TAXATION OF FREE SPEECH

THOMAS E. SUNDERLAND†

The title of this article has been chosen carefully. Nevertheless, some explanatory comment may be helpful. The article deals with the deductibility from gross income of expenses for activities which influence legislation, either at the federal, state or local level.¹ The activities in question run the gamut from those of the full-time professional Washington lobbyist to occasional or even accidental contacts with members of Congress by officers or employees of a business firm. They embrace public relations programs and institutional advertising aimed at creating a favorable climate of public attitude. Whatever the mechanics involved, however, the activities have two things in common. They cost money and they have all the orthodox earmarks of ordinary and necessary business expenses.²

More is involved than would be covered by the title "Deductibility of Legislative Expenses." The activities discussed here involve freedom of speech and the right to petition, which the courts have consistently declared to be among our most "preferred" freedoms.³ The mere suggestion of a direct tax on some speech "value" would be shocking. But, from a practical standpoint, that is exactly what is happening today under the Internal Revenue Code. Tax deductions for the expenses of exercising these constitutional rights are

† Member of the Chicago Bar.


now universally disallowed. The rejection of tax deductibility for an ordinary and necessary business expense, because it is incurred for the purpose of influencing legislation, frequently results in doubling the cost of these activities. While the exact cost will vary with the tax rates of different taxpayers, the inevitable effect is to deter the exercise of a constitutional right.

The problem is squarely presented in a case involving a small Tacoma, Washington, partnership now pending before the United States Supreme Court. Mr. Cammarano and his wife owned a quarter interest in a partnership carrying on the wholesale distribution of beer. Pursuant to the state constitution, a proposal was submitted to the voters in 1948 which would have placed the retail sale of wine and beer exclusively in state-operated stores and would have put the partnership out of business. Accordingly, the entire industry undertook a publicity program directed to the citizens who were to vote on the measure. Mr. and Mrs. Cammarano contributed $886.29 to the program, for which they claimed a deduction as an "ordinary and necessary" business expense. When this was disallowed by the Commissioner, they paid the $153.98 tax and brought suit for recovery in the District Court.

It must have been a meager source of comfort to the Cammaranos to hear the District Court deny their claim but announce:

This is not to indicate that there is anything evil or corrupt about spending money for these purposes. Quite the contrary. The expenditure of money to enlighten and inform the public with respect of initiative measures is a perfectly proper and laudable activity. When the general public are called upon to enact or refuse to enact legislation, the more information they are given and the more widespread it is distributed the better. Certainly neither this taxpayer nor the Washington Brewers Institute nor the brewing industry are in any manner to be criticized for having spent the money to defeat the legislation by fair publicity. They had a right to do that and propriety of expenditures therefor is not in question.8

Is there any justification for a tax policy which penalizes the constitutional right to keep the public informed by activity judicially determined to be "proper and laudable?" Significantly, the text of the Revenue Code contains no denial of deductibility in these circumstances. Yet denial of the tax deduction by the lower courts in the Cammarano case falls into a pattern set in Textile Mills Securities Corp. v. Comm’r6 in 1941 and followed by the courts and the Internal Revenue Service ever since.7

6 314 U.S. 326 (1941).
TAXATION OF FREE SPEECH

The Cammaranos are not alone in their plight. Increased intervention by government in all matters of private economic concern has given to all business and industry a direct interest in governmental programs and policies. Indeed, the continued preservation of concepts basic to our political and economic system, such as free markets and a competitive system, becomes a matter of self-preservation so far as private interests are concerned.

In a democratic society private interests should have an unfettered right of presenting their views to the lawmakers, and the free exercise of this right is one of the distinctive features of our governmental system. Our legislatures cannot function well unless they can know all the facts and hear the opinions on all sides of an issue. The theory of our Constitution is that society itself is best served by free trade in ideas. It is anomalous that our tax laws should run diametrically counter to this fundamental philosophy.

THE STATUTORY CONTEXT

There are two provisions in the Internal Revenue Code of 1954 which form the statutory basis for determining the deductibility of legislative expenses. Section 162 authorizes a deduction for "all the ordinary and necessary expenses... in carrying on any trade or business." A seemingly unrelated section of the law also must be noted. Section 170 allows deductions of educational or charitable contributions. Section 170(c) defines these contributions

Co. v. Comm'r, 19 T.C. 297 (1952), rev'd on other grounds 217 F.2d 329 (C.A.9th, 1954); Delaware Steeplechase and Race Assoc. v. Comm'r, 9 T.C.M. 893 (1950); Bellingrath v. Comm'r, 46 B.T.A. 89 (1942); Smith v. Comm'r, 3 T.C. 696 (1944), allowing a lawyer to deduct a contribution to the Missouri Institute for the Administration of Justice, whose purpose was the adoption of an amendment to the state constitution. The Commissioner's acquiescence in this decision was recently withdrawn. Int. Rev. Bull. No. 1958-21, May 26, 1958.

