuting Disallowance

Like the Business Entertainment issue, there is no guidance regarding the actual dollar amount that is nondeductible under the new Commuting rules. There are at least three possible interpretations: (1) no expenses are deductible, not even the amount included in income; (2) only the amount included in income is deductible; or (3) all expenses are deductible where there is any income exclusion, because the flight would now be deductible as wages, not Commuting.

To illustrate this, suppose expenses related to New York–to–Florida Commuting flights are $1 million and wage-imputed income using the SIFL rates is $100,000. Under the alternative interpretations:

1 The full $1 million is nondeductible, despite the fact that $100,000 was included in income.

2 $900,000 is nondeductible, as attributable to the excess over the amount included in income.

3 $1 million is completely deductible because it is not considered Commuting.

Unfortunately, the final regulations indicate an intent by Treasury to not permit the deduction of the amount included in income (SIFL).[190] Specifically, the final regulation states,

"The disallowance is not subject to the exceptions provided in section 274(e)."[191] Of course, the exceptions in Sections 274(e) are limited by their terms to the entertainment classification of the flight. Commuting is Personal Nonentertainment, and therefore qualification for an exception to entertainment classification is not relevant. Nevertheless, Treasury's intent expressed by this provision in the final regulations casts doubt on whether deducting some or all of the costs of the flight as compensation (method 2 and method 3 above) would be permitted. The IRS also considered comments requesting that only incremental costs be subject to the commuting disallowance, but rejected such a position.[192]

What if there are nonemployee Commuting passengers on the same trip? Would the full expenses be allocable and deductible in accordance with the number and nature of the flight per passenger, or would the entire flight be ''tainted'' as a Commuting flight? Again, like the new Business Entertainment disallowance, the most reasonable interpretation may be to follow the allocation method in Regulations Section 1.274 10, which applies to Personal Entertainment flights.

6. Charitable Flights

Surprisingly, flights for exclusively charitable purposes may result in significant adverse tax consequences. Charitable flights are generally not considered entertainment flights. However, the tax problem with these flights does not arise from the entertainment disallowance, but from the fact that a charitable flight not related to the business of the taxpayer does not support a business deduction for the costs attributable to the flight.

Furthermore, a charitable deduction is only allowed for the out-of-pocket costs of the flight (such as fuel).[193] Thus, fixed costs allocable to the flight (such as depreciation, hangar rental, regular maintenance, salaries, and insurance) are not deductible as either business expenses or charitable contributions.[194]

It is possible that a company may determine that flights in connection with a charitable activity are deductible as a business expense, depending on the facts and circumstances. For example, participation in a charitable activity may qualify as institutional or goodwill advertising by keeping the company's name before the public.[195]

Another possibility is to treat the charitable flight as the personal activity of a particular employee and report the SIFL value of the flight as a taxable fringe benefit to that employee. The employer would deduct the entire cost of the flight as a compensation expense since it is a Personal nonentertainment flight. The employee would have to report the SIFL amount as additional taxable income, but at least in the aggregate, this is a less adverse tax result than having the fixed costs attributable to the charitable flight disallowed.

E. ENTERTAINMENT FACILITY

There is some risk that aircraft are subject to an additional expense disallowance under the prohibition on deducting expenses with respect to entertainment *facilities*.[196] Treasury Regulations provide that expenditures with respect to an aircraft are deemed business travel, rather than expenses with respect to an entertainment facility, to the extent that the aircraft is used in pursuit of a trade or business and not for entertainment.[197] That regulation cross-references another section of the Regulations with respect to nonentertainment use of an entertainment facility, which more generally provides that the entertainment-facility disallowance does not apply to "[e]xpenses or items attributable to the use of a facility for other than entertainment purposes such as expenses for an automobile when not used for entertainment."[198] This provision suggests that Personal nonentertainment flights should not be subject to the entertainment-facility disallowance.

However, the preamble to the proposed regulations states that the IRS believes that the entertainment-facility disallowance should apply to Personal nonentertainment flights.[199] This statement appears to be based solely on the wording of IRC Section 274(a)(1)(B), without considering the legislative history and existing Regulations referenced above. Furthermore, the preamble states that, in passing the Jobs Act, Congress did not consider the effect of the amendment to IRC Section 274(e)(2) on the entertainment-facility disallowance. Possibly in contrast to the preamble to the proposed regulations, the preamble to the final Regulations states that "Section 274(e)(2) and the associated regulations apply to expenses for entertainment facilities."[200] It is unclear whether this means that the Treasury has abandoned the view that Personal nonentertainment flights are subject to the entertainment-facility disallowance.

Further complicating the matter is the question of whether an aircraft should be classified as an entertainment facility at all. Treasury Regulations state that aircraft and automobiles are types of assets that may be entertainment facilities.[201] Existing caselaw indicates that any use of a facility for entertainment during the year makes it an entertainment facility.[202] However, in *Sutherland Lumber-Southwest, Inc. v. Commissioner*, 114 T.C. 197, 202 n.3 (2000), *aff'd*, 255 F.3d 495 (8th Cir. 2001), *acq.* 2002-1 C.B. xvii., the Tax Court raised the question in a footnote of whether an aircraft is an entertainment facility.

In view of the ambiguous guidance regarding the applicability of the entertainment-facility disallowance to aircraft, most companies are currently applying only the entertainment-expense disallowance set forth in proposed Treasury Regulations Sections 1.274 9 and 10 and are not disallowing additional deductions under the entertainment-facility disallowance.

III. FAA REGULATORY CONSIDERATIONS

Whether an aircraft is used for business or personal reasons, it is necessary to comply with the Federal Aviation Administration ("FAA") regulations. Section III provides a general description of those regulations with respect to Personal flights. A complete explanation of the Federal Aviation Regulations ("FARs") in title 14 of the Code of Federal Regulations is beyond the scope of the Personal Use Handbook.

Aircraft operators may obtain an air carrier certificate to perform commercial operations in common carriage with their aircraft under the FARs. To conduct *charter* flights (also referred to as a "wet lease"), the operator generally must obtain an air carrier certificate to operate under FAR Part 135 (on demand charter), which allows the aircraft operator to receive compensation for conducting charter flights. The FAA defines "compensation" very broadly to include all forms of consideration and good will. If no air carrier certificate is obtained from the FAA, the aircraft operations are governed by the provisions in FAR Part 91. Subject to certain exceptions, Part 91 generally forbids the operator to receive compensation for providing air-transportation of persons or property, defined as providing both the aircraft and at least one crew member to transport persons or property. Leasing an aircraft without a crew member (a "dry lease") does not violate the FAA regulations provided the parties are not indirectly providing an aircraft and crew member as a package deal or informal arrangement to circumvent the FARs.

