[COMMITTEE PRINT]

BUSINESS USE OF HOME, VACATION HOMES, AND FOREIGN CONVENTIONS

PREPARED FOR THE USE OF THE

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A. BUSINESS USE OF THE HOME

General

An individual's principal or other residence may be used for a variety of purposes in connection with his trade or business or in the production of income. Generally, a categorization of uses on a broad functional basis would include use of a residence or a portion of the residence (1) for an office or study for the performance of trade or investment-related clerical, bookkeeping, and research activities, (2) for a business office, storage area, or shop in which a trade or business is actively conducted, (3) for providing entertainment to the taxpayer's clients, customers or other business associates, (4) for lodging while away from home in the pursuit of a trade or business, and (5) for the production of rents. These uses of the residence may involve self-employed individuals, employees, or investors. Also, most of these uses may be availed of by taxpayers who are engaged in an almost unlimited range of occupations (including outside salesmen, attorneys, doctors, accountants, teachers, artisans, or investors).

The problems considered in this part of the pamphlet relate to the use of a principal or other residence by a taxpayer for both personal and business purposes. In some cases, a clearly delineated portion of the residence will be used on a full-time basis for business purposes. In other cases, it is more difficult to delineate that portion of the residence which is used for business purposes and that portion which is used for personal use. Additionally, when a residence is used on a part-time basis for both business and personal purposes, it is difficult to determine how much of the use is attributable to each of the activities. It is primarily the element of the dual use of a principal or other residence which raises the following issues: (1) whether a tax deduction is allowable with respect to any business use of the home, and (2) if so, how much may be deducted (i.e., how should expenses be allocated between business and personal use).

In the case where the expenses attributable to the residence are treated as deductible business expenses, an opportunity exists to convert nondeductible personal, living and family expenses into deductible business expenses. In addition to property taxes, interest and casualty losses attributable to the home which would be deductible in any event, the types of expenses for which an allocable portion may be claimed as a business expense include, for example, rent (if the taxpayer rents his home), depreciation, heat, electricity, insurance, cleaning and repairs. In the case of certain business uses of a home, it is more readily demonstrated that incremental costs are incurred by reason of the business use, e.g., where a portion of the home is exclusively used as a shop or business office in actively conducting a trade or business. With respect to some other uses, it may be extremely difficult to ascertain that any incremental cost has been incurred because of the

business use, e.g., the use of a family room on a part-time basis by an investor to review financial reports and periodicals.

In the case of a resort home which is maintained to entertain business clients and customers as well as for personal recreational purposes, it might be shown that certain incremental costs may have been incurred because of the nature and extent of the business use or that the home would not have been maintained but for the business purpose (i.e., the personal recreational motives for maintaining the resort home are incidental and subordinate to the principal business purpose). Thus, a showing of additional or incremental costs attributable to the use of a residence as an entertainment facility would depend on the facts and circumstances of a particular case. The same is true with respect to a home which is used for personal purposes and for lodging while away from the principal home in the pursuit of a trade or business, (e.g., the case where a business executive or professional maintains an apartment away from home because he must make frequent business trips to that destination). In certain cases, there may be no showing whatever of incremental costs incurred for lodging while away from home in the case of an employee on temporary assignment away from his "tax home" if he does not continue to maintain his permanent home or rents it out, (e.g., a professor on leave of absence while temporarily employed away from his permanent home).

With respect to the broad functional categorization of business uses described above, these uses may be further classified into two separate groups on the basis of those uses that do not directly produce income and those that do. The first group includes uses of the home which are essentially for the purpose of providing working space for the performance of services, clerical duties and the production of goods. The second group includes uses which result in the production of rents. Since different considerations may be involved with respect to each of these groups, the business uses other than rental activities are treated under the first section of this pamphlet and the rental activities undertaken with respect to a taxpayer's residence are treated in the second section of the pamphlet which deals with vacation homes.

Present Law

Under present law, no deductions are allowed for personal, living, and family expenses except as expressly allowed under the code (sec. 262). Generally, under this provision, expenses and losses attributable to a dwelling which is occupied by a taxpayer as his personal residence are not deductible. However, deductions for interest, certain taxes, and casualty losses attributable to a personal residence are expressly allowed under other provisions of the code. Moreover, if a portion of the residence is used in the taxpayer's trade or business or is used in the production of income, a deduction may be allowed for an allocable portion of the expenses incurred in maintaining such personal residence.