Justice Holmes summed this up in his famous dissenting opinion in Abrams v. United States, 250 U.S. 616 (1919): "Persecution for the expression of opinions seems to me perfectly logical. If you have no doubt of your premises or your power and want a certain result with all your heart you naturally express your wishes in law and sweep away all opposition. To allow opposition by speech seems to indicate that you think the speech impotent, as when a man says that he has squared the circle, or that you do not care whole-heartedly for the result, or that you doubt either your power or your premises. But when men have realized that time has upset many fighting faiths, they may come to believe even more than they believe the very foundations of their own conduct that the ultimate good desired is better reached by free trade in ideas—that the best test of truth is the power of the thought to get itself accepted in the competition of the market, and that truth is the only ground upon which their wishes safely can be carried out. That at any rate is the theory of our Constitution. It is an experiment, as all life is an experiment. Every year if not every day we have to wager our salvation upon some prophecy based upon imperfect knowledge. While that experiment is part of our system I think that we should be eternally vigilant against attempts to check the expression of opinions that we loathe and believe to be fraught with death, unless they so imminently threaten immediate interference with the lawful and pressing purposes of the law that an immediate check is required to save the country." Id., at 630. (Italics added.)

"It is only the present danger of immediate evil or an intent to bring it about that warrants Congress in setting a limit to the expression of opinion where private rights are not concerned. Congress certainly cannot forbid all effort to change the mind of the country." Id., at 628. (Italics added.)
to include a contribution or gift to a domestic corporation, trust, community fund, or foundation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes if no part of the net earnings inures to the benefit of any private shareholder or individual and if no "substantial part" of its activities is the carrying on of propaganda, or otherwise attempting, to influence legislation. Other relevant statutory provisions are set forth in the footnotes.\(^9\)

The foregoing Code provisions\(^9\) furnish the statutory framework for consideration of the questions relating to deductibility of expenditures made to influence legislation either directly or indirectly. It should be noted that the statute does not explicitly require the disallowance of expenditures of this kind. Section 162, the basic provision for the allowance of ordinary and necessary trade or business expenses, does not expressly exclude from this category expenditures made to influence legislation.

The only statutory provisions expressly referring to uses of money to influence legislation are those found in Sections 170(c) and 501(c). It is clear from these provisions that an organization cannot claim an exemption from income tax as charitable, educational, etc., if a substantial part of its activities involves carrying on propaganda, or otherwise attempting, to influence legislation. It is clear also that no tax deduction may be taken by a taxpayer under the authority of Sec. 170(c) for an "educational or charitable" contribution made to such an organization.

On the other hand, the statute, in exempting labor and agricultural organizations\(^11\) and business leagues, chambers of commerce, etc.,\(^12\) from the income tax, does not provide for disallowance of the exemption if any substantial part of the activities of these organizations consists of attempts to influence legislation.\(^13\) Likewise, it is to be noted that the Revenue Code does not expressly allow a deduction for contributions or dues paid by taxpayers to such organizations. The deductibility of dues paid by labor union members and of contributions or dues paid by businessmen and corporations to business leagues and chambers of commerce must depend, therefore, upon their allowance as ordinary and necessary trade or business expenses by Section 162.

\(^9\) \(\S 501(c)\) exempts from income tax various classes of organizations listed therein. Paragraph (3) deals with corporations, funds, and foundations organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual, and "no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office." Paragraph (5) lists labor, agricultural, and horticultural organizations. Paragraph (6) lists business leagues, chambers of commerce, real estate boards, or boards of trade, not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

\(^10\) These provisions substantially re-enact the corresponding provisions found in the 1939 Code.

\(^11\) \(\S 501(c)(5)\).

\(^12\) \(\S 501(c)(6)\).

\(^13\) See note 9 supra.
Standing alone, the Code provisions appear to point to the following conclusions: (1) no organization may claim exemption as a charitable, educational, etc., organization under Section 501(c) if a substantial part of its activities is attempting to influence legislation, and, in turn no deduction may be taken by a taxpayer under the authority of Section 170 for a contribution to such an organization; (2) the exemption of labor and farm organizations, business leagues, and chambers of commerce under Sections 501(c)(5) and (6) is not limited by the qualification that no substantial part of their activities consists of attempts to influence legislation; (3) as a result, the deductibility of expenditures made by taxpayers to influence legislation, whether by direct expenditures or by contributions to business organizations of various types, should be made to depend entirely on the question whether these are ordinary and necessary expenses incurred in carrying on a trade or business.

THE TREASURY REGULATIONS

Under the Regulations prior to those now proposed under the 1954 Code, the Treasury recognized that some donations made by corporations to various types of organizations could qualify as ordinary and necessary trade or business expenses. Section 39.23 (a)-13 of Regulations 118, while stating the rule that corporations could not deduct as trade or business expenses under the authority of Section 23(a)(1) contributions to organizations coming within the classification of charitable organizations, expressly recognized the deductibility of contributions to other organizations “which [bore] a direct relationship to the corporation’s business and are made with a reasonable expectation of a financial return commensurate with the amount of the donation...” This covered the case of contributions and dues paid by corporations to business associations, chambers of commerce, etc.15

However, Section 39.23(q)-1 of Regulations 118, in interpreting the provision under the 1939 Code authorizing deductions for corporate contributions to