A company can operate an aircraft under Part 91 to transport passengers or property as long as the transportation is within the scope of the operating company's business and transportation by air is not the primary purpose of the business operating the aircraft.[203] Such flights can only be provided to the company's parent company, a subsidiary company, or a subsidiary of the company's parent company – i.e., vertical relationships. The company operating the aircraft may accept reimbursement from these companies for the cost of owning, operating, and maintaining the airplane for such flights. The prohibition in Part 91 on providing air transportation for compensation or hire generally permits a company to provide flights to its employees and others for their personal purposes as long as no compensation is accepted for such flights. Unless an exception such as a time-share or Nichols opinion applies, a company is not permitted to receive any reimbursement from its employees for Personal flights provided by the company.[204]

A company can provide flights under FAR Part 91 through a time-sharing agreement, which permits the company to accept reimbursement up to a maximum of twice the fuel cost plus certain enumerated expenses.[205] If the aircraft's maximum takeoff weight is less than 12,500 lbs., the company must utilize the NBAA Small Aircraft Exemption. FAR Part 91 also permits a company to lease an aircraft without providing crew and to own and operate an aircraft with others under a joint-ownership arrangement as defined in the FARs.

Unless a specific exception to the general rule exists, an operator cannot accept compensation for transportation by air conducted under Part 91 and an air carrier certificate is required. Also, companies whose primary business purpose is operating an aircraft may be considered by the FAA to be a "flight-department company."[206]

In general, a flight-department company is a company that operates an aircraft when such operations are the primary purpose for the company's existence. For this reason, it is generally not advisable for a single purpose LLC to provide both the aircraft and the pilot to another entity, because it may be construed as a flight-department company for FAA purposes, which would trigger Federal Transportation Excise Taxes (FET).

The FARs require that flights conducted by a company operating an aircraft under Part 91 be "incidental" to another business of the company. In contrast, a company can operate an aircraft as its only activity under Part 135 as a commercial on-demand charter operator.

An individual can operate an aircraft under Part 91 to transport him/herself in connection with either business or personal activities. However, there is some risk that Part 91 would not permit an individual to operate an aircraft in

connection with his or her business activities and accept reimbursement for such flights, such as reimbursement from the individual's employer. An exception applicable to owner-pilots may permit such a reimbursement to an owner-pilot if he or she is the only person on board the aircraft.[207]

Owner-pilots also risk violation of the terms of their pilot license. Both private and commercial pilots should consult the applicable FARs for the limitations on receiving compen- sation for flights.

FAR Section 91.501(b)(6) allows for the carriage of company officials, employees, and guests of the company on an airplane operated under a time-sharing, interchange, or joint-ownership agreement as defined in Section 91.501(c).

A. TIME-SHARE AGREEMENTS

FAR Section 91.501(c)(1) defines a time-sharing agreement as an arrangement whereby a person leases his or her airplane with flight crew, wet lease, to another person, and no charge is made for the flights conducted under that arrangement other than those specified in Section 91.501(d).

According to FAR Section 91.501(d), the following, as expenses of a specific flight, may be charged for transportation as authorized by paragraphs (b)(3), (b)(7), and (c)(1):

1. 91.501(b)(3) – demonstration flights
2. 91.501(b)(7) – carriage of property
3. 91.501(c)(1) – time-sharing

For these three operations alone, FAR Section 91.501(d) provides that the items listed below may be charged:

1. Fuel, oil, lubricants, and other additives
2. Travel expenses of the crew, including food, lodging, and ground transportation
3. Hangar and tie-down costs away from the aircraft's base of operations
4. Insurance obtained for a specific flight
5. Landing fees, airport taxes, and similar assessments
6. Customs, foreign permits, and similar fees directly related to the flight
7. In-flight food and beverages
8. Passenger ground transportation
9. Flight planning and weather-contract services
10. An additional charge, equal to 100% of the expenses listed in item #1 above

This list of permissible charges is a *maximum* amount and is often referred to as the "two-times fuel" rule. Item #1 is the actual fuel burn for the flight and item #10 is twice the amount of item #1, meaning that it will help offset some costs that are not allowed to be charged. These costs could include pilot salaries, maintenance reserves, hangar rent, and depreciation. The costs to be recovered, if listed in items #2 through #9, are a portion of the expenses result- ing from the movement of the aircraft.

The time-share is a wet-lease (with-crew) transportation arrangement. As such, it is subject to the FET and FAR Sec- tion 91.23 ("Truth-in-Leasing Clause Requirement in Leases and Conditional Sales Contracts"). More information about the Federal Transportation Excise Tax is available at www. nbaa. org/taxes.

FAR Section 91.501(a) applies only to the operation of large (over 12,500 lbs.) or turbojet-powered multiengine civil airplanes of U.S. registry. If the aircraft does not fall under these parameters, the owner may opt into Section 91.501 operations by utilizing NBAA's Small Aircraft Exemption.

B. NICHOLS-OPINION REIMBURSEMENT

Because most companies with business aircraft do not want to fly under Part 135 as a charter flight, or have more expenses than permitted for reimbursement under a time-share agreement, the FAA responded to NBAA's request for relief to permit reimbursements. In response to NBAA's Michael Nichols request, the FAA authorized reimbursements in situations where employees designated by the employer company fly for personal purposes in circumstances where the business needs of the employer may require prompt return from the personal trip for business purposes. This FAA response is commonly referred to as the Nichols opinion.[208] Thus, where a company has identified those employees to which the business-necessity return ap- plies, the executive is permitted to reimburse for the business travel. Note that reimbursement would not be permitted under the authority for personal-guest travel where the employee

is not on board, because the business-necessity requirement would not be met as required by the Nichols opinion. The Nichols opinion is a useful tool for those public-company executives who wish to reduce the amount of personal travel that might otherwise be reported for SEC proxy purposes, but companies must comply with many administrative requirements for each flight, which may be too burdensome for some companies.

IV. SECURITIES AND EXCHANGE COMMISSION REPORTING

The Securities and Exchange Commission ("SEC") corporate reporting affects publicly traded companies with greater than $10 million in assets and greater than 500 shareholders. The portion of the SEC regulations relating to personal use of the corporate aircraft is contained in the Code of Federal Regulations 17, subpart 229.402 (item 402) ("Executive Compensation").

SEC rules differ significantly from the tax rules as its mission is to protect investors and maintain the integrity of the securities markets. By enforcing its rules, the SEC – with its civil powers and the criminal powers of the Justice Department – increases the amount, accuracy, consistency, and comparability of information available to investors.

The amount imputed to an employee (under either the SIFL or the charter-rate methods) for tax purposes for Personal flights under the IRS rules is not the same as the amount to be reported to the SEC.

For SEC-reporting purposes, all annual and long-term compensation for certain top executives of reporting companies must be disclosed. Note that 17 C.F.R. Section 229.402, item 402(b)(2), describes the information to be reported, which includes salary, bonus, and other annual compensation. Additional annual compensation includes perquisites – i.e., personal use of corporate aircraft (item 402(C)(1)) – which should be reported at the perquisite's "aggregate incremental cost," unless the aggregate amount of such compensation is less than $10,000.

Item 402(a)(2) All compensation covered. This requires clear, concise, and understandable disclosure of all plan and non-plan compensation awarded to, earned by, or paid to named executive officers and directors.