In any case involving the business use of a personal residence, there must a showing that the expenses were incurred in carrying on a trade or business (sec. 162) or for the production of income (sec. 212). Thus, there must be some relatively clear connection between the activities conducted in the home and a trade or business or the production of

income. Under the regulations (Reg. § 1.262–1(b)(3)), the expenses of maintaining a household are treated as nondeductible personal expenses if the taxpayer only incidentally conducts business in his home. However, if a part of the house is used as the taxpayer's place of business, the portion of the expenses attributable to the place of business is an allowable deduction.

For this purpose the expenses attributable to the office or business use of the home are deductible if they are "ordinary and necessary" expenses paid or incurred in carrying on a trade or business or for the production of income. These expenses are claimed as deductions by self-employed individuals who use portions of their residences for trade or business purposes, employees who maintain offices in connection with the performance of their duties, or investors who maintain offices in connection with investment activities. Typically, the expenses for which a deduction is claimed include an allocable portion of the depreciation or rent, maintenance, utility, and insurance expenses incurred in connection with the residence.

With respect to the maintenance of an office in an employee's home, the position of the Internal Revenue Service is that the office must be required by the employer as a condition of employment and regularly used for the performance of the employee's duties. (Revenue Ruling 62–180, 1962–2 C.B. 52, sets forth these standards as they apply to the deductibility of expenses attributable to an office maintained in an employee's home.)

Certain courts have decided that a more liberal standard than that urged by the Internal Revenue Service is appropriate. Under these decisions, the expenses attributable to an office maintained in an employee's residence are deductible if the maintenance of the office is "appropriate and helpful" to the employee's business. *George H. Newi*, T.C. Memo. 1969–131, aff'd 432 F. 2d 998 (2d Cir. 1970); *Jay R. Gill*, T.C. Memo. 1975–3; *Hall* v. *United States* 387 F. Supp. 612 (D.C.N.H., 1975).

In *Stephen A. Bodzin*, 60 T.C. 820 (1973), the Tax Court, in a decision allowing a deduction for an office in an employee's residence, held that "the applicable test for judging the deductibility of home office expenses is whether, like any other business expense, the maintenance of an office in the home is appropriate and helpful under all the circumstances." However, the court cautioned that no deduction would be allowable if personal convenience were the primary reason for maintaining the office notwithstanding any conclusion as to the "appropriateness" and "helpfulness" of the office. On appeal, the Fourth Circuit reversed the decision of the Tax Court (509 F. 2d 679). The Appellate Court held that, as a factual matter, the expenses attributable to the taxpayer's residence were nondeductible personal expenses and that it was therefore unnecessary to decide if the maintenance of the office was appropriate and helpful in carrying on his business. Thus, it is not clear as to which standard would be applied in the Fourth Circuit in a case in which the court found both personal and business use of a residence. However, the Court suggested that, to obtain a deduction, an employee would have to show that the office provided by the employer is not available at the times the employee uses the office in his residence or that the employer's office is not suit-

able for the purposes for which the taxpayer is using the office in his residence.

The Tax Court has also applied the "appropriate and helpful" standard to determine the deductibility of expenses attributable to the maintenance of an office in the home of an investor. (*Lena M. Anderson*, TC Memo 1974–49.) In that case, the taxpayer was allowed a portion of the expenses attributable to a family room which was partially used to conduct investment activities which consisted of keeping records with respect to rental properties, preparing the taxpayer's income tax returns, and writing letters to brokers and taxing authorities.

With respect to an apartment or residence used by a taxpayer while in a travel status, the expenses attributable to the maintenance of the apartment or residence are treated as lodging expenses subject to certain other rules relating to deductibility (sec. 162). As such, the expenses are deductible only if they are reasonable and necessary in the conduct of the taxpayer's business and directly attributable to it. "Lavish or extravagant" expenses are not allowable deductions. The expenses attributable to the apartment or house are deductible as lodging expenses if properly allocable to the taxpayer's trade or business even though the transportation expenses are not deductible because the trip was undertaken primarily for personal purposes.

Additional requirements also apply with respect to a residence where the business use consists of entertainment of clients, customers, or business associates. In such cases, the residence is treated as an entertainment facility, and no deduction is allowed for any expenditure unless the taxpayer establishes that the facility was used primarily for the furtherance of the taxpayer's trade or business and that the item of expense was directly related to the active conduct of such trade or business (sec. 274).