15 The substance of the provisions quoted above is carried forward into §1.162-15c of the proposed new regulation under the 1954 Code. The following regulation was proposed by the Treasury on July 10, 1956, and is still receiving active consideration: “Expenditures for lobbying purposes, for the promotion or defeat of legislation, for political purposes, or for the development or exploitation of propaganda (including advertising other than trade advertising) relating to any of the foregoing purposes, are not deductible from gross income. No payment made, either directly or through any organization, for the specific purpose of attempting to promote or defeat legislation shall be deductible. Other payments, not so made and otherwise meeting the requirements of the regulations under §162, when made as dues or contributions to a trade or business organization, may be deductible under some circumstances, even though influencing, or attempting to influence legislation is incidentally involved in the use by such organization of such payments. Thus, the payment of such amounts made as dues or contributions to— (1) A labor, agricultural, or horticultural organization, exempt under §501(c)(5), or (2) A business league, chamber of commerce, real-estate board, or board of trade, exempt under §501(c)(6), for the furtherance of the general purposes and program of such an organization in promoting the common economic interests represented, shall be deductible in full if the activities of such organization which consist of lawfully attempting to promote or defeat legislation are incidental to the organization’s general purposes and program.”
charitable, educational, and similar organizations, contained the blanket provision:

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.

Although this regulation purported to be an interpretation of the section of the 1939 Code authorizing a deduction for charitable contributions, its language is much broader and states that all lobbying expenditures will be disallowed, regardless of the Code section the taxpayer relies upon to justify the deduction.

The history of this provision of the Regulations is traced in the Court's opinion in *Textile Mills Securities Corp. v. Comm'r.* As pointed out in that opinion, the administrative ban on the allowance of lobbying expenditures as deductible expenses for income tax purposes goes back to a Treasury Decision promulgated in 1915. Beginning in 1921 the provision of the regulations disallowing expenditures made for lobbying or to influence legislation appeared as an interpretation of the statutory provision allowing individuals a deduction for charitable contributions. It must be remembered that corporations were not expressly permitted a deduction for charitable contributions until the enactment of the Revenue Act of 1934. The regulations interpreting the section allowing individuals deductions for charitable contributions expressly stated that charitable contributions as such were not deductible by corporations but that contributions and donations which served a real business purpose of the corporation could be deducted as ordinary and necessary expenses. However, the regulations then went on to say that lobbying expenses would be disallowed.

**The Textile Mills Case**

The statutory provisions and the regulations referred to above furnished the setting for the *Textile Mills* case. The corporation in that case had been employed to represent certain German textile interests whose property in this country had been seized during World War I under the provisions of the Trading with the Enemy Act, toward the end of procuring legislation which would permit ultimate recovery of such property. The corporation was to be compensated on a percentage basis if successful. However, it was to bear all the expenses involved in attempting to procure such favorable legislation. In carrying on its campaign and program to secure the desired legislation, the corporation engaged the services of a publicist and two attorneys. It claimed the amounts paid for these services as deductions from gross income for the years 1929 and 1930. These years were governed by the 1928 Revenue Act which, under Section 23(a), permitted deductions for ordinary and necessary expenses of carrying on the taxpayer's trade or business, and, under Section 23(n), authorized individuals to take a deduction for charitable contributions.

16 314 U.S. 326 (1941).
Article 262 of Treasury Regulations 74, promulgated under the 1928 Revenue Act and purporting to be an interpretation of Section 23(n) of that Act, after reciting that charitable contributions by corporations were not deductible but that some donations by corporations might be allowed as trade or business expenses, depending on the benefits flowing directly to the corporation from such donations, continued:

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.

The Commissioner disallowed the deduction claimed by the taxpayer for expenditures made for services rendered in procuring desired legislation on the ground that the money was expended for lobbying purposes. The Commissioner argued that the provision of the Regulations quoted immediately above required their disallowance.

When the case reached the Supreme Court, the chief issues were whether the cited provision of the Treasury Regulation was controlling on the deductibility of these expenses as ordinary and necessary trade or business expenses under Section 23(a) of the 1928 Act and whether, if construed to limit deductibility under Sec. 23(a), the provision was a valid interpretation of the statute. After recounting the history of the provision of the regulations, the Supreme Court stated, respecting the first question, that the regulations did apply as an interpretation of Section 23(a) and that it was frivolous to assert that they did not purport to limit the deductibility of expenses under this section simply because this provision appeared formally to be an interpretation of Section 23(n) rather than 23(a). Turning then to the question whether the regulation as so applied was a valid interpretation of the statute, the Court held that the regulation in question came within the permissive rule-making power in the interpretation of the income tax law. The opinion stated that the words “ordinary and necessary” were sufficiently ambiguous to leave room for an interpretative regulation. Nor was there any indication that the regulation in barring lobbying expenditures as deductible expenses contravened any policy of Congress. On this point the Court pointed out in a footnote that when Congress finally authorized corporations to take deductions for charitable contributions, it expressly provided as a condition of the deduction that the donee corporation not carry on propaganda, or otherwise attempt to influence legislation, as a substantial part of its activities. In support of the Treasury’s classification of lobbying expenses as nondeductible, the Court stated that contracts to spread “such insidious influences” through legislative halls have long been condemned, citing early decisions by the Supreme Court. The Court continued:

