

DEDUCTION FOR EXPENSES TO  
INFLUENCE LEGISLATION, ETC.

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PREPARED FOR THE USE OF THE  
COMMITTEE ON WAYS AND MEANS  
OF THE  
HOUSE OF REPRESENTATIVES  
BY THE  
STAFF OF THE JOINT COMMITTEE ON  
INTERNAL REVENUE TAXATION



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## A. PRESENT LAW

For more than 40 years Treasury regulations have held that lobbying expenses are not deductible from gross income, even though such expenses are lawful and would clearly qualify as ordinary and necessary business expenses, because the deduction of such expenses would contravene a "sharply defined public policy." The validity of these regulations has frequently been challenged, but the courts have consistently held that, in the absence of any expression of congressional intent to the contrary, disallowance of the deduction by the regulations is valid. The courts have taken the position that these provisions of the regulations have acquired the force of law by reason of congressional reenactment, without change, of the basic provisions of the statute underlying the regulations.

The provisions of the regulations in effect prior to the enactment of the 1954 Code simply provided that sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions to campaign expenses, are not deductible from gross income.

The new regulations under section 162 of the 1954 code, promulgated on December 28, 1959, retain the basic rule of the earlier regulations, but, in addition, state for the first time that this rule requires the disallowance as a deduction of several different specific classes of expenditures. Thus, the new regulations state that the rule requires disallowance of a deduction for that portion of dues and other payments to any organization, a "substantial part" of the activities of which consist of lobbying, to the extent that such amounts are "attributable to" its lobbying activities—even though such dues and payments would otherwise qualify for deduction under section 162. Similarly, the regulations now state that expenditures for the promotion or defeat of legislation include expenditures for the purpose of attempting to influence members of a legislative body, directly or indirectly, by urging or encouraging the public to contact such members. Further, the regulations now state that such expenditures include expenses incurred for the purpose of attempting to influence the public to approve or reject a measure in a referendum, initiative, a vote on a constitutional amendment, or similar procedure. The new regulations also indicate for the first time that expenses may be considered as lobbying expenses whether they are incurred to influence the legislators directly or to influence them indirectly by means of "grass-roots" campaigns aimed at the voters.

## B. THE PROBLEM

The promulgation of the new regulations, as well as a recent decision of the Supreme Court in *Cammarano v. U.S.*, 358 U.S. 498 (1959), has provoked sharp criticism of the rule disallowing a deduction for such expenses and has stimulated widespread interest in having Congress reconsider the basic policy questions involved.

(1) *Problems of administration and compliance*

A great deal of criticism has been directed to the difficulties of administration and compliance which arise under the rule of the regulations. Many have stated that it is virtually impossible to administer the rule on a uniform and nondiscriminatory basis, and that the practical difficulties of enforcement are such that the rule has probably been applied only unevenly and occasionally in the past. The Treasury Department itself, in its letter of February 26, 1960, to the chairman of this committee, stated as follows:

It is only realistic to recognize that many of the expenditures in these areas which have passed the permissible borderline under the existing regulations have doubtless escaped detection in the audit of tax returns. Unless the Internal Revenue Service were to devote disproportionate manpower from its basic collection function to policing this difficult and controversial area, it would seem that uniform enforcement would be an unattainable goal. If there were to be a modification or relaxation of the existing rules, therefore, it would appear to be a desirable objective that it should help reduce, rather than aggravate, the practical administrative problems which are inherent in this area, and at the same time reduce to a minimum whatever inequalities among some taxpayers result from unavoidable imperfections in the administration of the law.

Areas cited as being those in which there may be extreme difficulty in establishing with accuracy the proportion of an expenditure which is attributable to influencing legislation include expenses for membership in organizations, expenses for legal and other services, expenses for advertising, etc.

(2) *Substantive problems*

Much of the criticism has also been directed to the substantive policy of the basic rule. It has been strenuously urged that if an expenditure is ordinary and necessary to the conduct of a taxpayer's trade or business and is lawful, it is unfair for the deduction to be disallowed because the expense is incurred to influence legislation. Many have pointed out, for example, that expenditures to influence legislation or the outcome of a referendum may be necessary for the very survival of the taxpayer's business. This might be the case, for example, where a measure before the voters in a referendum would outlaw the taxpayer's business, as was the situation in the *Cammarano* case. The point is also made that the deduction for expenses to influence legislation is disallowed on the grounds that allowance of the deduction would "frustrate sharply defined public policy," despite the fact that such expenses are lawful under legislation relating to lobbying activities and are not subject to any civil or criminal sanction. It is stated further, in this connection, that any effort to classify expenses to influence legislation as "bad" or "good" should be undertaken directly in legislation dealing with the subject and not indirectly through the tax laws. In this regard, however, it has been urged that it would be inappropriate for Congress by any means—whether by imposing limits on the deductibility for expenses for tax purposes or

otherwise—to discourage efforts by the interested public to advise and assist their representatives in formulating legislation. It is further stated that even if it should be decided to limit the deduction for expenses to influence legislation on some grounds of public policy, the limits on the deduction should be determined by Congress through legislation and not by the Secretary through regulations.