In determining whether or not an entertainment facility was used primarily for the furtherance of the taxpayer's trade or business, the taxpayer must establish that the primary use of the facility was ordinary and necessary based upon the facts or circumstances considered on a case-by-case basis. Generally, the actual use of the facility is controlling, and not its availability for use. The factors to be considered include the nature of each use, the frequency and duration of business use and the amount of expenditures incurred for business purposes.

The regulations provide that with respect to an entertainment facility, a taxpayer shall be deemed to have established that an entertainment facility was used primarily for the furtherance of his trade or business if more than 50 percent of the total calendar days of use of the facility during any taxable year were business use days.

An expenditure shall be considered directly related to the active conduct of the taxpayer's trade or business if four requirements are met: (1) the taxpayer had more than a general expectation of deriving income or benefit (other than goodwill) at some indefinite future time; (2) the taxpayer actually engaged in, or reasonably expected to engage in, business meetings, negotiations, etc., for the purpose of obtaining income or other benefits; (3) in light of all the facts and circumstances, the principal function of the combined business meeting, etc., and entertainment was the active conduct of the taxpayer's trade or

business, and (4) the expenditure was allocable to the taxpayer and person or persons with whom the taxpayer engaged in the active conduct of trade or business during the entertainment.

In determining the deductible amount attributable to the business use of the home, the general rule is that any reasonable method of allocation may be used. In all cases involving the dual use of a home, the expenses allocable to the portion of the residence used for business purposes would take into account the space used for those purposes, e.g., a percentable of the expenses based on the square feet of that portion compared to the total square feet of the residence. In addition, a further allocation based on time of use is required when the portion of the residence is not exclusively used for business purposes. In Rev. Rul. 62–180, 1962–2 C.B. 52, 54, the Internal Revenue Service held that, after allocating expenses attributable to a den used for business and personal purposes on the basis of space, a further allocation must be made on the basis of time of use to reflect the dual use. For purposes of the latter allocation, the Service ruled that the allocation should be made on the basis of availability for use rather than actual use, i.e., the ratio of time actually used for business purposes to the total time it is available for all uses. However, in *George W. Gino*, 60 T.C. 304, 314 (1973) (followed in *Lena M. Anderson*, T.C. Memo. 1974–49), the Tax Court held that such expenses should be allocated on the basis of actual business use as compared with actual total use.

In another case where the allocation could not clearly be determined, the Cohan rule was applied to estimate the approximate space of an apartment which was used for business purposes. *George H. Newi*, T.C. Memo. 1969–131, aff'd 432 F.2d 998 (2d Cir. 1970). The *Cohan* rule provides, generally, that where there is evidence that the taxpayer incurred certain deductible expenses but the exact amount cannot be determined, a close approximation would be acceptable and, therefore, the deduction would not be entirely disallowed. Under present law, however, because of certain substantiation requirements, no deduction is allowed for certain expenditures relating generally to travel or entertainment on the basis of a *Cohan* approximation or on the basis of unsupported testimony of the taxpayer.

Problem

It has been suggested that there is a great need for definitive rules to resolve the conflict that exists between several recent court decisions and the position of the Internal Revenue Service as to the correct standard governing the deductibility of expenses attributable to the maintenance of an office in the taxpayer's personal residence.

With respect to the "appropriate and helpful" standard employed in the court decisions, the determination of the allowance of a deduction for these expenses is necessarily a subjective determination. In the absence of definitive controlling standards, the "appropriate and helpful" test increases the inherent administrative problems because both business and personal uses of the residence are involved and substantiation of the time used for each of these activities is clearly a subjective determination. In many cases the application of the appropriate and helpful test would appear to result in the treatment of expenses which are directly attributable to the home (and therefore

not deductible) as ordinary and necessary business expenses, even though those expenses did not result in additional or incremental costs incurred as a result of the business use of the home. Thus, expenses otherwise considered nondeductible personal, living, and family expenses might be converted into deductible business expenses simply because, under the facts of the particular case, it was appropriate and helpful to perform some portion of the taxpayer's business in his personal residence. For example, if a university professor, who is provided an office by his employer, uses a den or some other room in his residence for the purpose of grading papers, preparing examinations or preparing classroom notes, an allocable portion of certain expenses might be claimed as a deduction even though only minor incremental expenses were incurred in order to perform these activities.