Whether the precise arrangement here in question would violate the rule of those cases is not material. The point is that the general policy indicated by those cases need not be disregarded by the rule-making authority in its segregation of non-
deductible expenses. There is no reason why, in the absence of clear Congressional action to the contrary, the rule-making authority cannot employ that general policy in drawing a line between legitimate business expenses and those arising from that family of contracts to which the law has given no sanction. The exclusion of the latter from "ordinary and necessary" expenses certainly does no violence to the statutory language. The general policy being clear it is not for us to say that the line was too strictly drawn.17

Because of the frequency with which the Textile Mills case is cited in later cases coming before the lower federal courts and the United States Tax Court, and in view of the assumption that the case is definitive with respect to all questions pertaining to the deductibility of expenses incurred for the purpose of influencing legislation one way or another, a close look at the Court's analysis and holding is warranted.

In the first place, it is clear that the long history of this provision of the regulations made a considerable impression upon the Court. That a regulation gains considerable force by the passage of time, particularly where Congress in the interim re-enacts the underlying legislation and may be assumed to ratify the interpretations previously given the same language, is a familiar doctrine of administrative law and statutory interpretation.18

Second, the Court, after pointing out that the words "necessary and proper" admit of sufficient ambiguity so as to properly be the subject of administrative interpretation, stated that it was within the permissive range of administrative discretion to establish a classification of nondeductible expenses based on public policy considerations. Here the basic public policy consideration was seen to be established by earlier Supreme Court decisions which had declared that contracts calling for contingent fees in respect to services to be rendered in procuring favorable legislation or favorable decisions by heads of governmental departments were opposed to public policy and hence unenforceable. It is interesting to note that the Court said it was unnecessary to pass on the question whether the particular services paid for by the taxpayer in this case and for which it claimed a deduction came within the rule of the earlier cases holding that contingent fee lobbying contracts were unenforceable. It was sufficient that these cases stated a general judicial policy which in turn justified the general Treasury policy of disallowing lobbying expenses on public policy grounds. It is noteworthy also that neither the Treasury nor the Court cited any federal or state statutes which prohibited either the contract made by the taxpayer in this case with its client or the contract entered into by the taxpayer with the publicist and the two attorneys. Nor was there any indication of any

17 Id., at 338, 339.

federal or state legislation which expressly prohibited or made unlawful the activities carried on by the taxpayer or by the persons employed by it in this connection. Insofar, then, as the Treasury's regulation disallowed lobbying expenses as a trade or business expense on the ground that public policy considerations require stigmatizing the expenditures as illegitimate, it is based on a conception of public policy not formulated by Congress or state legislatures, but developed by the Treasury Department, and left undisturbed by the courts.

The precise holding in the Textile Mills case was that the Treasury, in accordance with its long-standing regulation, could properly deny a deduction for expenses incurred in connection with a contingent fee contract that called for direct lobbying services in the effort to secure favorable legislation. This of course presented the best possible case both for holding the regulation valid and for finding it applicable. The Court did not have before it the question of deductibility of expenses incurred in attempting either to influence legislation indirectly by cultivating a public sentiment in respect to legislation pending before Congress or to educate and inform the public in regard to matters of basic economic policy regardless of whether related to matters of immediate legislative concern. It is apparent that some of the traditional judicial notions directed against lobbying contracts, which furnish the basis of the Treasury Rulings that expenditures pursuant to such contracts are opposed to public policy, have little relevance with respect to expenditures made to cultivate and educate the public and mold public opinion either in regard to pending legislative proposals or to basic considerations germane to the development of legislative policy.

INTERPRETATION OF THE REGULATION AND TEXTILE MILLS DECISION

But while the decision in the Textile Mills case admits of a narrow construction in respect to the particular type of lobbying expense that will be disallowed on public policy grounds, it is clear from subsequent cases decided before the Tax Court and the lower federal courts that these tribunals as well as the Commissioner rely upon the Supreme Court's ruling to sustain that part of the regulation which disallows expenditures for the promotion or defeat of legislation even though it does not involve direct lobbying in the usual and traditional sense. Thus, the Treasury's regulation, as sanctioned by the Textile Mills

19 Attention is called to the holdings in the following cases where the expenditures claimed as deductible expenses were disallowed: Roberts Dairy Co. v. Comm'r, 195 F.2d 948 (C.A.8th, 1952) (here the taxpayer contributed $750 to the National Tax Equality Association, a non-profit organization which studied and disseminated information concerning the disparities in taxes applicable to private for-profit dairies, but not cooperative dairies; the court stated that this organization was organized and primarily operated from its inception for carrying on propaganda, the ultimate objective being a revision in the tax structure); American Hardware & Equipment Co. v. Comm'r, 202 F.2d 126 (C.A.4th, 1953) (contribution to National Tax Equality Association); Mosby Hotel Co. v. Comm'r, 13 T.C.M. 996 (1954) (contribution to the Kansas Hotel Association which in turn contributed to the Kansas Legal Control Council for the purpose of opposing the "bone-dry" laws of the state); Revere Racing Ass'n
case, is construed to require disallowance not only of expenses incurred in direct lobbying activities but also of expenditures incurred by taxpayers (1) to influence the public on pending legislative proposals of vital interest to the taxpayer where the taxpayer's own activities are related directly to this end, (2) to support the work of non-profit organizations that are directly involved in attempts to influence the public in respect to matters of current legislative interest, and (3) to support the work of non-profit organizations engaged in activities concerned with general matters of legislative policy even though not directed at specific pending legislation.