Item 402(a)(3) Persons covered. Disclosure shall be provided pursuant to this Item for each of the following (the "named executive officers"):

> (i) All individuals serving as the registrant's principal executive officer or acting in a similar capacity during the last completed fiscal year ("PEO"), regardless of compensation level;

(ii) All individuals serving as the registrant's principal financial officer or acting in a similar capacity during the last completed fiscal year ("PFO"), regardless of compensation level;

(iii) The registrant's three most highly compensated executive officers other than the PEO and PFO who were serving as executive officers at the end of the last completed fiscal year; and

(iv) Up to two additional individuals for whom disclosure would have been provided pursuant to paragraph (a)(3)(iii) of this Item but for the fact that the individual was not serving as an executive officer of the registrant at the end of the last completed fiscal year.

Instructions to item 402(b)(2)(iii)(C)(2)(ix) 4. Perquisites and personal benefits may be excluded as long as the total value of all perquisites and personal benefits for a named executive officer is less than $10,000. If the total value of all perquisites and personal benefits is $10,000 or more for any named executive officer, then each perquisite or personal benefit, regardless of its amount, must be identified by type. If perquisites and personal benefits are required to be reported for a named executive officer pursuant to this rule, then each perquisite or personal benefit that exceeds the greater of $25,000 or 10% of the total amount of perquisites and personal benefits for that officer must be quantified and disclosed in a footnote.

An example of the SEC disclosure of the aggregate incremental costs is that in Coca-Cola's 2019 statement:

- In determining the incremental cost to the Company of personal use of the Company aircraft, the Company calculates, for each aircraft, the direct variable operating costs on an hourly basis, including all costs that may vary by the hours flown. Items included in calculating this cost are as follows
  - aircraft fuel and oil;
  - travel, lodging and other expenses for crew;
  - prorated amount of repairs and maintenance;
  - prorated amount of rental fee on airplane hangar (when away from home base);
  - catering;
  - logistics (landing fees, permits, etc.);
  - telecommunication expenses and other supplies; and
  - the amount, if any, of disallowed tax deductions associated with such use.

  When the aircraft is already flying to a destination for business purposes, only the direct variable costs associated with the additional passenger (for example, catering) are included in determining the aggregate incremental cost to the Company. While it happens very rarely, if an aircraft travels empty before picking up or after dropping off a passenger flying for personal reasons, this "deadhead" segment would be included in the incremental cost attributable to overall travel.

Along with the perquisite calculations and examples above, Coca-Cola permits "a reasonable number of personal trips" for the CEO's immediate family when it rides with him. Infrequently, spouses of other named executives may also travel on company aircraft when it is being flown for business purposes because costs to the company are minimal. Tax reimbursements are not issued for this sort of travel. These costs are imputed to the associated executive, and a nominal amount is included within executive compensation and benefits as "other compensation." All flight perquisites, including spousal travel, should be listed in a company's proxy statement under "other income" to avoid sanctions from the SEC. See the 2018 Dow Chemical Co. SEC settlement requiring a $1.75 million civil penalty and independent review of company policies as a result of inadequate perquisite recording for its CEO on its 2013–16 proxy statements.[209]

In summary, depending on a company's circumstances, personal use of the corporate aircraft could result in public reporting of the aggregate incremental cost. Although there is no official definition of *aggregate incremental cost*, it generally is interpreted to mean the variable or direct operating cost of the aircraft. These are costs that are incurred only because the aircraft was flown, unlike fixed costs, which are incurred and will be paid regardless of whether the aircraft remains in the hangar or is flown.

V. SOLE PROPRIETORS

A. DESCRIPTION OF SOLE-PROPRIETOR FLIGHTS

The term *sole proprietor* refers to an individual with a business who provides flights to himself or herself, rather than having the flights provided by an employer. A sole proprietor would include an individual who owns an aircraft or leases it from another party and who pilots the aircraft or hires the pilot. Sole-proprietorship business income is generally reported on Schedule C on the individual's Form 1040. The sole-proprietorship rules also apply to flights provided by a single-member LLC to its sole owner if the owner is an individual, assuming the single-member LLC is disregarded for federal income-tax purposes.

B. CLASSIFICATION OF FLIGHTS

The costs of a flight provided by a sole proprietorship to its sole proprietor primarily for the purposes of a business owned by the sole proprietor ordinarily are deductible as transportation costs incurred by the sole proprietor's business. The SIFL rules would not apply to a sole proprietor's flight, because there would be no employer–employee relationship between the business and the sole owner.

In general, any Personal flights by sole proprietors, whether entertainment or not, are nondeductible. The distinction between Business and Personal flights discussed above in Section II.C ("Distinguishing Personal Flights from Business Flights") would apply to flights provided by a sole proprietorship to its sole owner.

Section II discusses the ability of *employers* to deduct the costs of flights provided to employees for nonentertainment purposes. This exception for nonentertainment flights is not available to the sole proprietor or his guest's flights but is available to any employees or other service providers of the sole proprietor.

As discussed below with respect to Business Entertainment, sole proprietors will need to determine when a flight with a business purpose, such as to meet with customers, suppliers, employees, or other business associates, is characterized as Business Entertainment, the costs of which would now be 100% nondeductible because of the changes by the TCJA for years after 2017.

Allocation of Costs – "Primary Purpose" Method. In the case of a sole proprietor's flights incurred in connection with business, costs are allocated among the sole proprietor's flights in proportion to the miles or hours of the flight, referred to herein as the primary purpose method.[210] The business purpose of each flight is determined according to the primary purpose of the flight.[211]

In the case of a sole proprietor, there does not appear to be any requirement to allocate the cost of a flight among each passenger to determine its deductibility. The final entertainment Regulations would apply to the Personal Entertainment passengers other than the sole proprietor, but do not appear to apply the passenger-by-passenger allocation methods to make the allocation between the business vs. non-business-related portion of the flights. The discussion of the primary purpose test in the preamble to the final Regulations affirms that the Regulations are promulgated under IRC Section 274(e)(2), which relates to flights provided by the taxpayer to specified individuals for compensatory purposes, in contrast to a specified individual's use of his or her own aircraft.[212]

For example, a sole proprietor uses his aircraft for 20 flights purely for his own business purposes, but occasionally his spouse accompanies him. Applying the primary purpose, those 20 flights would be fully deductible. If the sole proprietor had several employees, some of whom took Personal Entertainment flights, presumably those would be subject to a deduction disallowance to the extent those individuals were specified employees.

C. COMPARISON TO EMPLOYER-PROVIDED FLIGHTS

The ability of a sole proprietor to use the primary purpose method to allocate costs is generally an advantage over the passenger-by-passenger allocation methods required for employer-provided flights, because it allows guests of the sole proprietor traveling for nonbusiness purposes to be ignored when the flight is primarily for business purposes. However, a sole proprietorship has the disadvantage of having the costs of all Personal flights disallowed, irrespective of whether the flights are for entertainment or nonentertainment purposes.

D. FOREIGN TRAVEL

The IRC Section 274(c) foreign-travel rule would prohibit the deduction of foreign travel in excess of one week and where personal activities are at least 25% of the days on a foreign trip.

Note that if the foreign trip was already primarily personal, the entire cost of the trip would be disallowed, rather than just a proportionate amount of the expenses that results under the foreign-travel rules.

