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Revenue Ruling 72-314

Amounts paid by a stock brokerage corporation to a charitable organization described in section 170 (c) (2) of the Code are deductible as a business expense under section 162 (a) since the payments are business related and could commensurately further its business.

Advice has been requested whether, under the circumstances described below, amounts paid to a charitable organization described in section 170 (c) (2) of the Internal Revenue Code of 1954 are deductible under section 162 (a) of the Code as an ordinary and necessary business expense.

The taxpayer corporation is engaged in a stock brokerage business. In order to promote business in the particular neighborhood in which its office is located, and in order to compete successfully with other brokerage firms located in more established financial neighborhoods of the city, the taxpayer, as an inducement to its customers, paid an amount equal to 6 percent of all brokerage commissions received by it to a charitable organization described in section 170 (c) (2) of the Code whose purpose was to reduce neighborhood tensions and combat community deterioration in the neighborhood in which the taxpayer's office was located.

The taxpayer emphasized in its advertisements to its customers and potential customers that the described payments made by it to the charitable organization would enable the customers to benefit the organization and, thus, the community, without incurring additional expenses. The taxpayer advised the organization of the procedure used in soliciting business and that it would pay the organization the amount mentioned above for the privilege of being able to advertise that such procedure was in effect. The charitable organization agreed to this procedure. It was the reasonable expectation of the taxpayer that the outlined procedure of payments to the described organization would direct new business to the taxpayer as well as retain the business of its existing customers.

Section 170 of the Code provides, in effect, that there shall be allowed as a deduction any contribution or gift to, or for the use of, an organization described in subsection (c), payment of which is made within the taxable year.

Section 170 (b) (2) of the Code provides that in the case of a corporation the total deduction under subsection 170 (a) of the Code for any taxable year shall not exceed 5 percent of the taxpayer's taxable income computed without regard to certain deductions.

Section 162 (a) of the Code provides that all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business shall be allowed as a deduction.

Section 162 (b) of the Code provides that no deduction shall be allowed under subsection (a) for any contribution or gift which would be allowed as a deduction under section 170 of the Code were it not for the limitations set forth in such section.

Section 1.162-15 (a) (2) of the Income Tax Regulations states that the limitation provided in section 162 (b) applies only to payments which are, in fact, contributions or gifts to organizations described in section 170 of the Code. See also Revenue Ruling 63-73, C.B. 1963-1, 35.

Whether payments of the nature described in the instant case are "contributions or gifts," within the meaning of section 170 of the Code, or are deductible as ordinary and necessary business expenses under section 162 of the Code depends upon whether such payments are completely gratuitous or whether they bear a direct relationship to the taxpayer's business and are made with a reasonable expectation of a financial return commensurate with the amount of the payment. See section 1.162-15 (b) of the regulations.

In the instant case, since the payments in question are related to the taxpayer's business and could reasonably be expected to commensurately further such business financially, such payments are deductible as ordinary and necessary business expenses under section 162 (a) of the Code.