The most striking recent example of the Revenue Service's attitude is its announcement that, even in the absence of any pending legislation, it will not allow private power companies to deduct the cost of institutional advertisements supporting the principle of private enterprise and showing some of the shortcomings of power systems financed by public funds. Commenting on this "censorship by taxation," an editorial in a leading newspaper said:

If arguing for private enterprise is propaganda, then so is arguing for highway safety, church attendance, or even patriotism. Any business concern which concluded that its interest was served by promoting any of these would be entitled to consider the advertising a business expense.

It looks to us as if the IRS had succumbed to the bureaucratic zeal to substitute its judgment for that of corporate management, and has mistaken its will for public policy. We trust the courts will knock this aberration in the head before tax penalties get attached to praising the spirit of Christmas or the Fourth of July.

It is not clear how far the Treasury and the courts will apply the regulation in order to disallow contributions made by corporations to business leagues and associations formed for the purpose of advancing the common interests of their members. If such an organization is formed for educational purposes, contributions may qualify as deductions under Section 170 of the 1954 Code, relating to charitable, educational, and similar contributions and gifts, subject to the percentage limitation and subject to the express statutory condition that no substantial part of the organization's activities is the carrying on of propa-

v. Scanlon, 232 F. 2d 816 (C.A.1st, 1956) (expenditures incurred to persuade voters that dog track license should be renewed; here the renewal of the license had to be submitted to the voters at a popular election every four years and the very existence of the enterprise depended on such renewal); Stover Co. v. Comm'r, 27 T.C. 434 (1956) (the taxpayer, a corporation engaged in the business of selling surgical and hospital supplies and equipment, paid transportation expense for a newspaperman who had been commissioned by the Arkansas Medical Society, which was concerned with socialized medicine legislation, to make a study of socialized medicine in England and upon his return to report his findings to the Society and write articles thereon for publication).


ganda, or otherwise attempting, to influence legislation. Under this section it is clear that the deduction is not denied, assuming that the organization otherwise qualifies as a charitable, scientific, or educational trust, foundation, or organization, even if an incidental part of its activities consists of efforts to influence legislation by propaganda or otherwise. However, the usual business league or association does not come under this category. It serves the common business interests of its members and enjoys a separate tax exemption under Section 501(c)(6) of the 1954 Code. In many cases, these organizations may, as part of the general purpose of serving the interests of their members, engage in some activities designed to influence legislation in one way or another.

So far as an organization's own tax-exempt status is concerned, it is immaterial that it engages in substantial legislative activities, since Section 501(c)(6), unlike Section 501(c)(3) which gives a tax-exempt status to charitable, educational, and similar organizations, does not condition exemption of business leagues and like groups on abstinence from activities designed to influence legislation. But the fact that the organization is itself tax-exempt does not automatically authorize a tax deduction for contributions or dues or other assessments paid by members. These expenditures, in order to be taken as tax deductions, must qualify as ordinary and necessary business expenses under Section 162 of the 1954 Code, and ordinarily there is no difficulty in establishing this to be the case. But here again the Treasury's regulation enters into the picture, and the deduction may be denied if attempts to influence legislation are a substantial part of the organization's activities, since the organization is deemed to be acting vicariously on behalf of its members. If activity of this kind is only a minor or incidental part of the organization's whole program, the expense deduction is not likely to be denied to contributing members. Thus, in Smith-Bridgman & Co. v. Commissioner,22 the Tax Court held that contributions made by the taxpayer to the Chamber of Commerce of Flint, Michigan, and to the Chamber of Commerce of the United States were deductible as ordinary and necessary trade or business expenses. Likewise dues paid by the taxpayer to the National Association of Manufacturers were held deductible in Addressograph-Multigraph Corporation v. Comm'r.23 On the other hand, if the league's major activity or if a substantial part of its activities are directed to the promotion or defeat of legislation, the members' contributions will be disallowed as trade or business expenses.24 Conceivably, of course, a part of the contribution might be disallowed depending on the extent to which the organization engages in legislative activities although no case has yet arisen involving a pro rata disallowance.

