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| PROPOSED MASSACHUSETTS TAX EXPENDITURES  EVALUATION SUMMARY |
| EVALUATION YEAR: 2020 |

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| **TAX EXPENDITURE TITLE** | Exclusion from Employee Income of Business-Related Meals and Entertainment |
| **TAX EXPENDITURE NUMBER** | 1.019 |
| **TAX EXPENDITURE CATEGORY** | Exclusion from income |
| **TAX TYPE** | Personal income tax |
| **LEGAL REFERENCE** | M.G.L. c. 62, § 2(a) |
| **YEAR ENACTED** | M.G.L. c. 62, § 2 was enacted in 1973 but the exclusion stems from IRC § 132 |
| **REPEAL/EXPIRATION DATE** |  |
| **ANNUAL REVENUE IMPACT** | $24.6 to $28.1 million FY18 to FY22 |
| **NUMBER OF TAXPAYERS** | Any employed taxpayer may benefit (3.3 million taxpayers in 2018) |
| **AVERAGE TAXPAYER BENEFIT** | Average of $8 per personal income taxpayer |

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| **Description of the Tax Expenditure:**  Provides an income exclusion for the value of business-related meals and entertainment provided to employees, consistent with the federal exclusion. | **Is the purpose defined in the statute?**  The statute does not explicitly state the purpose of this tax expenditure. |
| **What are the fiscal, economic, or other goals of the expenditure according to the statute?**  To promote business activity by allowing employers to provide meals and entertainment to employees at business- related events without requiring such employees to report the value received as income. | **Are there other states with a similar Tax Expenditure?**  Many states adopt the definition of income under the Code and therefore follow the federal exclusion rules for business-related meals and entertainment provided by employers. |

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| Incentive Evaluation Results |

**INTRODUCTION**

Businesses are permitted to provide meals and entertainment to employees, at business-related events, without these benefits being treated as income to the employee. This is a federal income exclusion that is allowed for Massachusetts personal income tax purposes due to the state’s conformity with the Internal Revenue Code (“the Code”) for purposes of defining Massachusetts gross income.

**INTENT OF THE TAX EXPENDITURE**

The Code, and thus the Massachusetts personal income tax, generally includes all amounts received by employees from their employers in the employees’ taxable income (with specified exclusions). The exclusion of the value of meals and entertainment from employees’ income encourages business activity by shielding employees from additional tax resulting from attending business meals and entertainment events. In addition, the income exclusion simplifies wage reporting for employers.

**COSTS**

The estimated revenue loss is based on the Joint Committee on Taxation’s (“JCT”)[[1]](#footnote-1) annual calculation of the impact to federal tax collections of this income exclusion. The JCT estimate is allocated to Massachusetts using the state’s wage and salary disbursements as a percentage of the national figure, and then adjusting for differences in tax rates.

**Actual and Forecast Tax Loss of Excluding from Employees’ Income**

**Business-Related Meals and Entertainment ($millions)**



**BENEFITS**

The direct benefits of this tax expenditure are in the form of non-taxed compensation to employees, in an amount equal to the $28.1 million in FY22, cited above. Employees are not required to report the value of business-related meals and entertainment provided by employers on their tax returns. Thus, there is insufficient data to evaluate the distribution of the direct benefits across industries or income levels.

It should be noted that the benefits excluded under this section, while “infrequent” can range in value from minor, such as an office holiday luncheon, to significant, such as premium tickets to a sporting or entertainment event.

**EVALUATION: COMPARING COSTS AND BENEFITS**

When evaluating the cost of this tax expenditure it should be noted that, if taxed as compensation, the administrative cost to the Commonwealth of enforcing the income inclusion could be significant relative to the tax collected. In many cases, employer-provided meals or entertainment is infrequent, and/or the dollar value is relatively small. The cost of tracking, assessing, and collecting the tax would offset some of the benefits to the broader economy that would result from the tax collected.

When examining the benefits, in addition to the direct benefits to the employee, there are indirect benefits to the employer. Employer-provided meals and entertainment may foster collaboration and innovation, increase employee satisfaction, improve team cohesion, and boost morale.

**SIMILAR TAX EXPENDITURES OFFERED BY OTHER STATES**

Most states adopt the definition of income under the Code and therefore also provide an income exclusion for business-related meals and entertainment excluded under the Code.

According to a 2019 report by the Tax Foundation, although each state has its own additions and subtractions, twenty-nine states and the District of Columbia use federal adjusted gross income (AGI) as their starting point for calculating individual income tax liability, including Vermont, which adopted federal AGI as its starting point beginning with tax year 2018. Another six states (Colorado, Idaho, Minnesota, North Dakota, Oregon, and South Carolina) use federal taxable income. The remaining six states which tax wage income use state-specific definitions of income, although they incorporate some provisions from the Code into these definitions.[[2]](#footnote-2) We are not aware of any state that requires the inclusion of business-related meals and entertainment excluded under the Code.

**IS THE INCENTIVE AS DESIGNED ACCOMPLISHING ITS PURPOSE?**

To be completed further by TERC

Conclusion/Recommendations: [To be Entered by TERC]

1. The Joint Committee on Taxation is a nonpartisan committee of the United States Congress, originally established under the Revenue Act of 1926. <https://www.jct.gov/> [↑](#footnote-ref-1)
2. See *Toward a State of Conformity: State Tax Codes a Year After Federal Tax Reform*: https://taxfoundation.org/state-conformity-one-year-after-tcja/#\_ftnref8 [↑](#footnote-ref-2)