### C. BILLS INTRODUCED AND OTHER SUGGESTED APPROACHES

#### (1) *Bills introduced*

There have been a large number of bills introduced which are directed to this problem.

Several of the bills are designed to reverse the basic rule now stated in the regulations and would, in effect, prevent any lawful expenditure which otherwise qualifies as a deduction from being disallowed as a deduction simply because incurred to influence legislation or action of the voters. Bills which take this approach include H.R. 7123 (Mr. Boggs), H.R. 10272 (Mr. Miller), H.R. 10502 (Mr. Lafore), H.R. 10848 (Mr. Dooley), H.R. 11153 (Mr. Teague), H.R. 11507 (Mr. Byrnes), H.R. 11866 (Mr. Mason), H.R. 12074 (Mr. Brooks), H.R. 12271 (Mr. Goodell), and S. 3145 (Mr. Hartke).

Some of the bills are more limited in scope and, generally speaking, would prevent the rule of regulations from disallowing a deduction only in the case of expenditures to influence action of the voters in a referendum, initiative, or similar proceeding. The bills which take this approach include H.R. 5193 (Mr. Forand), H.R. 5251 (Mr. King), H.R. 5579 (Mr. Karsten), and H.R. 6376 (Mr. Pelly).

Two other companion bills, H.R. 10591 and H.R. 10592, introduced by Messrs. Mills and Mason on behalf of the American Bar Association, include as a section 10 a provision which would permit the deduction from gross income of expenditures which otherwise qualify as deductions under either section 162 or section 212, but would limit the deduction to "reasonable expenses (including, but not limited to, traveling expenses and the cost of preparing testimony) incurred by a taxpayer in connection with appearances before, or submission of statements to, the committees of Congress" or of other legislative bodies.

#### (2) *Treasury comments*

The comments of the Treasury Department with respect to this subject have been set forth in a published letter of February 26, 1960, to the chairman of this committee, reporting the views of the Department with respect to some of the bills which have been introduced. (See, particularly, pp. 9-11.)

As part of its comments the Treasury states as follows:

A reasonable approach which should not lend itself to abuse would be the allowance of deduction of reasonable expenses directly connected with appearances and submissions at public hearings before committees of Congress or of any other comparable legislative body if such expenses otherwise satisfy the requirements of deductibility in the code. Broader legislation may well be indicated but should be examined in light of the policy considerations outlined in this report and in the light of possible need for safeguards or limitations. The Treasury recommends early consideration by the Congress of the various proposals designed to modify the bar to deductibility of expenditures in connection with the legislative process.

*(3) Department of Commerce comments*

In his published letter of February 25, 1960, to the chairman of this committee, the Secretary of Commerce stated in part that the Department favors the enactment of H.R. 7123 (Mr. Boggs) or of similar remedial legislation.

## D. STAFF SUGGESTION

If the committee desires to take action in this area, the joint committee staff suggests an approach—basically the same as that of H.R. 7123 and the similar bills described above—under which any expenditure which otherwise qualifies for deduction as an ordinary and necessary business expense under section 162 would not be disallowed as a deduction merely because incurred to influence action by a legislature with regard to any legislative or constitutional proposal or to influence action of the voters with respect to any such proposal submitted to them by initiative, referendum, or similar proceeding. Under the staff approach, however, it would be made clear that the provisions of the amendment should not be construed as allowing a deduction of any amount paid for participation or intervention in any political campaign on behalf of or in opposition to any candidate for public office. In addition, the staff would restate the substance of the bills in order to eliminate certain technical problems. Under the staff suggestion the amendment would apply to taxable years ending after the date of its enactment. A draft embodying the suggested approach in more detail appears below.

In order for an expense to influence legislation, etc., to be deductible under the approach suggested by the staff, it would have to meet the various tests prescribed by the statute, the regulations, and the court decisions for deductibility of any ordinary and necessary business expense. Thus, to be deductible, an expense to influence legislation, etc., would have to be (1) ordinary and necessary in carrying on a trade or business, (2) an expenditure which is not required to be capitalized, and (3) an expenditure which is not a personal expense. In addition, under the regulations and decisions interpreting the statute, the expense would have to be (1) reasonable in amount, and (2) an expenditure the deduction of which is not disallowed because it is made in violation of a sharply defined policy set forth in a Federal or State statute which makes such expenditure unlawful.