22 16 T.C. 287 (1951).
23 4 T.C.M. 147 (1945).
24 See, e.g., the holding and opinion in American Hardware & Equipment Co. v. Comm'r, 202 F.2d 126 (C.A.4th, 1953), disallowing contributions to the National Tax Equality Association.
NEED FOR RE-EXAMINATION OF THE QUESTION

The uncertainties raised by the present regulation, particularly in its application to contributions made by corporations to business leagues, industry-wide committees, etc., indicate the need for clarification of the law in regard to this problem. And, apart from clarification, the time seems to be ripe for a complete reconsideration of the issues here involved. The basic rationale of the Treasury regulation disallowing expenses incurred in connection with legislative activities needs to be re-examined. It must be remembered that Congress has never expressly disallowed such expenditures as trade or business expenses. A number of considerations may be adduced to support the view that this whole question needs re-examination.

In the first place, the Treasury's regulation, based on the idea that lobbying contracts and service were opposed to public policy, had its roots in types of lobbying activities that could well be described as reprehensible and insidious. Indeed, because of the evils associated with direct lobbying activities and the pressures and temptations to which Congressmen were subjected, lobbying in general was looked upon as an evil activity. But it is now recognized that lobbyists have much to contribute to the legislative process, that lobbying in itself is not an illegal activity, and that to engage in such activity is not to violate some implied conception of public policy. Moreover, in view of the nature of our democratic process, the efforts on the part of citizens to influence legislation which may be of vital interest to them, whether by direct communication with members of Congress or by educational programs directed to the public and designed to create a favorable climate of opinion in regard to legislative matters, represent a legitimate exercise of freedoms guaranteed by the First Amendment.

The opinions in United States v. Harriss,25 United States v. Rumely,26 and United States v. Congress of Industrial Organizations,27 all bear witness to the high regard that the Supreme Court entertains for the First Amendment freedoms and the caution it exercises in dealing with legislation that touches upon these freedoms. In the Harriss case, the Court, out of deference to constitutional limitations, gave the Federal Regulation of Lobbying Act a restricted interpretation so as to make its provisions apply only in respect to expenditures made for the principal purpose of direct communication with Congress. In the Rumely case the Court, again out of deference to constitutional limitations, found that a Congressional committee had no authority to require a publisher who distributed literature dealing with political matters to disclose the names of his customers. And in the C.I.O. case the Court substantially revised the provision of the Corrupt Practices Act, as amended by the Taft-Hartley

26 345 U.S. 41 (1953).
Act, so as to make these provisions inapplicable to expenditures by labor unions in endorsing political candidates by means of their house organs. The separate opinions in these cases are particularly noteworthy because of the forceful expressions in support of the right of individuals and organizations to engage in activities designed to influence legislative policy. In the face of these expressions of opinion it is anomalous to suggest that activities intended to influence legislation, all protected under the First Amendment, are opposed to public policy. On the contrary, it should hardly be a debatable proposition that the assertion of constitutional liberties is always in the public interest and consistent with public policy, however and by whomever defined.

Second, in 1946, five years after the *Textile Mills* decision, Congress passed the Federal Regulation of Lobbying Act.\(^2\) This statute was given a restricted application in the *Harris* case, as pointed out above, and, as so interpreted, was held constitutional. As interpreted by the Court, the statute validly applies to require registration of professional lobbyists and also to require disclosure of expenditures made for the principal purpose of direct communication to Congressmen. This legislation has very important implications with respect to the “public policy” involved in spending money to support legislative activities. It is axiomatic that any administrative or judicial conception of public policy should yield in the face of the policy determination by Congress. Congress in the Regulation of Lobbying Act did not declare a policy of invalidating lobbying activities. All persons who come within the provisions of the Act and comply with its provisions in respect to registration and periodic reports are, by hypothesis, engaged in lawful activities as recognized by Congress. Again, to suggest that activities lawful under federal legislation must be deemed in opposition to public policy for tax purposes is to state an incongruous proposition. Moreover, out of deference to constitutional limitations, the Court in the *Harris* case did not interpret the Act to apply to expenditures made for so-called indirect lobbying, i.e., to activities designed to influence public opinion on matters of legislative policy. Here too, it is a contradiction in terms to suggest that indirect lobbying activities must be branded as illegitimate for tax purposes.

Third, the clear trend of judicial opinion in recent years has been to condemn the Treasury's efforts to disallow trade or business expenses by reference to the Treasury's conception of proper public policy. In *Commissioner v. Heininger*\(^3\) the Court held that the Commissioner erred in denying a taxpayer a deduction for legal fees incurred in resisting a Post Office Department fraud order which threatened the very existence of the taxpayer's business. The Commissioner had defended his action on the ground that these expenditures were opposed to public policy. In overruling this contention the Court stated

- \(^3\) 320 U.S. 467 (1943).
that these expenses, if otherwise ordinary and necessary expenses of the trade or business, should not be disallowed unless they related to activities which violated some specifically declared state or federal policy. Moreover, the Court stated that the taxpayer in employing counsel to resist the Post Office's order was exercising a legal right and this could not be said to violate any recognized conception of public policy.