E. EMPLOYEE-PROVIDED FLIGHTS

An employee of an employer may own or lease an aircraft occasionally used for the employer's business. In contrast to a sole proprietor, the employee is not carrying on a separate business independent of the employer's business. In the case of an employee traveling for the employer's business, the employee is permitted to be reimbursed without imputed income on the reimbursement if proper substantiation is made to the employer of the expense under the accountable-plan rules of Section 62(c).[213] Historically, an employee could deduct non-reimbursed expenses related to the employer's business. Subsequent to the TCJA, the employee can no longer deduct the excess cost of such travel over the amount reimbursed by the employer. Note that the FAA rules may limit the amount the employee may receive as reimbursement where the travel is not within the scope of the employee services with respect to the employer.

Flights by a director or by another self-employed individual on an aircraft owned or leased by the director or other self-employed individual would be deducted under the rules for sole proprietors.[214]

APPENDIX 1: SAMPLE CALCULATIONS

EXAMPLE OF COST ALLOCATION

This is an example of the occupied-seat method and flight-by-flight method for allocating costs to entertainment flights for purposes of the entertainment disallowance under the proposed Regulations.

This example modifies the order of the steps described in the proposed Regulations. In the calculations below, entertainment percentages are calculated under the two methods using miles and hours. The lowest entertainment percentage is multiplied by the operating costs for the year to determine the costs allocable to entertainment flights. The imputed income at SIFL rates and the reimbursements with respect to entertainment flights are subtracted to determine the entertainment disallowance to report on the employer's income-tax return.

This example involves an employer-provided aircraft. The aircraft's operating costs for the year, including depreciation, total $1 million. There are only the following four flights on the aircraft during the year:

Flight 1 – Business Flight
Saint Louis to Chicago – 251 mi., 0.7 hours, six passengers

- Six passengers traveling for business

Chicago to Saint Louis – 251 mi., 0.7 hours, six passengers

- Six passengers returning from business trip

Flight 2 – Entertainment Flight
Saint Louis to Orlando – 874 mi., 2.1 hours, four passengers

- Specified individual and three personal guests traveling for entertainment

Orlando to Saint Louis – 874 mi., 2.1 hours, four passengers

- Four passengers returning from entertainment trip

Time-sharing reimbursement received from specified individual	$2,520
Imputed income at SIFL rates, before subtracting reimbursement	$4,694
Less time-sharing reimbursement	(2,520)
Imputed income reported to specified individual (net of reimbursement)	$2,174

Flight 3 – Personal Nonentertainment Flight
Saint Louis to Wichita – 378 mi., 0.9 hours, two passengers

- Specified individual and personal guest traveling for personal nonentertainment purposes

Wichita to Saint Louis – 378 mi., 0.9 hours, two passengers

- Two passengers returning from personal nonentertainment trip

Imputed income to specified individual at SIFL rates:	$1,218

Flight 4 – Mixed Business and Entertainment Flight
Saint Louis to New York – 895 mi., 2.1 hours, four passengers

- Two specified individuals traveling for business, with their spouses traveling for entertainment purposes

New York to Saint Louis – 895 mi., 2.1 hours, four passengers

- Four passengers returning from business/entertainment trip

Total imputed income to specified individuals at SIFL rates:	$2,392

(*See next page for Cost-Disallowance Worksheet)*

COST-DISALLOWANCE WORKSHEET

							Occupied Seat Method				Flight-by-Flight	
Flight	Miles	Hours	Total Pax	Bus. Pax	Pers. Nonent. Pax	Ent.Pax	Total O/S Miles	Ent. O/S Miles	Total O/S Hours	Ent. O/S Hours	Ent. Miles	Ent. Hours
1	251	0.7	6	6			1,506		4.2			0
1	251	0.7	6	6			1,506		4.2			0
2	874	2.1	4			4	3,496	3,496	8.4	8.4	874	2.1
2	874	2.1	4			4	3,496	3,496	8.4	8.4	874	2.1
3	378	0.9	2		2		756		1.8			0
3	378	0.9	2		2		756		1.8			0
4	895	2.1	4	2		2	3,580	1,790	8.4	4.2	*448	*1.1
4	895	2.1	4	2		2	3,580	1,790	8.4	4.2	448	1.1
Totals	4,796	11.6					18,676	10,572	45.6	25.2	2,644	6.4
Divided by								18,676		45.6	4,796	11.6
Entertainment Percentage								56.6%		55.3%	55.1%	55.2%
Lowest Entertainment Percentage											55.1%	

COST-DISALLOWANCE CALCULATION

Total Aircraft Operating Costs	$ 1,000,000
Entertainment Percentage	× 55.1%
Costs Attributable to Entertainment Flights	551,000
Less Reimbursements Received for Entertainment Flights – Flight 2	(2,522)
Imputed Income Reported for Entertainment Flights:	
Flight 2 – Net SIFL	(2,174)
Flight 4	(2,392)
Entertainment Disallowance	$ 543,914

* The flight-by-flight-method columns present the miles and hours of each flight multiplied by the percentage of passengers on the flight traveling for entertainment purposes. For Flight 4, the entertainment miles are calculated as follows: 895 total miles × 2 entertainment passengers ÷ 4 total passengers = 448 entertainment miles.

APPENDIX 2:
EXAMPLES OF COMMON SCENARIOS

Examples	Income Inclusion	Deduction Disallowance
Vacation flight by CEO of corporation and spouse; 1 hour	Yes. SIFL value x 2 legs (employee and spouse) in CEO's W-2	Yes. Two seat hours if occupied-seat-hour method used.
Vacation flight by non-specified individual of corporation and spouse; 1 hour	Yes. SIFL value x 2 legs (employee and spouse) in employee's W-2	No. Disallowance is only applicable to specified individuals.
Business flight by CEO of corporation, 2 hours. Spouse accompanies for personal but not for entertainment	Yes. SIFL value x 1 leg (spouse only) in CEO's W-2.	No. Disallowance is only applicable to entertainment flights by specified individuals, or business entertainment or commuting. The specified individual is flying for business and the spouse is not flying for entertainment.
Business flight by CEO, 2 hours. Spouse accompanies for entertainment	Yes. SIFL value x 1 leg (spouse only) in CEO's W-2	Yes. Two seat hours if occupied-seat-hour method used. Spouse is considered to be specified individual by attribution and thus entertainment flight, is disallowed.
Commute by partner in LLC.	Yes. SIFL value x 1 leg in partner's K-1	No. The partner is not considered to be an employee.
Vacation trip by non-specified individual, non-owner employee of LLC	Yes. SIFL value x 1 leg in employee's W-2	No. Disallowance is only applicable to specified individuals.
10-seat plane occupied by CEO of corporation and 4 non-specified individual employees on business, with their spouses for entertainment, 1 hour	No. Fifty percent seating-capacity rule applies.	Yes. One seat hour if occupied-seat-hour method used.
10-seat plane occupied by CEO of corporation and 3 non-specified individual employees on business; and 4 guests of CEO for entertainment; 1 hour	Yes. SIFL value × 4 legs (4 guests) in CEO's W-2	Yes. Four seat hours if occupied-seat-hour method used.
Vacation flight by CEO of corporation, spouse, and 3 children (1 of whom is 19 months old); 5 hours occupied trip to vacation destination, 5 hour deadhead return	Yes. SIFL value × 4 legs in CEO's W-2.	Yes. Fifty seat hours if occupied-seat-hour method used.
Business flight by sole proprietor as primary purpose, spouse accompanies; 1 hour	No	No
Vacation flight by sole proprietor and spouse; 1 hour	No	Yes, entire cost of flight
CEO of corporation uses *his own airplane* for Business flights for his work as an employee of the corporation	Only if reimbursements for use of airplane exceed actual *substantiated expenses*	No, and if current law permits, CEO can deduct as an employee business expense, the amounts not reimbursed by corporation.
Director of corporation uses *his own airplane* for Business flights for his work as a director of the corporation	Only if reimbursements for use of airplane exceed actual *substantiated expenses*	No, and director can deduct amounts not reimbursed by corporation.
Specified individual employee travels on employer aircraft from NY to Paris for 2 days of vacation, to London for 2 days of business meetings, return to NY (trip primarily business)	Yes. SIFL value of mileage equal to excess of NY to Paris to London to NY, over NY to London to NY	Yes, equal to excess of NY to Paris to London to NY, over NY to London to NY
Business Entertainment flight by CEO	No	Yes
Business Entertainment flight by non-specified individual employees	No	Yes
Sole proprietor travels to London for 6 days of business and four days of vacation	No	Yes, 40% disallowed since 4 of 6 days were for a personal purpose.
Executive of corporation travels to London for 6 days of business and four days of vacation	Yes. 40% of SIFL since Foreign Travel rule would be applicable.	No