The staff believes that of the various approaches which have been put forward, the approach suggested would do the most to alleviate the severe problems of administration and compliance raised by the rule of the existing regulations. The groups commenting on the various approaches suggested all concur in this view. The staff also believes that if the committee desires to take some action in this area, the approach suggested avoids the necessity of drawing arbitrary distinctions between expenditures which are not essentially different in purpose and effect.

## E. DISCUSSION DRAFT OF STAFF SUGGESTION

Section 162 of the Internal Revenue Code of 1954 is amended by redesignating subsection (d) thereof as subsection (c), and by adding a new subsection (d) as follows:

## (d) CERTAIN EXPENSES TO INFLUENCE ACTION WITH RESPECT TO LEGISLATIVE PROPOSALS, ETC.—

(1) GENERAL RULE.—No expenditure which otherwise qualifies as a deduction under subsection (a) (including but not limited to, dues and other amounts paid to any organization) shall be disallowed as a deduction merely because incurred to support or oppose or otherwise influence action by the Congress or by any legislative body of a State, a territory, a possession of the United States, the District of Columbia, or any political subdivision of the foregoing, with regard to any legislative or constitutional proposal, or to support or oppose or otherwise influence action of the voters with respect to any legislative or constitutional proposal submitted to them by initiative, referendum, recall, or similar proceeding.

(2) EXCEPTION.—The provisions of paragraph (1) shall not be construed as allowing the deduction of any amount paid (whether by way of contribution, gift or otherwise) for participation or intervention in any political campaign on behalf of, or in opposition to any candidate for public office.

SEC. 2. The amendment made by section 1 of this Act shall apply to taxable years ending after the date of enactment of this Act.

## F. APPENDIX.—PROVISIONS OF TREASURY REGULATIONS UNDER 1939 AND 1954 CODES

## 1. 1939 code regulations

The provisions of regulations under the 1939 Code with respect to deduction of expenses to influence legislation appeared at sections 39.23(o)–1(f) and 39.23(q)–1(a), and read as follows:

(f) Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income.

## 2. 1954 code regulations

The provisions of regulations under the 1954 Code with respect to deduction of expenses to influence legislation appear at section 1.162–15(c), and read as follows:

## § 1.162–15(c)

(1) Expenditures for lobbying purposes, for the promotion or defeat of legislation, for political campaign purposes (including the support of or opposition to any candidate for public office), or for carrying on propaganda (including advertising) related to any of the foregoing purposes are not deductible from gross income. For example, the cost of advertising to promote or defeat legislation or to influence the public with respect to the desirability or undesirability of proposed legislation is not deductible as a business expense, even though the legislation may directly affect the taxpayer's business. On the other hand, expenditures for institutional or 'good will' advertising which keeps the taxpayer's name before the public are generally deductible as ordinary and necessary business expenses provided the expenditures are related to the patronage the taxpayer might reasonably expect in the future. For example, a deduction will ordinarily be allowed for the cost of advertising which keeps the taxpayer's name before the public in connection with encouraging contributions to such organizations as the Red Cross, the purchase of United States Savings Bonds, or participation in similar causes. In like fashion, expenditures for advertising which present views on economic, financial, social, or other subjects of a general nature but which do not involve any of the activities specified in the first sentence of this subparagraph are deductible if they otherwise meet the requirements of the regulations under section 162.

(2) Dues and other payments to an organization, such as a labor union or a trade association, which otherwise meet the requirements of the regulations under section 162, are deductible in full unless a substantial part of the organization's activities consists of one or more of those specified in the first sentence of subparagraph (1) of this paragraph. If a substantial part of the activities of the organization consists of one or more of those so specified, deduction will be allowed only for such portion of such dues and other payments as the taxpayer can clearly establish is attributable to activities other than those so specified.

The determination as to whether such specified activities constitute a substantial part of an organization's activities shall be based on all the facts and circumstances. In no event shall special assessments or similar payments (including an increase in dues) made to any organization for any of such specified purposes be deductible.

(3) Expenditures for the promotion or the defeat of legislation include, but shall not be limited to, expenditures for the purpose of attempting to—

(i) Influence members of a legislative body directly or indirectly, by urging or encouraging the public to contact such members for the purpose of proposing, supporting, or opposing legislation, or

(ii) Influence the public to approve or reject a measure in a referendum, initiative, vote on a constitutional amendment, or similar procedure.