Even more striking was the decision in *Lilly v. Comm'r*, where the Court again overruled the Commissioner and held that taxpayers, engaged in the retail optical business, could properly deduct as a trade or business expense the amounts paid to physicians as kickbacks out of the prices of glasses sold by them. The Court stated that even though it could not condone the ethics of this practice, and even though several states had subsequently passed laws outlawing the practice, it found no basis on the ground of public policy for denying the tax deduction. The Court stated that to warrant disallowance on ground of public policy, "[t]he policies frustrated must be national or state policies evidenced by some governmental declaration of them." Significantly, the Court referred to its prior decision in the *Textile Mills* case with respect to lobbying expenses in the following language:

> In *Textile Mills Corp. v. Commissioner* ... this Court accepted an interpretation of that section by a Treasury Regulation which disallowed the deduction of certain expenditures for lobbying purposes. In doing so, the Court referred to the fact that some types of lobbying expenditures have long been condemned by it, and that the interpretative regulation had itself been in effect many years with congressional acquiescence. The instant case does not come within that precedent. (Italics added.)

The guarded and defensive language used by the Court to explain the *Textile Mills* case, although indicating that the Court continues to accept the authority of that decision, nevertheless indicates that the Court looks upon that case as presenting an exceptional situation arising from the fact that the regulation had been in force for many years and the further fact that "some types" of lobbying activities had previously been condemned by the Court. But it is clear that, as an original proposition, the regulation denying deduction for lobbying expenses on the ground of public policy cannot survive the rule stated in the *Heiningier* and *Lilly* cases, namely, that conceptions of public policy may not be used by the Commissioner to disallow expenditures otherwise recognized as proper trade and business expenses unless the expenditures violate state or national policies evidenced by some governmental declaration of them. Of the utmost importance here is the fact that five years after the *Textile Mills* case, Congress actually gave its blessing to legislative activities in the Federal Regulation of Lobbying Act. There is, in fact, now a Congressional declaration that legislative expenses are not contrary to public policy.

30 343 U.S. 90 (1952).
31 Id., at 97.
32 Id., at 95.
The Supreme Court's present reluctance to find any "governmental declaration" that expenditures contravene public policy is exemplified by the recent decision *Commissioner v. Sullivan*.\(^3\) The taxpayers ran a bookmaking establishment in Chicago, which was illegal under Illinois law. The Tax Court refused deductions for amounts paid for wages and for rent, since the acts performed by the employees constituted violations of state law and the payment of rent for the use of the premises for illegal purposes also violated that law. The Supreme Court, however, allowed the deductions, repeating its statement in the *Heininger* case that the fact that an expenditure bears a remote relationship to an illegal act does not render it non-deductible. Since the Treasury Regulations allowed the federal excise tax on wagers to be deducted, this was construed by the Supreme Court as recognition of a gambling enterprise as a business for federal tax purposes. The Court also commented that if the Internal Revenue Code was to be distorted in such cases into a gross receipts tax by the disallowance of deductions, that federal policy should be announced by Congress, and not by the Commissioner.

As an illustration of expenditures that do frustrate a clearly stated legislative policy, one may point to political contributions by corporations.\(^4\) Since the *Corrupt Practices Act*\(^5\) prohibits such contributions by corporations, it would clearly be contrary to public policy to permit a tax deduction for expenditures of this kind. There can be no quarrel with the provision of the Regulations disallowing deductions for these expenditures. But spending money to influence legislation by appeal to argument, facts, reason, and the educational process generally is not barred by legislation. Moreover, any such prohibition would be invalid under the First Amendment.

Finally, in view of the broad and active role now assumed by the government in regard to the regulation of the nation's economic affairs and in light of the impact of governmental policy upon business interests, corporations have a very vital interest in matters of legislative policy and in the shaping of public opinion for the purpose of creating a favorable climate of thought in regard to basic economic policies. Since it has become a common matter for corporations to engage in various types of activities and programs designed to influence legislation, whether directly or indirectly, since these activities are seen to

\(^3\) *356 U.S. 27* (1958).

\(^4\) See also *Tank Truck Rentals v. Comm'r*, *356 U.S. 30* (1958) and *Hoover Motor Express Co. v. United States*, *356 U.S. 38* (1958), companion cases to *Commissioner v. Sullivan*, *356 U.S. 27* (1958). In both cases deductions for fines imposed for violating state truck weight laws were disallowed.

be appropriate as a means of furthering the enterprise's corporate purpose, and since expenditures for these purposes can be expected to yield results advantageous to the continued operation of the business, there should be no difficulty in characterizing expenditures for these purposes as ordinary and necessary business expenses. Indeed, the decisions disallowing expenditures of this kind because of the Treasury's regulation which is premised on public policy considerations have not rejected the basic proposition that these expenditures are ordinary and necessary business expenses. Thus, in *Bellingrath v. Comm'r*, where the Board of Tax Appeals disallowed a taxpayer's payments to a trade association for the purpose of presenting arguments in opposition to proposed legislation, the Board recognized that these legislative activities were normal and proper but felt obliged to disallow them on the basis of the *Textile Mills* case. And in a series of earlier decisions antedating the *Textile Mills* case, the Board of Tax Appeals had upheld the deductibility, under the ordinary and necessary business expense category, of expenditures incurred in efforts to influence public opinion and legislative policy.