Proposals

1974 committee bill

Last year, the committee provided definitive rules of expenses attributable to the use of a taxpayer's home for business purposes. In general, a taxpayer would not be permitted to deduct any expenses attributable to the use of his home for business purposes. The proposal provides, however, for certain situations in which deductions for such expenses be permitted. A deduction would be permitted if a portion of the home is used exclusively on a rgular basis as:

(1) The taxpayer's principal place of business; or

(2) A place of business which is used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of business.

In the case of an employee, the business use must be for the convenience of the employer.

A special rule would have covered situations where self-employed individuals may use their home for trade or business purposes on a regular basis but do not use a specific portion of their home exclusively for such purposes. This rule would cover the situations where a trade or business is actively conducted by a taxpayer in his home and is not conducted at any other location. In this case, a deduction for the allocable expenses would be permitted but could not exceed the income generated by the business activities of the taxpayer in his home.

The deductions attributable to the rental of a portion of a taxpayer's home would be subject to the same limitations that would apply to vacation homes.

Mr. Ullman

His proposal is the same as that in the 1974 committee bill, except that he would not include the special rule described above.

B. VACATION HOMES

General

A taxpayer is allowed to deduct ordinary and necessary expenses that are paid or incurred with respect to an activity engaged in for profit. In addition, a taxpayer is allowed to deduct certain expenses even if it is determined that the taxpayer is not engaged in an activity for profit. This section of the pamphlet discusses the deductibility of expenses paid or incurred in connection with resort or vacation property which is used partially for business related purposes and partially for personal purposes.

Present Law

A taxpayer is allowed a deduction for the ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business (sec. 162), or for the management, conservation, or maintenance of property held for the production of income (sec. 212). In order to be entitled to a deduction under these provisions, it is necessary that the activity be engaged in by the taxpayer for profit (i.e., for the purpose of or with the intention of making a profit).[1] The determination of whether an activity is engaged in for profit is to be made on the basis of objective standards, taking into account all facts and circumstances of each case. Although a reasonable expectation of profit is not required, the facts and circumstances (without regard to the taxpayers subjective intent) must indicate that the taxpayer entered the activity or continued the activity with the objective of making a profit. No deduction is allowed under section 162 or section 212 if the activity is carried on primarily as a sport, hobby, or for recreation.

Even though an activity is not engaged in for profit (and therefore no deduction is allowed under sections 162 or 212), certain deductions are allowed under other provisions of the tax law. Subject to specific limitations discussed below, a deduction is allowed under section 183 for expenditures which are of the type that may be deducted without regard to whether they are in a trade or business or in the production of income. These items are the deductions which are allowed for interest (sec. 163) State and local property taxes (sec. 164), and the long-term capital gains deduction (sec. 1202).

Section 183 further provides that, in the case of an activity not engaged in for profit, a deduction is allowed for expenses which could be deducted if the activity were engaged in for profit, but only to the extent these expenses do not exceed the amount of gross income de-

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[1] See *Morton* v. *Commissioner*, 174 F. 2d 302, 304 (2 Cir.), cert. denied, 338 U.S. 828 (1949); *Schley* v. *Commissioner*, 375 F. 2d 747 (2d Cir.); and *George W. Mitchell*, 47 T.C. 120.

rived from the activity reduced by the deductions which are allowed in any event (e.g., interest and certain State and local taxes). In other words, as to expenses such as depreciation, insurance, and maintenance, a taxpayer is allowed a deduction but only to the extent of income derived from the activity. The taxpayer is not allowed to use these deductions to create losses which can be used to offset other income.

A taxpayer is presumed to be engaged in an activity for profit for the current taxable year if, in two or more years of the period of five consecutive taxable years (seven consecutive taxable years in the case of an activity which consists in major part of the breeding, training, showing, or raising of horses) ending with the current taxable year, the activity was carried on at a profit. For purposes of this presumption, the activity is treated as being carried on at a profit for a given taxable year if the gross income from the activity exceeds the deductions attributable to the activity which would be allowable if it were engaged in for profit.

The rules which apply in determining whether an activity is a trade or business or engaged in for the production of income also apply to the determination as to whether an activity is engaged in for profit. As a result, except for the presumption discussed above, if deductions with respect to the activity are not allowable as a trade or business expense (sec. 162) or as expenses incurred for the production of income, etc. (sec. 212), then the activity will be treated as an activity not engaged in for profit under section 183.