Endnotes

1 Treas. Reg. Sec. 1.61-21(b)(1).

2 Treas. Reg. Sec. 1.61-21(a)(3).

3 Treas. Reg. Sec. 1.61-21(a)(4).

4 Treas. Reg. Sec. 1.61-21(g)(11).

5 Treas. Reg. Sec. 1.61-21(a)(4).

6 Treas. Reg. Sec. 1.61-21(g)(1).

7 Treas. Reg. Sec. 1.61-21(a)(5).

8 Regulations Section 31.3501(a)-1T Q/A-5 provides in this regard that "[t]he provision of noncash fringe benefits by an entity to an employee of another employer does not make such entity the employer of such employee with respect to such noncash fringe benefits for any purposes of subtitle C, so long as such noncash fringe benefits are incidental to the provision of wages by the employer to such employee."

9 Treas. Reg. Sec. 1.61-21(a)(1), (3).

10 Treas. Reg. Sec. 1.61-21(g)(4)(v).

11 *See Manning v. Comm'r*, T.C. Memo (RIA) 1993-127 (whether personal use of corporate property is a constructive dividend or constructive wages is a question of fact).

12 Treas. Reg. Sec. 1.61-21(g)(4)(v).

13 Treas. Reg. Sec. 1.162-7, -8.

14 Treas. Reg. Sec. 1.61-21(b)(7).

15 I.R.C. Sec. 132(a)(3).

16 I.R.C. Sec. 132(d).

17 Treas. Reg. Sec. 1.61-21(b)(6), (g)(3)(ii).

18 *Noyce v. Comm'r*, 97 T.C. 670, 685 (1991); *Marshall v. Comm'r*, T.C. Memo (RIA) 1992-65, 7-8.

19 Id. at 8.

20 *See Noyce*, 97 T.C. 670, 677; *Marshall*, T.C. Memo (RIA) 1992-65; *Kurzet v. Comm'r*, 222 F.3d 830, 837 (10th Cir. 2000); *Richardson v. Comm'r*, T.C. Memo (RIA) 1996-368, 60.

21 E*dwards v. Comm'r*, T.C. Memo (RIA) 2002-169.

22 *Noyce*, 97 T.C. 670, K*urzet* 222 F.3d 830, 835.

23 Treas. Reg. Sec. 1.162-2(b)(1); Noyce, 97 T.C. 670; French v. Comm'r, T.C. Memo (RIA) 1990-314.

24 Treas. Reg. Sec. 1.162-2(b)(2).

25 *Finney v. Comm*'r, T.C. Memo (RIA) 1980-23, 34-5; *Nemish v. Comm'r*, T.C. Memo (RIA) 1970-276, aff'd per curiam, 452 F.2d 611 (9th Cir. 1971).

26 *Marshall,* T.C. Memo (RIA) 1992-65 (discussing travel to meet with contractors by officer in charge of project); *French*, T.C. Memo (RIA) 1990-314 (discussing travel to rental property); *Palo Alto Town & Country Village, Inc. v. Comm'r*, 565 F.2d 1388 (9th Cir. 1977) (discussing travel for shopping-center business).

27 *Kurzet*, 222 F.3d 830, 842.

28 *Richardson v. Comm'r*, T.C. Memo (RIA) 1996-368.

29 *Townsend Indus., Inc. v. United States*, 342 F.3d 890 (8th Cir. 2003) (discussing a fishing trip); *United Title Ins. Co. v. Comm'r*, T.C. Memo (RIA) 1988-38 (discussing meetings with clients at resort).

30 *See Noyce v. Comm'r*, 97 T.C. 670 (1991) (discussing service on college board of directors); *see also* Treas. Reg. Sec. 1.132-5(a)(2)(ii), Examples (3), (4) (discussing service on board of charitable organization).

31 Treas. Reg. Sec. 1.162-20(a)(2).

32 *Beckley v. Comm'r,* T.C. Memo (RIA) 1975-37, 8.

33 Treas. Reg. Sec. 1.162-2(d); Rev. Rul. 59-316, 1959-2 C.B. 57; Rev. Rul. 63-266, 1963-2 C.B. 88.

34 *Acacia Mutual Life Ins. Co. v. United States*, 272 F. Supp. 188 (D. Md. 1967); *Peoples Life Ins. Co. v. United States*, 373 F.2d 924 (Ct. Cl. 1967).

35 *See also* P*atterson v. Thomas*, 289 F.2d 108 (5th Cir. 1961), cert. denied, 368 U.S. 837 (1961).

36 *Love Box Co. v. Comm'r,* 842 F.2d 1213 (10th Cir. 1988), cert. denied, 488 U.S. 820 (1988).

37 D*anville Plywood Corp. v. United States*, 899 F.3d 3 (Fed. Cir. 1990).

38 *French v. Comm'r*, T.C. Memo (RIA) 1990-314.

39 *McReavy v. Comm'r,* T.C. Memo (RIA) 1989-172; *Leubert v. Comm'r*, T.C. Memo (RIA) 1983-457.

40 *Christine v. Comm'r*, T.C. Memo (RIA) 1974-249.

41 Treas. Reg. Sec. 1.162-2(e); *Comm'r v. Flowers*, 326 U.S. 465 (1946).

42 Rev. Rul. 99-7, 1999-1 C.B. 361 (travel to temporary place of work); *Chandler v. Comm'*r, 226 F.2d 467 (1st Cir. 1955) (travel to secondary regular place of business).

43 *Markey v. Comm'r*, 490 F.2d 1249 (6th Cir. 1974); *Terry v. Comm'r*, T.C. Memo (RIA) 1979-284.

