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Revenue Ruling 73-113

Voluntary contributions to a city's special oil pollution control fund used for research, beautification, and advertising to recover tourist business lost due to oil pollution are deductible as ordinary and necessary business expenses by a corporation conducting a retail business in the city; Revenue Ruling 69-90 distinguished.

Advice has been requested whether payments to a special fund, under the circumstances described below, are deductible as ordinary and necessary business expenses.

The taxpayer is a corporation engaged in a retail business in a resort city, and derives a significant portion of its income from the tourist industry in that city. In 1969, an oil well blow-out occurred in the vicinity of the city's coast line, causing crude oil to pollute the channel waters and beaches. Even though the beaches were cleaned after the blow-out, the shifting of winds and tides periodically caused large quantities of crude oil to wash ashore and blacken the area's beaches.

The widespread publicity concerning the continuing pollution had a significant adverse effect on the city's business community and its tourist industry, and the taxpayer in particular suffered a considerable loss of business as a result of the oil blow-out. In addition, the pollution resulted in heavy loss of wildlife and damage to the beaches and other real and personal property. The steady upward trend in the city's tourist traffic was reversed in 1969, while other coastal communities continued to enjoy increasing traffic.

To reverse the detrimental effects described above, the City Council adopted a resolution which established a special fund for the protection of local business through an oil pollution control fund. The resolution limited expenditures of money from the fund to uses which were exclusively for the economic benefit of local trade and commerce and prohibited the use of the fund's money for lobbying efforts to influence public opinion with regard to legislation through advertising or otherwise, or any other political activity which seeks to influence legislation.

Amounts paid to the fund may be used for, but are not limited to, the following purposes:

(a) nonpartisan scientific research on the subject of oil pollution and publication of the results thereof,

(b)

physical preservation of the city's natural beauty of its coastline and beaches, and

(c) advertising to counteract damaging publicity which threatened and continues to threaten the business community.

The taxpayer voluntarily paid an amount of money that was deposited in the fund administered by the city, and the amount thereof was commensurate with the financial return expected to be derived by the taxpayer. The specific question presented is whether the taxpayer may deduct the amount paid as an ordinary and necessary business expense.

Section 162 (a) of the Internal Revenue Code of 1954 allows a deduction for all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business.

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

Section 1.162-15 (a) (1) of the Income Tax Regulations provides, in part, that no deduction is allowable under section 162 (a) of the Code for a contribution or gift by an individual or corporation if any part thereof is deductible under section 170.

Section 1.162-15 (a) (2) of the regulations provides, in part, that the limitation in section 1.162-15 (a) (1) of the regulations and the limitation in section 162 (b) of the Code apply only to payments which are in fact contributions or gifts to organizations described in section 170.

Section 1.162-15 (b) of the regulations provides that donations to organizations other than those described in section 170 of the Code, which bear a direct relationship to the taxpayer's business and are made with the reasonable expectation of a financial return commensurate with the amount of the donation, may constitute allowable deductions as business expenses.

Section 170 of the Code provides for the deductibility of charitable contributions as defined in subsection (c), payment of which is made within the taxable year. A charitable contribution is defined, in part, in section 170 (c) (1) of the Code as meaning a contribution or gift to or for the use of a State or one of its political subdivisions, but only if the contribution is for an exclusively public purpose.

Sections 1.170-1 (c) (1) and 1.170A-1 (c) (5) of the regulations provide that transfers of property to an organization described in section 170 (c) of the Code which bear a direct relationship to the taxpayer's business and which are made with a reasonable expectation of financial return commensurate with the amount of the transfer may constitute allowable deductions as trade or business expenses rather than as charitable contributions.

Thus, where a taxpayer engaged in trade or business makes a transfer of property with a reasonable expectation of financial return to himself in his trade or business, commensurate with

the amount of the transfer, no deduction under section 170 of the Code is allowable with respect to such transfer and the transfer may constitute an ordinary and necessary business expense under section 162 of the Code. Conversely, where a taxpayer engaged in trade or business makes a voluntary contribution of property without a reasonable expectation of a financial return to him in his trade or business, the deductibility of the transfer is to be determined under section 170 of the Code and no deduction under section 162 of the Code will be allowable with respect to such transfer. These principles are applicable irrespective of whether the recipient of the payments is an organization described in section 170 of the Code.

Whether a particular transfer was made with a reasonable expectation of a financial return, commensurate with the amount of the transfer, is a question of fact. In the circumstances described above, the taxpayer had suffered a considerable loss of business as a result of the oil blow-out. The payment made by the taxpayer to the fund was reasonably calculated to improve the taxpayer's future business and was commensurate with the financial return expected to be derived by the taxpayer.

Accordingly, the taxpayer's payments to the special fund are deductible as ordinary and necessary business expenses of carrying on his trade or business under section 162 (a) of the Code.

Revenue Ruling 69-90, 1969-1 C.B. 63, concerning a situation where merchants and property owners voluntarily contributed money to enable the local government to acquire public parking facilities is distinguishable. In that Revenue Ruling, the taxpayers could not reasonably expect a financial return commensurate with the amount of payments, since the amount of the payments was not based on the proximity of the facilities to the taxpayer's property, nor on the probable use of the facilities by the taxpayers, their tenants, or customers.