The Regulations provide a list of relevant factors which should normally be taken into account in determining if the activity is engaged in for profit. Among other factors, the presence of personal motives must be considered, especially where there are recreational or personal elements involved.[2] By way of illustration, the regulations indicate that a taxpayer will be treated as holding a beach house primarily for personal purposes if, during a three-month season, the beach house is personally used by the taxpayer for one month and used for the productions of rents for the remaining two months (Regs. § 1.183–1(d)(3)). However, except for this example, there are no definitive rules relating to how much personal use of vacation property will result in a finding that the rental activities of vacation homes are not engaged in for profit.

As previously discussed in the first section of this pamphlet, no deduction is allowed for personal, living, and family expenses except as otherwise expressly provided under the tax laws (sec. 262). Deductions that are expressly allowable even though they are attributable to personal use include items of interest, certain taxes, and casualty losses. However, no deduction is allowed for such items as depreciation, maintenance, insurance, and utilities to the extent these items are attributable to personal use. As a result, where property is used

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[2] Treas. Reg. § 1.183–2(b). These factors include: (1) The manner in which the taxpayer carries on the activity, (2) the expertise of the taxpayer or his advisors, (3) the time and effort expended by the taxpayer in carrying on the activity, (4) the expectation that assets used in the activity may appreciate in value, (5) the success of the taxpayer in carrying on other similar or dissimilar activities, (6) the taxpayer's history of income or losses with respect to the activity, (7) the amount of occasional profits, if any, which are earned, (8) the financial status of the taxpayer, and (9) the elements of personal pleasure or recreation.

for both personal and business use, the total amount of maintenance, insurance, and utilities expenses and depreciation incurred during a taxable year must be allocated on a reasonable and consistently applied basis.

Problem

As previously mentioned where expenses attributable to a residence are treated as deductible business expenses, an opportunity exists to convert nondeductible personal, living and family expenses into deductible expenses. In the case of so-called "vacation homes" that are used both for personal purposes and for rental purposes, it has been argued that the rental activities are undertaken to minimize the expenses of ownership of the property rather than to make an economic profit.

In selling vacation homes, it has become common practice to emphasize that certain tax benefits can be obtained by renting the property during part of the year, while reserving the remaining portion for personal use. In addition, certain arrangements have been devised whereby an individual owner of a condominium unit is entitled to exchange the time set aside for the personal use of his own unit (typically three to six weeks) for the use of a different unit under the same general management at another location.

Under many of these arrangements, it is extremely difficult under existing law to determine when an activity is engaged in for profit. The present Regulations provide that in making this determination, a number of factors shall be taken account of including the presence of "personal motives" especially where there are recreational or personal elements involved. However, except for the example mentioned above, no objective standards are set forth in the regulations. As a result, it is argued that definitive rules should be provided to specify the extent of personal use which, in the absence of other pertinent factors, will result in the allowance of deductions allocable to the rental activities as well as the extent of personal use which would result in the disallowance of certain deductions in excess of gross income. In a case where personal use is the controlling factor to be considered, this approach would obviate the need to require subjective determinations to be made concerning the taxpayer's motive and the primary purpose for which the vacation home is held.

In addition, it is argued that if there is any personal use of a vacation home, the portion of expenses allowable to rental activities should be limited to an amount determined on the basis of the ratio of time that the home is actually rented, to the total time the vacation home is used during the taxable year for all purposes (i.e., rental, business, and personal activities).

Proposals

1974 committee bill

The committee last year provided that if a vacation home is used by a taxpayer for personal purposes for more than two weeks or 5 percent of the actual business use (that is, its actual rental time), then deductions would be subject to two limitations whether or not the presumption under present law would otherwise apply. These limitations would not apply if the vacation home is used for personal purposes for two

weeks or less, or no more than 5 percent of the actual business use. In addition, they would not apply if the rental of the vacation home results in a profit for the year.

However, where the two week or 5 percent rule does apply, first, the allowable deductions for trade or business or production of income relating to the vacation home are not to be allowed as deductible expenses to the extent they exceed the gross income from the business use of the vacation home. Second, where the two weeks or 5 percent rule applies, the deductions treated as being attributable to the rental activities would be limited to *actual* rental use divided by the total *actual* use of the property (that is, business use plus personal use) times the business expenses attributable to the vacation home (other than expenses which are allowable in any event).

Mr. Ullman

His proposal is the same as the 1974 committee bill.