44 Treas. Reg. Sec. 1.162-2(b)(2).

45 *Sherry v. Comm'r*, T.C. Memo (RIA) 1975-337.

46 *Cowing v. Comm'r*, T.C. Memo (RIA) 1969-135.

47 Rev. Rul. 59-316, 1959-2 C.B. 57; Rev. Rul. 63-266, 1963-2 C.B. 88.

48 *Acacia Mutual Life Ins. v. United States*, 272 F. Supp. 188 (D. Md. 1967).

49 *See Patterson v. Thomas*, 289 F.2d 108 (5th Cir. 1961), *cert. denied*, 368 U.S. 837 (1961); *Manning*.

50 *See Patterson*; *Manning*.

51 Treas. Reg. Sec. 1.162-2(c).

52 *Anchor National Life v. Comm'r*, 93 T.C. 382 (1989).

53 *See United States v. Gotcher*, 401 F.2d 118 (5th Cir. 1968); *Manning v. Comm'r*, T.C. Memo (RIA) 1993-127 (sightseeing and shopping); *Danville Plywood Corp. v. United States*, 899 F.2d 3 (Fed. Cir. 1990) (employees' wives "manned the hospitality desk" and entertained the spouses of the customer representatives while on the trip); E*state of Shantz v. Comm'r*, T.C. Memo (RIA) 1983-743 (staffing a hospitality suite, serving as a hostess, assisting in social settings); *Sisson v. Comm'r*, T.C. Memo (RIA) 1994-545, aff'd, 108 F.3d 339 (9th Cir. 1996) ("Attending social functions arranged for guests of conference participants is not a bona fide business purpose, even though such activities may contribute to the promotion of the taxpayer's business."); *Challenge Manufacturing Co. v. Comm'r*, 37 T.C. 650 (1962), acq. 1962-2 C.B. 4; *Price v. Comm'r*, T.C. Memo (RIA) 1971-323; Rev. Rul. 56-168, 1956-1 C.B. 93 (typing notes or attending business luncheons and dinners).

54 *See Peoples Life Ins. Co. v. United States*, 373 F.2d 924 (Ct. Cl. 1967) (spouses participated in seminars); *Bywater Sales and Service Co. v. Comm'r*, T.C. Memo (RIA) 1965-160 (serving as a translator); *Kerr v. Comm'r*, T.C. Memo (RIA) 1990- 155; *Warwick v. United States*, 236 F. Supp. 761 (E.D. Va. 1964) (entertaining and attending business tours in European and Latin America; performing clerical duties); *United States v. Disney*, 413 F.2d 783 (9th Cir. 1969) (wife of president of Walt Disney Productions was present to promote company's family image and cultivate relationships with other executives; wife attended luncheons, dinners, receptions, film screenings, press conferences and went on good will visits).

55 Treas. Reg. Sec. 1.274-5T(b)(2), (6).

56 Treas. Reg. Sec. 1.274-5T(b)(3), (4).

57 Treas. Reg. Sec. 1.274-5T(c)(2)(i).

58 Treas. Reg. Sec. 1.274-5T(c)(2)(ii).

59 Treas. Reg. Sec. 1.274-5T(c)(2)(ii)(B).

60 Treas. Reg. Sec. 1.274-5T(c)(3)(i).

61 Treas. Reg. Sec. 1.274-5T(c)(1).

62 *See*, e.g., *Christian v. Comm'r*, T.C. Memo (RIA) 2000-385; *Finney v. Comm'r*, T.C. Memo (RIA) 1980-23; *Romer v. Comm'r*, T.C. Memo (RIA) 2001 168.

63 Treas. Reg. Sec. 1.61-21(b)(6)(ii).

64 Treas. Reg. Sec. 1.61-21(b)(6)(iii).

65 Treas. Reg. Sec. 1.61-21(b)(7).

66 Treas. Reg. Section 1.61-21(g)(2).

67 Ann. 85-113, 1985-31 I.R.B. 31; *see also* Treas. Reg. Sec. 1.61-21(c)(7); Notice 2005-45, 2005-1 C.B. 1228, Sec. A.

68 Treas. Reg. Sec. 1.61-21(g)(3)(i).

69 Treas. Reg. Sec. 1.61-21(g)(4).

70 Treas. Reg. Sec. 1.61-21(g)(3)(iii).

71 Treas. Reg. Sec. 1.61-21(g)(3)(i).

72 Treas. Reg. Sec. 1.132-5(m).

73 Treas. Reg. Sec. 1.61-21(a)(5).

74 Treas. Reg. Sec. 1.61-21(g)(8)(ii)(B).

75 Treas. Reg. Sec. 1.61-21(g)(8)(ii)(A).

76 Treas. Reg. Sec. 1.61-21(g)(11).

77 Treas. Reg. Sec. 1.61-21(g)(7).

78 Treas. Reg. Sec. 1.61-21(g)(8)(ii)(A).

79 IRC Sec. 267(c)(4).

80 Treas. Reg. Sec. 1.61-21(c)(4) & Treas.Reg. Sec. 1.61-21(g)(10).

81 Treas. Reg. Sec. 1.61-21(g)(8)(ii)(B).

82 Treas. Reg. Sec. 1.132-5(m)(4).

83 *See* Priv. Ltr. Rul. 2007-05-010 (Feb. 2, 2009).

84 Treas. Reg. Sec. 1.132-5(m)(3)(ii).

85 Treas. Reg. Sec. 1.132-5(m)(2)(i).

86 Treas. Reg. Sec. 1.132-5(m)(2)(ii), (iv).

87 Treas. Reg. Sec. 1.132-5(m)(2)(iii).

88 Treas. Reg. Sec. 1.132-5(m)(2)(iv).

89 Treas. Reg. Sec. 1.132-5(m)(4).

90 Treas. Reg. Sec. 1.274-4(f)(1).

91 Treas. Reg. Sec. 1.274-4(d)(2)(i).

92 Treas. Reg. Sec. 1.274-4(d)(2)(ii).

93 Treas. Reg. Sec. 1.274-4(d)(2)(v).

94 Treas. Reg. Sec. 1.61-21(g)(4)(iv).

95 I.R.C. Sec. 274(h).

96 Treas. Reg. Sec. 1.61-21(g)(12)(i).

97 Treas. Reg. Sec. 1.61-21(g)(12)(i)(A)

98 Treas. Reg. Sec. 1.61-21(g)(12)(iii)(A).

99 Treas. Reg. Sec. 1.61-21(g)(12)(iii)(B).

100 Treas. Reg. Sec. 1.61-21(g)(12)(v).

101 Treas. Reg. Sec. 1.61-21(g)(14).

102 Treas. Reg. Sec. 1.61-21(g)(14)(iii).

103 Treas. Reg. Secs. 1.61-21(c)(5), (g)(13).

104 *See* Treas. Reg. Sec. 1.162-25T.