Unfortunately, the emphasis upon the public policy argument, as reflected in the Treasury’s regulation, as a basis for disallowance has obscured the central question of whether these expenditures should not be allowed as ordinary expenses of the business. Certainly it is no less appropriate for a company to spend money to help defeat legislative proposals that may seriously threaten the company's continued operations than to spend money for legal fees incident to protecting the company's legal interests before courts and administrative tribunals. In the *Heininger* case the Court in allowing as expenses for tax purposes the attorney's fees paid by the taxpayer in resisting the Post Office Department's fraud order, emphasized that the taxpayer's very business existence was at stake. This same line of reasoning may properly be invoked to justify expenditures made to influence the determination of legislative policy. This principle has been recognized by the English Court of Appeal in *Morgan v. Tate & Lyle, Limited*, a case worthy of note and emphasis.

The taxpayer was an English company engaged in the sugar refining business. In view of the nationalization program then being followed by the English government, the company, having serious reason to believe that efforts would be made to nationalize the sugar refining industry, made a considerable expenditure in conducting an anti-nationalization campaign, including expenditures for advertising, film-making, film showing, the issue of pamphlets, photographs and recordings. The question presented was whether these expenditures were deductible. This issue was controlled by the following section of the English income tax law:

*46 B.T.A. 89 (1942).*

*37* See *Los Angeles & Salt Lake R.R. v. Comm'r*, 18 B.T.A. 168 (1929), and the cases reviewed therein.

In computing the amount of the profits or gains to be charged, no sum shall be deducted in respect of—(a) any disbursements or expenses, not being money wholly and exclusively laid out or expended for the purposes of the trade.... (Italics added.)

It will be noted that in order to justify a deduction under this section it must be shown that the money was wholly and exclusively laid out or expended for the purposes of the trade. While stated in different words, it corresponds exactly to the deduction authorized under American law for ordinary and necessary business expenses. The Court of Appeal held that the expenditures here incurred in carrying on the anti-nationalization campaign were wholly and exclusively expended for the purposes of the trade. The chief opinion emphasized that there was evidence to support the finding that the directors of the company had reason to apprehend a threatened nationalization of their company and that it was therefore appropriate for the company to carry on the anti-nationalization campaign as a means of protecting the company's business and assets and assuring its continued operation and earning of profits. There is no intimation in the Court's opinion of the notion that the company in engaging in this kind of activity for the purpose of influencing public opinion and legislation was violating some implied conception of public policy. On the contrary, the English court, as did the District Court in the *Cammarano* case, recognized that under the circumstances this was the proper thing for the company to do.

The considerations briefly outlined above support the conclusion that the time is ripe for a reconsideration of the basic assumption underlying the Treasury's regulation disallowing expenditures made for lobbying purposes or to influence legislation. The recognition in our day that lobbying and other attempts to influence legislation are not only not reprehensible but on the contrary represent an exercise of important constitutional privileges, the enactment by Congress of the Regulation of Lobbying Act and the policy implicit in the Act of recognizing lobbying as a legitimate activity, the repudiation by the Supreme Court in recent years of a power in the Treasury or the courts to disallow expenses on grounds of public policy not articulated by legislative bodies, and the common realization that spending to influence legislative policy is necessary and proper in carrying on a business, all point persuasively to the conclusion that the position taken in the Regulations is an anachronistic carry-over from a day when lobbying and attempts to influence legislation were regarded in an entirely different light.

**CONCLUSION**

The most direct approach in any attempt to correct the situation resulting from the Treasury's position is to persuade Congress to amend the Internal Revenue Code to provide that an expenditure, otherwise deductible as an or-

39 Id., at 167.
ordinary and necessary trade expense under Section 162 of the 1954 Code, shall not be disallowed on the ground that the purpose of the expenditure is to promote or defeat legislation. This appears to be the best form that any remedial legislation could take. Under the Code as so amended it would not follow that a taxpayer could automatically deduct all expenditures made to influence legislation. It would still be necessary to demonstrate that the expenditures were ordinary and necessary for the purpose of the trade or business. Moreover, the implied limitation that expenses be "reasonable" as well as ordinary and necessary would furnish a further vehicle for limiting expenditures of this kind that appeared to be grossly excessive. Or, if Congress were apprehensive that taxpayers would unduly exploit this type of expenditure if it became a deductible expense, Congress might establish a percentage limitation to limit the deduction as it has done in the case of charitable contributions.

The need for relief through new legislation may be eliminated by the Supreme Court itself. It has granted certiorari in the Cammarano case and in the similar Strauss$^{40}$ case arising in the Eighth Circuit. This will be the first time the Supreme Court will have spoken on the subject since 1941. It may be hoped that the Court's reason for granting certiorari is to reverse Textile Mills. At the very least, the Court ought to be able to eradicate the inequities which have resulted from the unanimous and blind acceptance of that decision in situations where it is not at all applicable. There surely is no justification for administering the tax laws so as to allow deductions to persons unsuccessfully resisting post office fraud orders, paying kickbacks to referring physicians or operating bookmaking houses, and yet denying deductions to a conscientious businessman who, in order to preserve his business, exercises his right of free speech in a way that aids the public or members of Congress in making up their minds on matters which could be the subject of legislative action.