C. FOREIGN CONVENTIONS

Present Law

Under present law, the deductibility of traveling expenses paid or incurred to attend a foreign convention, seminar, or similar meeting while away from home is governed by the ordinary and necessary standard under sections 162 and 212 of the code and, in certain cases, the special disallowance rules provided under section 274(c).

Generally, to be deductible, traveling expenses must be reasonable and necessary in the conduct of the taxpayer's business and directly attributable to the trade or business. If a trip is primarily related to the taxpayer's business and the special foreign travel allocation rules do not apply, the entire traveling expenses (including food and lodging) to and from a destination are deductible. If a trip is primarily personal in nature, the traveling expenses to and from the destination are not deductible even if the taxpayer engages in business activities while at the destination.[1] However, expenses incurred while at the destination which are allocable to the taxpayer's trade or business are deductible even if the transportation expenses are not deductible.

With respect to expenses incurred in attending a convention or other meeting, the test under section 162 is whether there is a sufficient relationship between the taxpayer's trade or business and his attendance so that he is benefiting or advancing the interests of his trade or business. Generally, deductibility depends upon the facts and circumstances of each particular case. (Reg. § 1.162–5(e)(1)). If the convention is for political, social, or other purposes unrelated to the taxpayer's business, the travel expenses are not deductible. The Internal Revenue Service has ruled that the test for allowance of deductions for convention expenses is met if the agenda of the convention or other meeting is so related to the taxpayer's position as to show that attendance was for business purposes. (Rev. Rul. 63–266, 1963–2 C.B. 88).

If an individual travels away from home primarily to obtain education for which the expenses are deductible as a trade or business expense, the expenses for travel, meals, and lodging incurred while away from home are deductible. However, the portion of the travel expenses attributable to personal activities, such as sightseeing, is treated as a nondeductible personal or living expense. If the travel away from home is primarily personal, only the meals and lodging incurred during the time spent in participating in educational pursuits are deductible. Further, in the case of foreign travel to obtain education, deductions are subject to special allocation rules.

Under section 274(c) of the code, expenses of travel outside the United States are deductible only to the extent allocable to the tax-

[1] See *Patterson* v. *Thomas*, 289 F. 2d 108 (5th Cir., 1961); *Espandiar Kadivar*, T.C. Memo 1973–95; Rev. Rul. 74–292, 1974–1 C.B. 43.

payer's trade or business or income-producing activities if such travel is for more than one week or the time of travel outside the United States which is not attributable to the pursuit of the taxpayer's trade or business is 25 percent or more of the total time on such travel. In the case of foreign travel to which section 274(c) applies, this allocation requirement overrides the general rule that the entire expenses of travel are deductible if the primary purpose of the trip was related to a trade or business.[2]

Problem

Serious administrative problems have arisen because of the recent proliferation of conventions, educational seminars, and cruises which are ostensibly held for business or educational purposes, but which are held at locations outside the United States primarily because of the recreational and sight-seeing opportunities. In Technical Information Release 1275 (February 14, 1974), the Internal Revenue Services announced that it intended to scrutinize deductions for business trips, conventions, and cruises which appear to be vacations in disguise. The Service noted that a number of professional, business and trade organizations have been sponsoring cruises, trips and conventions during which only a small portion of time is devoted to business activity and that the practice seemed to be growing. In cases where there are indications of abuse, the Service intends to request lists of the names and addresses of the participants on cruises and other trips. However, allowance of deductions claimed by participants would continue to depend upon the facts and circumstances, including the relationship of the meeting to a particular taxpayer's trade or business, as under present law.

As indicated above, the basic test that is applied by the Internal Revenue Service is whether the convention or other meeting is primarily related to the taxpayer's business or whether it is primarily personal in nature. Thus, in administering this test, the Internal Revenue Service is required to make a subjective determination as to the motives and intentions of the taxpayer after taking all the facts and circumstances in a particular case. One of the important factors that is considered by the Service in making this subjective determination is the amount of time spent on business activities as compared to the amount of time spent on personal activities. There are no specific guidelines or formulae in the statute or regulations that specify when this factor will weigh in the favor of or against the taxpayer. The taxpayer is not required to keep detailed records relating to the amount of time spent on each of these activities. Upon audit, the taxpayer frequently attempts to substantiate the business nature of his trip by providing the Service with the agenda from the meeting or a certificate of attendance which is furnished by the organization sponsoring the meeting.[3]

The administrative problems created by the lack of specific guidelines are substantial. The process of trying to ascertain all the facts

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[2] If less than 25 percent of the total foreign travel time is attributable to business activities, no deduction would be allowable for the traveling expenses to and from the taxpayer's destination because the trip would be considered primarily personal. (Reg. § 1.162–2(b)).