105 Treas. Reg. Secs. 1.274-9, -10, T.D. 9597, 77 Fed. Reg. 45,480 (Aug. 1, 2012).

106 Taxpayers may rely on the proposed regulations after December 31, 2017.

107 Notice 2018-76(2018-42 I.R.B. 599) is obsolete as of October 9, 2020.

108 Treas. Reg. Sec. 1.274-11(b)(1).

109 Treas. Reg. Sec. 1.274-11(b)(1)(i).

110 Treas. Reg. Sec. 1.274-11(b)(1)(i).

111 Treas. Reg. Sec. 1.274-2(c)(3)(iii).

112 Treas. Reg. Sec. 1.274-11(b)(1)(i).

113 Treas. Reg. Sec. 1.274-11(b)(1)(i).

114 Treas. Reg. Sec. 1.274-11(b)(1)(iii).

115 Treas. Reg. Sec. 1.274-11(b)(1)(iii).

116 *Walliser v. Commissioner*, 72 T.C. 433 (1974).

117 Treas. Reg. Sec. 1.274-11(b)(1)(iii).

118 Treas. Reg. Sec. 1.274-11(b)(1)(iii).

119 Treas. Reg. Sec. 1.274-11(b)(1)(ii).

120 Treas. Reg. Sec. 1.274-11(b)(1)(ii).

121 Treas. Reg. Sec. 1.274-11(b)(1)(ii).

122 Treas. Reg. Sec. 1.274-12(a)(1).

123 Treas. Reg. Sec. 1.274-12(b)(3).

124 I.R.C. Sec. 132(d).

125 Treas. Reg. Sec. 1.274-10(b)(3).

126 The primary purpose test applies to determine whether each passenger on each flight is traveling for business or personal purposes. Treas. Reg. Sec. 1.162-2(b).

127 It seems appropriate to determine the entertainment character of a passenger's flight based on the passenger's primary purpose for travel, since the regulations applied a "principal character or aspect" standard for purposes of the "directly related" test. Treas. Reg. Sec. 1.274-2(c)(3)(iii).

128 Treas. Reg. Sec. 1.274-10(e)(1).

129 Treas. Reg. Sec. 1.274-2(c)(3)(iii).

130 H.R. Rep. No. 87-1881, Section IV, B (1962).

131 *Walliser v. Comm'r*, 72 T.C. 433 (1979) (sightseeing vacation with customers); *Andress v. Comm'r*, 51 T.C. 863 (1969), aff'd per curiam, 423 F.2d 679 (5th Cir. 1970) (parties at taxpayer's residence); *Danville Plywood Corp. v. United States*, 899 F.2d 3 (Fed. Cir. 1990) (Super Bowl); *Manning v. Comm'r*, 1993-127 (meals and golf); *St. Petersburg Bank & Trust Co. v. United States*, 362 F. Supp. 674 (M.D. Fla. 1973) aff'd per curiam, 503 F.2d 1402 (5th Cir. 1974), cert. denied, 423 U.S. 834 (1975) (cocktail and dinner parties at taxpayer's residence).

132 Treas. Reg. Sec. 1.274-2(c)(4).

133 Treas. Reg. Sec. 1.274-2(c)(3)(iii).

134 Treas. Reg. Sec. 1.274-2(c)(7).

135 IRC Section 274(a)(1)(A); Treas. Reg. Sec. 1.274-2(d).

136 Treas. Reg. Sec. 1.274-2(d)(3)(i).

137 Treas. Reg. Sec. 1.274-2(d)(3)(i).

138 I.R.C. Sec. 274(e)(2); Treas. Reg. Sec. 1.274-10(a).

139 Preamble to Prop. Treas. Reg. Secs. 1.274-9, -10, Sec. 1(a); 72 Fed. Reg. 33,169, 33,171 (June 15, 2007).

140 Rev. Rul. 63-144, 1963-2 C.B. 129, Q&A 10, 76.

141 Treas. Reg. Sec. 1.274-9, -10.

142 Treas. Reg. Sec. 1.274-2(f)(2)(iii)(C), Example.

143 Exchange Act Rule 16a-2.

144 Exchange Act Rule 16a-1(f).

145 Treas. Reg. Sec. 1.274-9(c).

146 Treas. Reg. Sec. 1.274-10(b)(3); *see also* Preamble to Prop. Treas. Reg. Secs. 1.274-9, -10, Sec. 4; 77 Fed. Reg. 45,480, 45,481 (Aug. 1, 2012).

147 *See*, e.g., *Noyce v. Comm'r*, 97 T.C. 670 (1991); *Sutherland Lumber-Southwest, Inc. v. Comm'r*, 114 T.C. 197 (2000), aff'd, 255 F.3d 495 (8th Cir. 2001), acq. 2002-1 C.B. xvii; Temp. Treas. Reg. Sec. 1.274-5T(b)(6)(i)(B).

148 Treas. Reg. Sec. 1.274-10(e).

149 Prop. Treas. Reg. Sec. 1.274-10(a); Notice 2005-45, Sec. 5.

150 Treas. Reg. Sec. 1.274-10(e)(2)(iii).

151 Treas. Reg. Sec. 1.274-10(f)(3).

152 Preamble to Final Regs., Sec. 6; 77 Fed. Reg. 45,482.

153 Treas. Reg. Sec. 1.274-10(f)(3)(iii).

154 For a detailed explanation of the errors in the examples in the final Regulations, refer to the article on NBAA's website entitled "Final Regulations on Entertainment Use of Business Aircraft."

155 Treas. Reg. Sec. 1.274-10(d)(4).

156 Treas. Reg. Sec. 1.274-10(d)(2).

157 Preamble to Prop. Reg. Sec. 5i; 72 Fed. Reg. 33,169, 33,173 (Jun. 15, 2007).

158 Treas. Reg. Sec. 1.274-10(d)(1).

159 Treas. Reg. Sec. 1.274-2(e)(3)(i).

160 Treas. Reg. Sec. 1.274-10(e)(3)(ii).

161 *See, e.g., Noyce v. Comm'r*, 97 T.C. 670 (1991) (maintenance flights included in denominator).

162 Treas. Reg. Sec. 1.274-10(d)(3).

163 Treas. Reg. Sec. 1.274(d)(3)(ii).

164 Treas. Reg. Sec. 1.274-10(d)(3)(1).

165 The preamble to the final Regulations explains that under the proposed regulations (which did not limit the disallowance of straight-line depreciation to the allowable amount of depreciation) there was no transition adjustment for aircraft placed in service in prior years. Preamble to Final Regulations, Section 1(c), 77 Fed. Reg. 45,480. As noted above, under this transition rule, if an aircraft was placed in service in a year before the straight-line election, then the straight-line depreciation method was applied in the year of the election as if the aircraft had been depreciated under the straight-line method (rather than an accelerated method) since it was placed in service. The result was (and still is) that the transition rule could cause more than 100% of the cost of the aircraft to be subject to the entertainment disallowance. NBAA pointed out this problem in comments on the proposed regulation and suggested that Treasury provide for the change in depreciation method to the straight-line method to be made on a prospective basis. However, rather than adopt this approach, the preamble explains that Treasury adopted the limitation described above, because it would prevent the total amount of disallowed depreciation from exceeding the total amount of allowable depreciation over the life of the aircraft.