[3] A few organizations now maintain attendance records and require participants to "sign in" at each session of the convention or seminar.

and circumstances is extremely time consuming both for the taxpayer and the Service. Further, additional importance is placed on the subjective judgment of the IRS because of the basically "all or nothing" approach under present law. If the primary purpose is determined to be pleasure, no amount of the travel expense can be deducted. Since reasonable and competent auditors will differ in evaluating all the facts and circumstances, the deduction of one taxpayer may be totally disallowed while another taxpayer (perhaps with slightly differing facts) can obtain a complete deduction for travel expenses. This disparity of treatment results in complaints that the Service does not treat taxpayers equally.

Many argue that the lack of specific detailed requirements has resulted in a proliferation of conventions, seminars, etc. which, in effect, amount to Government-subsidized vacations and serve little, if any, business purpose. Those making this argument point out that the promotional material often highlights the deductibility of the expenses incurred in attending a convention or seminar and, in some cases, describe the meeting in such terms as a "tax-paid vacation" in a "glorious" location. In addition, they point out that there are organizations that advertise that they will find a convention for the taxpayer to attend in any part of the world at any given time of the year. This type of promotion has an adverse impact on public confidence in the fairness of the tax laws.

Few would dispute that many conventions and similar meetings serve a bona fide business purpose and that individuals attending them benefit by exchanging ideas and technology, improving professional skills, and observing new products. However, it would appear questionable whether a deduction should be allowed for expenses incurred in connection with a convention held outside the United States when an organization's membership has no international purpose, especially when the membership represents a relatively small geographic area. Many question whether a deduction should be allowed for expenses incurred in attending a seminar of any local organization held in an attractive resort area outside the United States. On the other hand, others argue that it is improper to provide much more stringent rules for meetings outside the United States than for meetings inside the United States. For example, those making this argument state that at least rules which apply should not deny all deductions for meetings held in London, England, while allowing deductions without significant limitations for meetings held in Honolulu, Hawaii.

Proposals

1974 committee bill

Last year the committee limited deductions allowable for the expenses of taxpayers attending conventions, educational seminars or similar meetings outside North America. The general rule agreed to by the Committee was that no deduction is allowable for foreign travel expenses (including expenses for transportation, meals and lodging) for an individual with respect to a convention, seminar or similar meeting held outside North America unless, taking into account certain factors, it is more reasonable to hold the meeting

outside the North American area. North America is defined to include the Caribbean.

The general rule would not apply to a meeting conducted by an organization which has foreign members to the extent the number and location of its foreign meetings are reasonable in light of the number of foreign members and their geographical dispersion. Present law relating to the allocation of expenses would continue to apply in any case where the travel expenses attributable to foreign meetings may still be deductible.

This rule also is not intended to apply to the expenses incurred in attending a convention, etc., at a location that is uniquely suited to the purposes of the convention, provided that the attendance at the conference by an individual is related to his trade or business. Thus, a deduction would be allowed in the case of an individual who attends a meeting conducted or sponsored by a domestic organization which meets outside North America if there is a compelling reason for meeting outside, taking into account the membership and purpose of the organization.

Mr. Ullman

His proposal is the same as the 1974 committee bill except that in no event would deductions be allowable for cruises. He also wishes to review possible rules which might be imposed before deductions are allowed for conventions, conferences, etc., within North America.

Mr. Karth

The proposal would disallow, in the case of professional and other closely held corporations, the expense of attending shareholder or directors' meetings held outside the United States or, if within the United States, not held at the principal place of business of the corporation.

Mr. Helstoski

The proposal would end business deductions for all foreign held conventions with the following exceptions: (1) individuals attending conventions of international organizations provided that they are members of the organization or they attend as a representative of a U.S. member organization; and (2) conventions, etc., attended by U.S. citizens living abroad as bona fide residents of foreign countries (e.g., an uninterrupted period that includes one full tax year or 510 days during a period of 18 consecutive months—foreign residency rules presently in sec. 911 of the code). The proposal would provide deductions for conventions outside of the United States (not including possessions) only to the extent they meet the criteria set forth above.

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