166 Treas. Reg. Sec. 1.274-10(d)(1).

167 Notice 89-35, Sec. VI, 1989-1 C.B. 675.

168 Prop. Treas. Reg. Sec. 1.274-10(d)(1).

169 Treas. Reg. Sec. 1.274-2(e)(3)(i).

170 Rev. Rul. 63-144, 1963-2 C.B. 129, Q&A 45 ("The facility expenditure limitations cover depreciation and general operating costs such as rent, utility charges, repairs, insurance, salaries of watchmen, etc."); TAM 9608004 (Feb. 23, 1996) (entertainment-facility disallowance applied to "fuel and oil, insurance, pilot's salary, repairs, hangar rental, and depreciation" with respect to an aircraft used 80% for business and 20% for customer trips to hunting lodge).

171 Other Section 274(e)(4) cases: Edilberto R. Beltran, TC Memo 1982-153., Code Sec(s). 162; 183; 274 (Mar. 25, 1982) (Christmas party for nurses employed by corporation deductible). William L. McReavy, TC Memo 1989-172., Code Sec(s). 162; 274; 301; 6653 (Apr. 17, 1989 (daughter's wedding not deductible).

172 Formerly Sec. 274(e)(6).

173 *See* Treas. Reg. Sec. 1.274-2(f)(2)(vi).

174 *See* Treas. Reg. Sec. 1.274-2(f)(2)(vi).

175 *See* Treas. Reg. Sec. 1.274-10(d)(2).

176 *See* Tech. Adv. Mem. 2002-14-007 (Section 274(e)(8) applied to company that provided use of facility to related company, based in part on fact that company was paid fair value for the use of the facility); Rev. Rul. 63-144, 1963-2 C.B. 129, Q&A 52, 53 (lessor not subject to entertainment facility disallowance on lease to related party with fair market rental rate and terms); Catalano v. Comm'r, T.C. Memo (RIA) 1998-447, aff'd, 240 F.3d 842 (9th Cir. 2001) (individual lessor and wholly owned S corporation lessee were respected as separate taxpayers for purposes of entertainment disallowance).

177 Preamble to Prop. Treas. Reg. Secs. 1.274-9, -10, Sec. 5(i); 72 Fed. Reg. 33,169, 33,173 (June 15, 2007).

178 H.R. Rep. No. 1447, 87th Cong., 2d Sess. 25-26 (1962); S. Rep. No. 1881, 87th Cong., 2d Sess. 37-38 (1962). [The exception in IRC Section 274(e)(8)] is designed to insure that a taxpayer who sells entertainment to others will be allowed to deduct expenses of producing that entertainment. Thus salaries paid to employees of nightclubs and amounts paid to performers other than employees will continue to be deductible by the operator. Moreover, since this type of expense is not considered to be "entertainment" the detailed substantiation requirements . . . will not apply.

179 Treas. Reg. Sec. 1.274-2(g).

180 Treas. Reg. Sec. 1.274-2(b)(2)(iii).

181 *See French v. Comm'r*, T.C. Memo (RIA) 1990-314 (family members accompanied taxpayer on private aircraft); *Pohl v. Comm'r*, T.C. Memo (RIA) 1990-298 (spouse accompanied taxpayer traveling by car); *Marlin v. Comm'r*, 54 T.C. 560 (1970), acq. 1970-2 C.B. xx (spouse accompanied taxpayer on trip to Europe); Rev. Rul. 56-168, 1956-1 C.B. 93; IRS Pub. 463, at 5 (2008).

182 Preamble to Prop. Treas. Reg. Secs. 1.274-9, -10, Sec. 5(h); 72 Fed. Reg. 33,169, 33,173 (June 15, 2007).

183 General Explanation of the Tax Reform Act of 1986 (the "Blue Book"), at 64 (J. Comm. Print 1987) ("the cost of transportation . . . is not reduced pursuant to this rule"). Thus, while the pre-2018 50 percent entertainment disallowance may have generally applied to business entertainment expenses, the legislative history to the Tax Reform Act of 1986 clarified that it does not apply to travel expenses.

184 Treas. Reg. Sec. 1.274-14(b).

185 Treas. Reg. Sec. 1.274-14(c)(2).

186 Treas. Reg. Sec. 1.274-14(c)(3).

187 *Id.*

188 Treas. Reg. Sec. 1.274-14(a) ("The rules in section 274(l) and this section do not apply to business expenses under section 162(a)(2) paid or incurred while traveling away from home.")

189 Treas. Reg. Sec. 1.274-14(c)(1).

190 Treas. Reg. Section 1.274-14(c)(a) provides that the exceptions in Section 274(e) do not apply, which would indicate that the commuting disallowance would not apply to the extent of amounts included in income under Sections 274(e)(2) and (9).

191 Treas. Reg. Sec. 1.274-14(a)(1).

192 *See* preamble to final section 1.274-13 and 14 regulations. 85 Fed. Reg. 81401 (Dec. 16, 2020).

193 Treas. Reg. Sec. 1.170A-1(g).

194 *Orr v. United States*, 343 F.2d 553 (5th Cir. 1965).

195 Treas. Reg. Sec. 1.162-20(a)(2).

196 I.R.C. Sec. 274(a)(1)(B).

197 Treas. Reg. Sec. 1.274-2(b)(1)(iii)(c).

198 Treas. Reg. Sec. 1.274-2(e)(iii)(b); *see also General Explanation of the Revenue Act of 1978* at 206 (J. Comm. Print 1979).

199 Preamble to Prop. Treas. Reg. Secs. 1.274-9, -10, Sec. 5(e); 72 Fed. Reg. 33,169, 33,172 (June 15, 2007).

200 Preamble to Final Regs., Sec. 5; 77 Fed. Reg. 45,481-2.

201 Treas. Reg. Sec. 1.274-2(e)(2)(i).

202 *Mediaworks, Inc. v. Comm'r*, T.C. Memo (RIA) 2004-177 (yacht was classified as entertainment facility).

203 FAR Sec. 91.501(b)(5).

204 FAA Chief Counsel Interpretation 1993-17 (Aug. 2, 1993) (involving Charles Schwab).

205 FAR Sec. 91.501(b)(6).

206 FAA Chief Counsel Interpretation 1989-22 (Aug. 8, 1989).

207 FAR Sec. 61.113(c).

208 https://www.faa.gov/about/office_org/headquarters_offices/agc/practice_areas/regulations/interpretations/data/interps/2010/nichols%20-%20(2010)%20legal%20interpretation.pdf

209 https://www.sec.gov/enforce/34-83581-s; Administrative Proceeding File No. 3-18570

210 *See, e.g., Noyce v. Comm'r*, 97 T.C. 670 (1991).

211 Treas. Reg. Sec. 1.162-2(b).

212 Preamble to Final Regs. Sec. 2.a; 77 Fed. Reg. 45,481; *see also* Treas. Reg. Sec. 1.274-10(a)(1).

213 *See* IRS Publication 463.

214 *See Noyce v. Comm'r*, 97 T.C. 670 (1991) for an illustration of the deduction rules of a director using his own aircraft for his director services and other business purposes.

About NBAA

Founded in 1947 and based in Washington, DC, the National Business Aviation Association (NBAA) is the leading organization for companies thta rely on general aviation aircraft to help make their businesses more efficient, productive and successful.

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